VOLKSWAGEN FINANCIAL SERVICES

THE KEY TO MOBILITY

ANNUAL REPORT (IFRS) OF VOLKSWAGEN BANK GMBH

2016

Volkswagen Bank GmbH Group

Key Figures (IFRS)

in € million (as of December 31)	2016	2015	2014	2013	2012
Total assets	56,334	49,206	42,947	39,378	39,220
Loans and receivables attributable to					
Retail financing	24,940	23,312	21,779	20,431	19,557
Dealer financing	10,538	10,302	8,928	7,973	7,738
Leasing business	3,014	2,502	2,108	1,789	1,540
Customer deposits	35,666	27,877	25,252	23,140	23,722
Equity	7,156	5,030	4,864	4,699	5,021
Operating profit	645	539	446	455	448
Profit before tax	669	575	464	459	558
Income tax expense	–186	–157	–153	–151	–127
Profit after tax	482	418	310	308	431

in % (as of December 31)	2016	2015	2014	2013	2012
Equity ratio	12.7	10.2	11.3	11.9	12.8
Common Equity Tier 1 capital ratio[1]	14.3	11.1	13.2	–	–
Tier 1 capital ratio[1]	14.3	11.1	13.2	14.0	13.5
Total capital ratio[1]	14.4	11.2	13.4	14.7	14.9

Number (as of December 31)	2016	2015	2014	2013	2012
Employees[2]	1,293	1,185	1,123	1,241	1,174

RATING (AS OF DECEMBER 31)	STANDARD & POOR'S			MOODY'S INVESTORS SERVICE		
	Commercial paper	Senior unsecured	Outlook	Commercial paper	Senior unsecured	Outlook
Volkswagen Bank GmbH	A–2	A–	Watch negative	P–1	Aa3	negative
Volkswagen Financial Services AG	A–2	BBB+	Watch negative	P–1	A2	negative

1 The regulatory capital ratios for the years 2012 and 2013 were calculated in accordance with the Solvabilitätsverordnung (SolvV – German Solvency Regulation). Since January 1, 2014, these ratios have been calculated in accordance with article 92 of the Capital Requirements Regulation (CRR). The Common Equity Tier 1 capital ratio has been added in accordance with the requirements in the CRR and other terminology has been aligned with that in the CRR.

2 Since 2012 including Volkswagen Bank Polska S.A., Warsaw

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Fundamental Information about the Group

Continuous international growth demonstrates the validity of the Volkswagen Bank GmbH Group's business model

BUSINESS MODEL

Within the Financial Services division of the Volkswagen Group as a whole, Volkswagen Bank GmbH is responsible for the operating activities relating to the provision of banking transactions for retail and business customers. The individual activities include those described below.

Financing

The Volkswagen Bank GmbH Group provides finance for retail customers, business customers and authorized dealers. The principal activity is the financing of vehicles.

Leasing

At the branches of the Bank in Italy and Portugal, the Volkswagen Bank GmbH Group operates finance lease business. The branch in France is also involved in operating lease business in addition to finance lease activities.

Direct banking

The Volkswagen Bank GmbH Group offers retail customers the entire range of direct banking services, including account management, consumer finance, savings plans and investment products. The facilities provided for business customers by the Volkswagen Bank GmbH Group include instant-access accounts, fixed-term deposits and saving certificates as well as a comprehensive range of payment services.

Broking

The Volkswagen Bank GmbH Group acts as an insurance broker in connection with the financing of vehicles. As part of its direct banking operations, it arranges loans secured by charges entered in the land register and other long-term forms of financing; it is also an intermediary for stock market or fund investments.

One of the ways in which the Volkswagen Bank GmbH Group pursues its objectives is to carry out joint customer relationship management activities with other companies in the Financial Services division of the Volkswagen Group and this has led to continuous improvement in customer loyalty, service quality and the range of products offered.

The business operations of the Volkswagen Bank GmbH Group are tightly integrated with those of the manufacturers and the dealer organizations in the Volkswagen Group.

ORGANIZATION OF THE VOLKSWAGEN BANK GMBH GROUP

Generally speaking, the aim of all structural measures in the Volkswagen Bank GmbH Group is to improve the quality offered to both customers and dealers, make processes more efficient and leverage synergies. The motivation and satisfaction of employees are key factors that enable us to defend our position as a leading employer of choice.

With a view to setting up a comprehensive, sustainable process management structure, this area of activity has been brought together as a single area of responsibility under the remit of Torsten Zibell. This structure will ensure optimum collaboration between the process management units responsible for the retail, corporate, fleet and direct banking customer groups. Mr. Zibell is also responsible for direct banking sales and customer service as well as market development and internal services.

The Retail Customers & Corporate Customers group headed by Anthony Bandmann had set up its internal customer service along regional lines with north, west, south and east regions in a structure similar to field sales. In 2016, this structure was narrowed down to three regions to optimize the holistic advisory services provided for the customer. Marketing and sales controlling have been added to the sales function in this case to consolidate the approach still further. The processes for acquiring financing contracts and, as a service for Volkswagen Leasing GmbH, for acquiring leases have been amalgamated. Consistent integration between the front office and back office for each region forms the basis for

activities in the corporate customer segment. Anthony Bandmann also took over responsibility for brand management and marketing from Volkswagen Leasing GmbH from April 1, 2016. From February 1, 2016, responsibility for Human Resources was also transferred from Dr. Heidrun Zirfas to Anthony Bandmann.

Credit approval processes in Bank back-office activities and special customer care are brought together under the Back Office to ensure that processes are completed quickly and a high degree of customer satisfaction is achieved. Harald Heßke was appointed as a member of the Management of Volkswagen Bank GmbH on February 1, 2016 and he has taken over responsibility for this area from Dr. Heidrun Zirfas. Responsibility for Legal Affairs, Internal Audit, Compliance, Finance and Risk Management in the German market was also transferred from Dr. Zirfas to Mr. Heßke from February 1, 2016.

Responsibility for Europe (excluding Germany), which has been taken over by Jens Legenbauer, was expanded from September 1, 2016. Mr. Legenbauer thus now has responsibility for the management of the European branches of Volkswagen Bank GmbH.

In 2016, Volkswagen Financial Services AG initiated a reorganization of its structures under company law, encompassing all legal entities. The aim of the restructuring is to segregate the entire European lending and deposits business from the other financial services activities going forward and to pool this business under Volkswagen Bank GmbH, structured in the future as a direct subsidiary of Volkswagen AG. From 2017, detailed plans will be drawn up for the restructuring and preparations will be carried out for its implementation in terms of any necessary changes to organizational structures. The reorganization aims to improve transparency, enhance efficiency and increase flexibility. The structure and the organization of Volkswagen Bank GmbH satisfy the requirements of the Mindestanforderungen an das Risikomanagement (MaRisk – German Minimum Requirements for Risk Management in Banks and Financial Services Institutions).

REPORT ON THE SUBSIDIARIES AND BRANCHES

On April 11, 2016, MAN Financial Services S.p.A., Dossobuono di Villafranca (VR), Italy, – a subsidiary at that time – was merged into Volkswagen Bank GmbH, effective retroactively from January 1, 2016. Volkswagen Bank GmbH acquired MAN Financial Services S.A.S., Evry Cedex, France on April 1, 2016 from MAN Finance International, Munich. The acquired company was merged into Volkswagen Bank GmbH on July 28, 2016, effective retroactively from January 1, 2016. In Poland, the Volkswagen Bank GmbH Group is represented by its subsidiary Volkswagen Bank Polska S.A., Warsaw. In turn, this company has a 100% shareholding in Volkswagen Serwis Ubezpieczeniowy Sp.z.o.o., Warsaw, which is not consolidated because it is of minor significance.

The brand-related branches of the Volkswagen Bank GmbH Group (Audi Bank, SEAT Bank, ŠKODA Bank, AutoEuropa Bank and ADAC FinanzService) are intended to provide specific support for the financing of the corresponding vehicles. The Ducati Bank Branch supports the financing of motorcycles.

In Berlin, Braunschweig, Emden, Hanover, Ingolstadt, Kassel, Neckarsulm, Salzgitter, Wolfsburg and Zwickau, the Volkswagen Bank GmbH Group maintains branches offering customers counter services, advisory support and, in some cases, ATMs.

At the end of fiscal year 2016, the Volkswagen Bank GmbH Group had a presence in the European market outside Germany with branches in eight different countries of the European Union set up using the EEA “passport” for financial services institutions. Each of the Volkswagen Bank GmbH Group’s international branches in France, Greece, the United Kingdom, Ireland, Italy, the Netherlands, Portugal and Spain has its own employees and services the business in the country concerned. The branches had 955 (previous year: 853) employees as of December 31, 2016.

INTERNAL MANAGEMENT

The key performance indicators used by the Group are determined on the basis of IFRS and are presented as part of the internal reporting system. The most important non-financial performance indicators are penetration, current contracts and new contracts. The financial key performance indicators are the volume of business, deposit volume and operating profit. Return on equity (RoE) and the cost/income ratio (CIR) are used as further key performance indicators, but at the level of the Volkswagen Financial Services AG Group, of which the Volkswagen Bank GmbH Group forms part.

	Definition
Nonfinancial performance indicators	
Penetration	Amount of new contracts for new Group vehicles under retail financing and leasing business to deliveries of Group vehicles, based on Volkswagen Bank GmbH's consolidated entities.
Current contracts	Contracts recognized as of the reporting date
New contracts	Contracts recognized for the first time in the reporting period
Financial performance indicators	
Volume of business	Loans to and receivables from customers arising from retail financing, dealer financing, leasing business and direct banking
Volume of deposits	Customer deposits, i.e. total liabilities from deposits arising from direct banking business, dealer current account and from nondirect banking business
Operating profit	Net income from lending and leasing transactions after provision for credit risks, plus net fee and commission income, less general and administrative expenses, plus other operating income and less other operating expenses. Some amounts under net interest income, net other operating expenses/income and general and administrative expenses are eliminated (see also Segment Reporting).

CHANGES IN EQUITY INVESTMENTS

On April 11, 2016, MAN Financial Services S.p.A., Dossobuono di Villafranca (VR), Italy, – a subsidiary at that time – was merged into Volkswagen Bank GmbH, effective retroactively from January 1, 2016.

Volkswagen Bank GmbH acquired MAN Financial Services S.A.S., Evry Cedex, France on April 1, 2016 from MAN Finance International GmbH, Munich. The acquired company was merged into Volkswagen Bank GmbH on July 28, 2016, effective retroactively from January 1, 2016.

On June 21, 2016, Volkswagen Bank GmbH sold its holding in VISA Europe Limited, London.

Report on Economic Position

The pace of global economic growth was slightly slower in 2016 than in the previous year. In contrast, the global demand for cars was higher than in the year before. Profit before tax generated by the Volkswagen Bank GmbH Group increased year-on-year.

GLOBAL ECONOMY GROWS MODERATELY

The moderate growth rate of the global economy slowed to 2.5% (previous year: 2.8%) in fiscal year 2016. While economic momentum decelerated in the industrialized countries as a whole, growth rates in emerging economies remained virtually constant year-on-year. Inflation increased as a result of the expansionary monetary policies pursued by many central banks and due to rising energy and commodity prices.

Europe

The economy of Western Europe continued to recover in the reporting period. At 1.7% (previous year: 2.0%), growth in gross domestic product (GDP) was slightly lower than in the previous year. The picture was mixed as regards economic growth in both Northern and Southern Europe. The UK's Brexit referendum in June, when a small majority voted to leave the EU, had a dramatic effect, with direct consequences including uncertainty in the financial markets and dimmer economic prospects for the United Kingdom and Europe as a whole. The eurozone unemployment rate continued to decrease, falling to an average of 10.6% (previous year: 11.3%), though rates remained considerably higher in Greece and Spain.

Germany

The German economy continued to profit from positive consumer sentiment and a good labor market, with the 1.8% (previous year: 1.5%) rise in GDP being somewhat stronger than in the previous year.

FINANCIAL MARKETS

In 2016, global financial markets were characterized by some degree of uncertainty and the environment continued to be dominated by the expansionary monetary policies pursued by international central banks. The main sources of uncertainty included recurring doubts about economic growth in key industrialized nations, the United Kingdom's membership of the European Union (EU), geopolitical conflicts, political developments and the unexpected instability in the price of oil. The European Central Bank (ECB) maintained its expansionary monetary policy to achieve its inflation targets; in March, it cut its key interest rate to 0.0 % and increased its negative interest rate for bank deposits at the ECB to –0.4%. This reduced rates of return to negligible levels and led to a shift toward a willingness to invest in higher risk equities and paper. In June, the ECB extended its bond-buying program to include unsecured corporate bonds and raised the volume of monthly buying. At the end of the year, the ECB decided to reduce the program's monthly volume but to extend the bond-buying once again to the end of 2017. The uncertainty in the Italian banking system has persisted, even after the change of government in December, and government bailouts are becoming necessary in some cases. The Bank of England reduced its key interest rate and announced an asset-buying program covering government and corporate bonds. Coupled with hopes for a slow rise in interest rates in the US, this led to a rally on stock markets. The US presidential election in the fall of 2016 generated uncertainty in financial markets. At the moment, it is not yet possible to assess the long-term impact from the new political situation in the US.

Following falls in market prices at the end of the third quarter, hopes for an extension to the ECB's bond-buying program and for a cut in the basic interest rate by the People's Bank of China initially led to a rise in equity prices in the fourth quarter. However, at the same time, market players were unnerved by negative economic indicators from China and the fall in the oil price. European stock markets responded positively to the widely expected hike in the benchmark rate by the US Federal Reserve (Fed) towards the end of the fourth quarter. The rate increase was implemented in December, with the Fed nudging up the target range for its federal funds rate by 25 basis points to 0.5%-0.75%. Three further rises are planned for 2017, taking the range to 1.25%-1.5%.

Europe

The ECB's bond-buying program and the improved economic outlook for the eurozone had an impact on market prices. Viewed across the eurozone as a whole, the indicators continued to point to modest growth, which was slightly below

the prior year. In June, the United Kingdom held a referendum in which a narrow majority voted in favor of leaving the EU. This led to uncertainty in financial markets but there has been no significant impact on capital markets to date other than heightened volatility affecting the pound sterling exchange rate. In Portugal and the Netherlands, economic growth has weakened slightly, whereas in Eastern Europe the recovery in energy prices has had a positive impact. The Russian economy rebounded to the extent that economic output only contracted to a minor degree compared with the previous year.

Germany

Growth in the German economy was robust, although some momentum was lost at the end of the year compared with the first six months. A slide into deflation was successfully averted, and consumer spending and a sustained high level of exports remain the drivers of the German economy. A significant acceleration in inflation was apparent at the end of the year, fueled by the expansionary monetary policy pursued by the ECB.

INTEGRATION INTO THE VOLKSWAGEN GROUP

The Volkswagen Bank GmbH Group forms an integral part of the Volkswagen Financial Services AG subgroup, which brings together the financial services activities of the Volkswagen Group as a whole. The Volkswagen Bank GmbH Group operates, in particular, the financing business for retail customers, business customers and authorized dealers in close cooperation with the brands of the Volkswagen Group.

GLOBAL DEMAND FOR PASSENGER CARS REACHES RECORD HIGH

Worldwide, the number of new passenger car registrations increased to 81.1 million vehicles in fiscal year 2016, exceeding the previous year's record level by 5.4%. Demand rose in the Asia-Pacific, Western Europe, North America and Central Europe regions, while new passenger car registrations in South America, Eastern Europe and Africa failed to match the prior-year levels.

SECTOR-SPECIFIC ENVIRONMENT

The sector-specific environment was influenced significantly by fiscal policy measures, which contributed substantially to the mixed trends in sales volumes in the markets last year. The instruments used were tax cuts or increases, incentive programs and sales incentives, as well as import duties.

In addition, non-tariff trade barriers to protect the respective domestic automotive industry made the free movement of vehicles, parts and components more difficult. Protectionist tendencies were particularly evident where markets were on the decline.

Europe

New passenger car registrations in Western Europe rose by 5.8% in the reporting period to 14.0 million vehicles, the highest level since 2007. This better-than-expected trend was mainly attributable to the positive overall economic environment, low interest rates, low fuel prices and manufacturers' incentive programs. Double-digit growth rates were achieved in Italy (+15.4%) and Spain (+10.9%), especially due to the release of pent-up demand for replacement vehicles. By contrast, growth in new passenger car registrations was relatively moderate in France, at 5.2%. Demand volume in the United Kingdom (+2.3%) was slightly higher than the record level of the previous year.

Germany

In Germany, 3.4 million new passenger vehicles were registered in 2016, 4.5% more than in the previous year. This positive demand trend was due in particular to higher real incomes, the strong labor market and attractive financing options. New passenger car registrations for both private (+6.8%) and commercial (+3.3%) customers contributed to this increase, which resulted in the highest passenger car market volume since 2009. A slight increase in domestic production (up 0.6% to 5.7 million vehicles) contributed to the ongoing recovery of the German passenger car market, whereas passenger car exports (up 0.2% to 4.4 million vehicles) were on a par with the high levels of the previous year.

MIXED REGIONAL DEMAND FOR COMMERCIAL VEHICLES

In 2016, demand for light commercial vehicles was up slightly overall on the previous year: in total, around 9.6 million (previous year: 9.5 million) vehicles were registered worldwide.

In Western Europe, the number of new vehicle registrations rose by 10.0% during the year to 1.8 million units, driven by the region's positive economic performance. The markets in Italy (+28.9%), Spain (+11.6%) and France (+9.4%) recorded high growth rates. In Germany, the 2015 figure was significantly exceeded by 10.2%.

Global demand for mid-sized and heavy trucks with a gross weight of more than six tonnes was higher in fiscal year 2016 than in the previous year, with 2.3 million new vehicle registrations (+0.9%). The volume of vehicles rose by 0.5% in the markets that are relevant for the Volkswagen Group.

In Western Europe, the number of new truck registrations increased by 8.6% to a total of 280 thousand vehicles on the back of positive economic stimulus. The markets in Italy (+41.9%), France (+13.7%) and Spain (+11.6%) in particular recorded high growth rates. In Germany, Western Europe's largest market, the prior-year figure was exceeded by 3.9%.

OVERALL ASSESSMENT OF BUSINESS PERFORMANCE

The Management of Volkswagen Bank GmbH considers the course of business in the year 2016 to have been positive.

Operating profit was better than forecast, coming in above the 2015 level despite the diesel issue. Thus, operating profit was not adversely impacted by the diesel issue. The provision for credit risks from lending and leasing business was below the prior-year level; the margins remained stable.

On September 18, 2015, the US Environmental Protection Agency (EPA) issued a Notice of Violation, publicly announcing that irregularities in relation to nitrogen oxide (NOx) emissions had been discovered in emissions tests on certain vehicles with Volkswagen Group diesel engines. This was followed by further notifications regarding the extent of the diesel issue. As a result of this situation, the Board of Management of Volkswagen Financial Services AG set up a task force in 2015. This task force initially continued its activities in 2016, i.e. reporting regularly to the Management, interfacing with the Volkswagen Group and its brands, and maintaining close contact with the international subsidiaries, regulatory authorities and investors. Concerns focused on funding, the credit quality of the dealer network and residual value risk. The impact from the diesel issue on these concerns is currently receding. Further details are described in the relevant sections of this report. The work of the task force was brought to an end in December 2016 because the effects from the diesel issue on the Volkswagen Bank GmbH Group are now dissipating and can be handled within normal management processes. The Volkswagen Group provided support in dealing with the effects.

New business across Europe recorded strong positive growth over the reporting period. Business volume increased year-on-year, especially in Germany, France, Ireland, Italy and Spain. Margins were maintained at close to the same level compared with the prior year. Interest income rose year-on-year in 2016. Interest expenses went up because of the significantly higher volume of deposits in the direct banking business.

Volkswagen Bank GmbH also continued its efforts to better leverage the potential along the automotive value chain. The integration of financial services into the sales activities of the Volkswagen Group's core brands, already greatly expanded in recent years, was stepped up. A consistent focus on customer wishes makes it possible to accompany the customer and the vehicle throughout the vehicle's lifecycle. The GO^{40} growth program, launched and developed in partnership with the automotive brands, has played a key role in this regard.

One objective of the GO^{40} growth program is to achieve greater penetration and promote customer loyalty. Incorporating service and maintenance packages and insurance services has further increased the value of the customer for the Volkswagen Group and further strengthened the dealer network by generating additional revenue streams. Extending the current GO^{40} growth contracts for all Group brands in key European countries thus plays an essential role in leveraging further potential within the sales activities of the Volkswagen Group.

Fiscal year 2016 saw a continuation in the positive trend in credit risk in Germany, the market in which the Group generates its highest volume of business. A sustained economic recovery was evident in European markets. This led to further growth in vehicle markets with a positive impact on the credit risk position. The UK market saw substantial portfolio growth overall when measured in local currency. However, the volume of loans and receivables was virtually unchanged in 2016 when translated into euros because of the fall in the value of the pound sterling.

The diesel issue in the Volkswagen Group did not have any impact on the credit risk portfolio of the Volkswagen Bank GmbH Group in 2016. The monitoring measures introduced for the dealer portfolio remained in place in the year under review. These measures did not reveal any impact on dealer credit quality. Overall, the credit risk position remained stable in 2016.

Volkswagen Bank GmbH also saw continued contract growth in the residual value portfolio in fiscal year 2016, boosted by the recovery of vehicle markets in Europe. The diesel issue in the Volkswagen Group only had a marginal effect overall on the trend in the residual value portfolio of the Volkswagen Bank GmbH Group in 2016. The used vehicle market was not materially affected by this issue in the year under review either. It was therefore possible to reduce the provision for credit risks, which had been increased at the end of 2015. The remaining risks continue to be adequately covered. Overall, it was clear that the risk position in the residual value portfolio had stabilized in fiscal year 2016.

The Volkswagen Bank GmbH Group achieved a significant increase in its deposit business compared with the prior year.

CHANGES IN KEY PERFORMANCE INDICATORS FOR FISCAL YEAR 2016 COMPARED WITH PRIOR-YEAR FORECASTS

We had forecast an operating profit for fiscal year 2016 slightly above that achieved in 2015. The actual operating profit generated in fiscal year 2016 was significantly higher, representing year-on-year growth of 19.5%.

The Bank managed to expand the portfolio of new contracts and existing contracts as a result of successful collaboration with the brands. Overall, the volume of business was increased in 2016 as forecast. The penetration rate in 2016 remained at the prior-year level and was thus slightly lower than forecast.

A slight increase in the balance of deposits had been forecast for 2016. As a result of focused management of this activity, the actual volume of deposits expanded by 27.9% in 2016.

	Actual 2015	Forecast for 2016	Actual 2016
Nonfinancial performance indicators			
Penetration	17.7%	Slight increase	17.6%
Current contracts (thousands)[1]	2,821	Slight increase	3,002
New contracts (thousands)[1]	1,017	Slight increase	1,081
Financial performance indicators			
Volume of business (€ million)	36,330	Slight increase	38,748
Volume of deposits (€ million)	27,877	Slight increase	35,666
Operating profit (€ million)	539	Slightly above prior-year level	645

1 Since January 1, 2016, a new method has been used to determine the contract figures. The figures for the previous year and the equivalent period in 2015 have been restated accordingly.

FINANCIAL PERFORMANCE

The Volkswagen Bank GmbH Group achieved solid earnings performance in fiscal year 2016, exceeding the level posted in 2015.

Operating profit improved significantly by 19.5% to €645 million (previous year: €539 million). This figure benefited in particular from the positive impact generated by higher volumes and stable margins in the lending and leasing business. The figure also includes support payments from Volkswagen Financial Services AG to compensate for higher funding costs resulting from the diesel issue. These payments were recognized as other operating income. The operating profit was not therefore negatively affected by the diesel issue.

Profit before tax amounted to €669 million (+16.3%), well above the figure of €575 million achieved in the prior year. Of this total, the share accounted for by the international branches and companies was €327 million or 49%. This reflected, in particular, the impact from rising volumes of business in the Italian, French and Irish markets

Net income from lending and leasing transactions before provision for credit risks amounted to €1,299 million, a year-on-year gain of €58 million. This increase was mainly attributable to the uptrend in the volume of leasing business and a lower provision for credit risks.

Net income from leasing transactions before provision for credit risks also included impairment losses on lease assets in an amount of €37 million and reversals of impairment losses recognized in the previous year amounting to €6 million. The new impairment losses were attributable to normal market movements; only the prior-year figure was affected by the diesel issue.

The required provision for credit risks expenses of €334 million were 12% higher than the equivalent expenses in the previous year (€299 million). Income from the reversal of valuation allowances no longer required and income from loans and receivables previously written off amounting to a total of €296 million was significantly more than in the prior year (€227 million), with the result that the provision for credit risks from the lending and leasing business at €38 million was €33 million lower year-on-year (previous year: €71 million).

Net fee and commission income was in negative territory in 2016, with a net expense of €30 million. The equivalent figure in the prior year had been net income of €39 million. This was largely attributable to increased dealer commissions as part of the strategy to lift penetration rates.

General and administrative expenses were up on the prior-year level to €829 million (previous year: €794 million). The main reasons were the higher non-staff operating expenses and greater expense for advertising and sales promotion activities.

Other operating income largely consisted of the reimbursement of costs from Group companies. In 2016, the net income in this regard amounted to €215 million (previous year: €189 million). Income from the reversal of provisions also went up by €48 million to €81 million. Other operating expenses declined to €108 million (previous year: €131 million), the largest item being the expenses for litigation and legal risks.

Including the net loss on the measurement of financial instruments in the amount of €9 million (previous year: net gain of €10 million) and the other components of profit or loss, the Volkswagen Bank GmbH Group generated profit after tax of €482 million (+15.3%).

The German market accounts for the greatest proportion of the volume of current contracts in the Volkswagen Bank GmbH Group at around 53.0% (previous year: 56.9%). It generated profit before tax (excluding income from equity-accounted investments) of €431 million (previous year: €363 million).

The profit of Volkswagen Bank GmbH determined in accordance with the HGB (after deduction of taxes) amounting to €414 million will be transferred to the parent company, Volkswagen Financial Services AG, under the existing profit-and-loss transfer agreement.

NET ASSETS AND FINANCIAL POSITION

Lending Business

The lending business of the Volkswagen Bank GmbH Group mainly consists of loans granted to retail customers, business customers and dealers. The volume of these loans and receivables went up by 6.7% to €38.7 billion. The share of the customer lending volume accounted for by the international branches and Volkswagen Bank Polska S.A. rose from €12.9 billion to €13.8 billion. This increase in the volume of loans and receivables resulted from the business expansion, particularly in Germany, France and Italy.

Retail financing

In Germany and the other European markets, the overall level of current contracts went up by 8.5% as a consequence of the greater demand for passenger cars. The number of retail financing contracts increased by 2.2% to 2,196,598 (previous year: 2,149,433). The number of new retail financing contracts reached 714,153 (previous year: 693,177).

As of December 31, 2016, the volume of loans and receivables in retail financing amounted to €24.9 billion (previous year: €23.3 billion). The foreign branches of Volkswagen Bank GmbH and the Polish company accounted for €4.9 billion (previous year: €4.5 billion) of these loans and receivables.

Dealer financing

The lending volume in dealer financing – which comprises loans to and receivables from dealers in connection with financing for inventory vehicles, as well as working capital and investment loans – rose marginally by 2.3% to €10.5 billion.

The share of this volume of loans and receivables accounted for by the international branches and Volkswagen Bank Polska S.A. in 2016 remained unchanged at €5.7 billion.

The valuation allowances on loans and receivables were reduced year-on-year by €59 million to €520 million.

Leasing business

Receivables from leasing transactions were significantly up by 20.5% year-on-year to €3.0 billion. By far the greatest proportion was attributable to finance lease receivables.

Marketable securities

The portfolio held by the Volkswagen Bank GmbH Group predominantly comprises bonds from various countries amounting to €2.2 billion (previous year: €2.2 billion) and ABSS issued by the special purpose entities of Volkswagen Financial Services (UK) Ltd., Milton Keynes, Volkswagen Leasing GmbH and Volkswagen Finance S.A., Madrid, Spain, totaling €2.3 billion (previous year: €0.3 billion).

Long-term financial assets

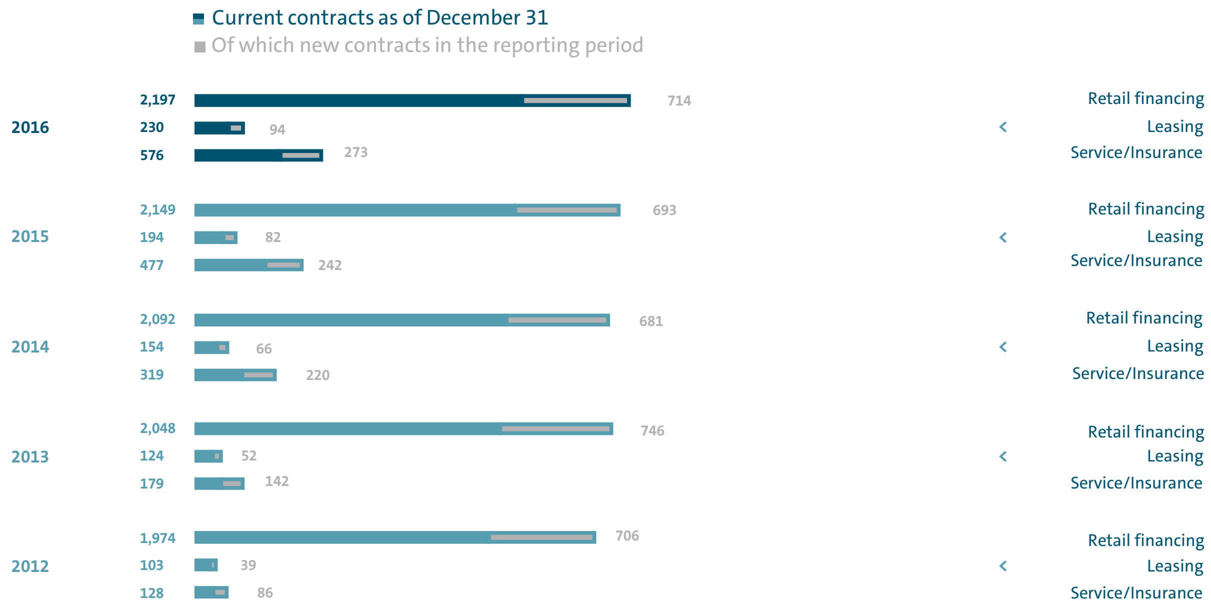
As of December 31, 2016, Volkswagen Bank GmbH held 1% of the equity in OOO Volkswagen Bank RUS, Moscow. This holding remained unchanged year-on-year. Volkswagen Bank Polska S.A., Warsaw, is the sole shareholder of Volkswagen Serwis Ubezpieczeniowy Sp.z.o.o., Warsaw.

CURRENT CONTRACTS AND NEW CONTRACTS

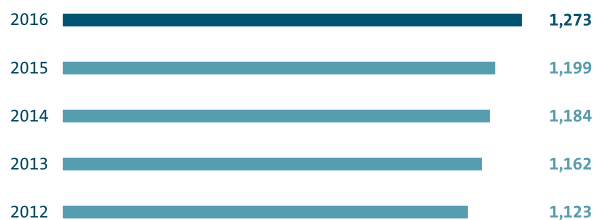
Thousands[1,3]	VW Bank Group	of which Germany	of which Italy	of which France	Other
Current contracts	3,002	1,590	527	622	264
Retail financing	2,197	1,571	277	142	207
Leasing business	230	-	44	168	17
Service/insurance	576	19	206	311	39
New contracts	1,081	504	214	269	94
Retail financing	714	502	93	48	71
Leasing business	94	-	16	69	9
Service/insurance	273	2	104	152	13
€ million					
Loans to and receivables from customers attributable to					
Retail financing	24,940	19,993	2,220	945	1,782
Dealer financing	10,538	4,846	659	1,458	3,575
Leasing Business	3,014	-	864	1,942	208
Lease assets	877	-	-	877	-
Percent					
Penetration[2]	17.6	14.1	37.5	40.6	9.6

1 All figures shown are rounded, so minor discrepancies may arise from addition of these amounts.
2 Ratio of new contracts for new Group vehicles to deliveries of Group vehicles in each case in relation to the markets shown for the Volkswagen Bank GmbH Group.
3 Since January 1, 2016, a new method has been used to determine the contract figures. The figures for the previous year 2015 have been restated accordingly.

DEVELOPMENT OF NEW CONTRACTS AND CURRENT CONTRACTS AS OF DECEMBER 31
In thousands



DIRECT BANK CUSTOMERS AS OF DECEMBER 31
Lending and deposit business and borrowings (in thousands)



Including corporate customers since 2013

CUSTOMER DEPOSITS AS OF DECEMBER 31
in € million

Deposit Business and Borrowings

On the equity and liabilities side of the balance sheet, the main items other than equity are liabilities to customers, which grew by 24.5% to €37.9 billion (previous year: €30.5 billion), notes and commercial paper issued of €4.3 billion (previous year: €7.6 billion) and liabilities to banks of €4.9 billion (previous year: €4.0 billion).

DEPOSIT BUSINESS

The Volkswagen Bank GmbH Group achieved a significant increase in its deposit business compared with the prior year. As of the reporting date, the volume of customer deposits amounted to €35.7 billion, which equates to a year-on-year rise of 27.9% (previous year: €27.9 billion). Based on this deposits portfolio, the Volkswagen Bank GmbH Group continued to maintain its market-leading position in the automotive direct banking segment. The deposit business is a significant contributing factor in helping the Volkswagen Group retain its customers. On this basis, customer deposits funded 63.3% of the business volume (previous year: 56.7%).

In addition to the cover provided by statutory deposit guarantees, Volkswagen Bank GmbH is also still a member of the Deposit Protection Fund of the Bundesverband deutscher Banken e.V. (Association of German Banks).

EQUITY

The subscribed capital of Volkswagen Bank GmbH remained unchanged at €318.3 million in fiscal year 2016.

In the year under review, Volkswagen Financial Services AG increased the equity of Volkswagen Bank GmbH by €2.1 billion. Following this increase, the capital reserves of Volkswagen Bank GmbH amounted to €6.0 billion as of December 31, 2016.

The profit in accordance with the HGB to be transferred to Volkswagen Financial Services AG under the existing profit-and-loss transfer agreement amounted to €414 million (previous year: €268 million).

Equity in accordance with IFRSs as of December 31, 2016 was €7.2 billion (previous year: €5.0 billion). This resulted in an equity ratio (equity divided by total assets) of 12.7% (previous year: 10.2%) based on total assets of €56.3 billion.

CAPITAL ADEQUACY ACCORDING TO REGULATORY REQUIREMENTS

Under the provisions of the Capital Requirements Regulation (CRR), a bank is deemed to have adequate capital backing if the Common Equity Tier 1 (CET1) capital ratio is at least 4.5%, the Tier 1 capital ratio is at least 6.0% and the total capital ratio is at least 8.0%.

The ECB, acting on the basis of Article 16 of Council Regulation No. 1024/2013 of October 15, 2013 conferring specific tasks on the European Central Bank concerning policies relating to the prudential supervision of credit institutions, issued a decision on November 25, 2016, establishing regulatory requirements for Volkswagen Bank GmbH. The decision was based on a supervisory review in 2016. Volkswagen Bank GmbH satisfied both the minimum requirements of the CRR and the additional requirements specified by the supervisor at all times in the reporting period.

The total capital ratio (ratio of own funds to the total risk exposure amount) was 14.4% at the end of the reporting period (previous year: 11.2%), well above the statutory minimum ratio of 8%.

The Tier 1 capital ratio and Common Equity Tier 1 capital ratio were each 14.3% (previous year: 11.1%) at the end of the reporting period, likewise well above the respective minimum ratios of 6% and 4.5% specified in the CRR.

The total risk exposure amount is made up primarily of credit risks, market risks, operational risks and credit valuation adjustment (CVA charge). The Credit Risk Standardized Approach (CRSA) is used to quantify credit risk and to determine risk-weighted exposures. The Standardized Approach as specified in Article 317 of the CRR is used to calculate the own funds requirements for operational risk. The own funds requirements for the CVA charge are determined using the standardized method specified in Article 384 of the CRR.

The following overview shows a breakdown of the total risk exposure amount and own funds:

		Dec. 31, 2016		Dec. 31, 2015
Total risk exposure amount[1] (€ million)		44,552		38,288
of which risk-weighted exposure amounts for credit risk	41,716		35,700	
of which own funds requirements for market risk *12.5	384		244	
of which own funds requirements for operational risk *12.5	2,400		2,297	
of which own funds requirements for credit valuation adjustments *12.5	52		47	
Eligible own funds (€ million)		6,401		4,292
Own funds (€ million)		6,401		4,292
of which Common Equity Tier 1 capital	6,372		4,262	
of which Additional Tier 1 capital	0		0	
of which Tier 2 capital	29		30	
Common Equity Tier 1 capital ratio (percent)[2]		14.3		11.1
Tier 1 capital ratio (percent)[2]		14.3		11.1
Total capital ratio (percent)[2]		14.4		11.2

1 According to Article 92(3) of the CRR.
2 According to Article 92(1) of the CRR.

REGULATORY RATIOS OF THE VOLKSWAGEN BANK GMBH AS OF DECEMBER 31

1 Calculation was based on the Solvabilitätsverordnung (SolvV – German Solvency Regulation) for the years 2012 and 2013; since January 1, 2014, it has been based on the CRR.
2 The amounts of Tier 1 capital and Common Equity Tier 1 capital are the same because Volkswagen Bank GmbH has not issued any Additional Tier 1 capital instruments.

The year-on-year change in the regulatory capital ratios (CET1 capital ratio, Tier 1 capital ratio and total capital ratio) is largely attributable to the additions to capital totaling €2.1 billion and to the rise in business volume.

TIER 1 CAPITAL RATIO/COMMON EQUITY TIER 1 CAPITAL RATIO UNDER CRR/SOLVV*
figures in %

OVERALL RATIO/TOTAL CAPITAL RATIO UNDER CRR/SOLVV*
figures in %

1 Calculation was based on the Solvabilitätsverordnung (SolvV – German Solvency Regulation) for the years 2012 and 2013; since January 1, 2014, it has been based on the CRR.

As an individual bank, Volkswagen Bank GmbH has a relatively high total capital ratio, which ensures that there is an adequate level of capital, even with a sharp rise in the volume of business. In addition to making additions to capital reserves and using Tier 2 capital in the form of subordinated liabilities, the Bank can also make use of ABS transactions to optimize its capital management. Volkswagen Bank GmbH, as an individual bank, therefore has the benefit of a sound foundation for further expansion of the financial services business.

CHANGES IN OFF-BALANCE-SHEET LIABILITIES

The Volkswagen Bank GmbH Group's irrevocable credit commitments increased year-on-year by €175 million and as of December 31, 2016 amounted to €1,465 million.

LIQUIDITY ANALYSIS

The Volkswagen Bank GmbH Group is funded largely through capital market and asset-backed security programs, and through direct banking deposits. Volkswagen Bank GmbH holds liquidity reserves in the form of securities deposited in its operational safe custody account with Deutsche Bundesbank. Proactive management of the operational safe custody account, which allows Volkswagen Bank GmbH to participate in funding facilities, has proven to be an efficient liquidity reserve approach. The securities deposited as collateral in the operational safe custody account include, in addition to bonds from various countries amounting to €1.8 billion, senior ABS bonds issued by special purpose entities of Volkswagen Leasing GmbH, Volkswagen Finance S.A. and Volkswagen Bank GmbH amounting to €9.0 billion. These senior ABS bonds are not reported in the consolidated financial statements of Volkswagen Bank GmbH because these special purpose entities are themselves consolidated.

Certain standby lines of credit at other banks are also available to protect against unexpected fluctuations in cash flows. There are no plans to make use of these standby lines of credit; their sole purpose is to serve as backup to safeguard liquidity.

To ensure there is appropriate liquidity management, Treasury prepares four different funding matrices, carries out cash flow forecasts and uses this information to determine the relevant range of liquidity coverage. In these calculations, the legally determined cash flows are assumed for funding instruments, whereas estimated cash flows are used for other factors that affect liquidity. In the reporting period, the range of liquidity coverage taking into account simulated, limited funding and a partial withdrawal of overnight deposits came to a minimum of 37 weeks.

A stricter constraint on the management of liquidity at Volkswagen Bank GmbH and in the entities within the regulatory basis of consolidation of Volkswagen Financial Services AG is the liquidity coverage ratio (LCR). From January to December in the year under review, this ratio varied between 78% and 226% for Volkswagen Bank GmbH and was therefore well above the lower regulatory limit of 70% at all times. The changes in the liquidity ratio are continuously monitored by Treasury and proactively managed by issuing a lower limit for internal management purposes. Central bank balances and government bonds are eligible as highly liquid assets for the purposes of the LCR.

The requirement under the Mindestanforderungen an das Risikomanagement (MaRisk – German Minimum Requirements Risk Management) for Volkswagen Bank GmbH to provide a highly liquid cash buffer and appropriate liquidity reserves to cover any liquidity requirements over seven-day and thirty-day time horizons was also satisfied at all times, even under various stress scenarios. Compliance with this requirement is determined and continuously reviewed as part of the liquidity risk management system. In this process, the cash flows for the coming twelve months are projected and compared against the potential funding available

in each maturity band. Adequate potential funding to cover the liquidity requirements was available at all times, both in the normal scenario and in the stress tests required by MaRisk.

FUNDING

Strategic Principles

In terms of funding, the Volkswagen Bank GmbH Group generally pursues a strategy of diversification with the aim of achieving the best possible balance of cost and risk. This means accessing the widest possible variety of funding sources in the various regions and countries with the objective of safeguarding funding on a long-term basis at optimum terms.

Implementation

In 2016, the funding situation was shaped by the diesel issue in the Volkswagen Group.

Volkswagen Bank GmbH did not issue any unsecured bonds on capital markets in the reporting period. It was able to compensate for the impaired access to the capital market by using promissory notes, ECB funding instruments and attracting a greater volume of deposits.

In the reporting period, Volkswagen Bank GmbH held the Driver Master volume at the same level and did not issue any further securitization transactions.

In the reporting period, customer deposit business grew by €7.8 billion to €35.7 billion.

The Bank continued to implement its strategy of obtaining maturity-matched funding as far as possible by borrowing on terms with matching maturities and by using derivatives. Currency risks were largely eliminated by using derivatives. The Volkswagen Bank GmbH Group was able to meet its payment obligations when due at all times in the reporting period. Our diversified funding structure and our proactive management of liquidity ensure that the Bank will also remain solvent at all times in the future. No liquidity commitments have been issued to special purpose entities.

Volkswagen Bank GmbH

(Condensed, in accordance with the HGB)

Volkswagen Bank GmbH has significant influence over the business performance of the Volkswagen Bank GmbH Group. For further information, please refer to the previous section. In the following section, we report on the developments in the annual financial statements of Volkswagen Bank GmbH in accordance with the HGB.

BUSINESS PERFORMANCE 2016

The result from ordinary activities amounted to €553.3 million compared with €423.2 million in the prior year.

The net interest income earned by Volkswagen Bank GmbH, including interest anomalies from negative interest and net income from leasing transactions, came to €1,518.7 million compared with €1,399.2 million in the prior year.

As in the prior year, interest income from lending and money market transactions including finance leases arose predominantly from financing business with end customers and from vehicle and capital investment financing with dealers in the Volkswagen Group, increasing by €59.5 million year-on-year to €1,356.2 million.

Income from leasing business amounted to €351.2 million (previous year: €271.4 million). Interest anomalies amounting to an expense of €9.1 million (previous year: expense of €1.3 million) resulted primarily from money market transactions in connection with the Bank's reserve balance at the ECB in excess of the minimum reserve requirement and from short-term deposits with domestic banks.

Volkswagen Bank GmbH earned interest income of €86.4 million (previous year: €76.1 million) from marketable securities. Of this amount, €35.4 million (previous year: €31.4 million) was attributable to marketable securities purchased from ABS special purpose entities of Volkswagen Bank GmbH. A further €13.7 million (previous year: €5.4 million) was accounted for by interest income on marketable securities purchased from special purpose entities of Volkswagen Financial Services (UK) Ltd., Milton Keynes, UK, Volkswagen Leasing GmbH and Volkswagen Finance S.A., Madrid, Spain.

Net fee and commission income decreased by €60.0 million compared with the net income earned in the prior year and amounted to a net expense in 2016. Fee and commission income rose in particular in connection with insurance broking and the administration and collection of loans and receivables sold as part of ABS transactions. However, higher commission expenses arose from the payment of greater commissions to dealers in the consumer credit and leasing business as part of the strategy to lift penetration rates.

The rise of €144.5 million in other operating income to €475.2 million resulted primarily from income generated on the termination of ABS transactions. This income went up by €98.4 million compared with the prior year. Income generated from internal cost allocations within the Volkswagen Financial Services AG subgroup also increased by a total of €18 million.

General and administrative expenses went up by €33.4 million. The primary reasons were increases of €14.0 million in third-party services (previous year: €64.0 million) and €18.1 million in expenses for advertising and sales promotion campaigns.

Depreciation and write-downs on lease assets at the French and Italian branches rose by €60.2 million to €324.7 million. Other operating expenses amounted to €156.9 million (€135.5 million).

The provision for credit risks recognized in fiscal year 2016 was €29.6 million less than in the prior year (previous year: €12.6 million). This figure arose from the combination of an increase of €54.2 million in income from the reversal of valuation allowances and a rise of €24.6 million in additions to the provision for credit risks.

The profit after tax of €413.7 million will be transferred to Volkswagen Financial Services AG pursuant to the existing control and profit-and-loss transfer agreement.

The volume of customer loans and receivables reported in the balance sheet went up by 17.2% to €43.2 billion (previous year: €36.9 billion). In particular, sales financing loans and receivables rose by €3.1 billion to €22.7 billion, and the loans to and receivables from affiliated companies increased to €5.6 billion.

In the year under review, loans and receivables in a nominal amount of €4.8 billion were sold to special purpose entities as part of the following existing, revolving ABS structures: Driver Master Compartment 1, Driver Master Compartment 2,

Driver Master Compartment 3, Driver Master Compartment 4, Driver Master Compartment 5, Driver Master Compartment 6 and Driver Master Compartment 7. In the case of ABS transactions in which Volkswagen Bank GmbH has not acquired any securities from the special purpose entities concerned, the sold loans/receivables are no longer reported in the HGB balance sheet. As of the reporting date, the carrying amount of these loans and receivables was €2.4 billion (previous year: €3.8 billion).

On April 11, 2016, MAN Financial Services S.p.A., Dossobuono di Villafranca (VR), Italy, – a subsidiary at that time – was merged into Volkswagen Bank GmbH, effective retroactively from January 1, 2016.

Volkswagen Bank GmbH acquired MAN Financial Services S.A.S., Evry Cedex, France on April 1, 2016 from MAN Finance International GmbH, Munich. The acquired company was merged into Volkswagen Bank GmbH on July 28, 2016, effective retroactively from January 1, 2016.

On June 21, 2016, Volkswagen Bank GmbH sold its holding in VISA Europe Limited, London.

Most of Volkswagen Bank GmbH's portfolio comprises securities from ABS transactions. In 2016, Volkswagen Bank GmbH acquired in full the additional securities (€1.9 billion) issued under some of its own ABS transactions (Driver Master Compartment 2, Driver Master Compartment 3, Driver Master Compartment 4, Driver Master Compartment 5, Driver Master Compartment 6 and Driver Master Compartment 7). The value of the portfolio of securities resulting from all transactions amounted to €8.5 billion (previous year: €9.2 billion). For investment purposes, the portfolio also included ABSs with a total value of €2.3 billion (previous year: €0.3 billion) issued by special purpose entities of Volkswagen Financial Services (UK) Ltd., Milton Keynes, UK, Volkswagen Leasing GmbH and Volkswagen Finance S.A., Madrid, Spain.

Marketable securities of €9.5 billion (previous year: €8.0 billion) are used as collateral for participating in the open market operations of Deutsche Bundesbank. As of the reporting date, the existing participation in these open market operations stood at €4.5 billion.

The main items on the equity and liabilities side of the balance sheet are the liabilities to customers (including direct banking business) of €37.4 billion (previous year: €29.8 billion) and the notes and commercial paper issued of €1.8 billion (€3.7 billion).

Volkswagen Bank GmbH successfully achieved further expansion in its deposits business. The total volume of customer deposits amounted to €35.3 billion as of the reporting date. This equated to a substantial rise of 28.2% compared with the volume as of December 31, 2015 (€27.5 billion). The proportion of the funding mix at Volkswagen Bank GmbH accounted for by deposits was 58.1% (previous year: 52.4%).

The other provisions mainly comprised provisions to cover costs associated with litigation and legal risks. The provisions for litigation and legal risks of €279 million (previous year: €246 million) reflect the risks identified as of the reporting date in relation to utilization and legal expenses arising from the latest decisions by the courts and from ongoing proceedings.

The capital reserves of Volkswagen Bank GmbH increased to €6.0 billion in 2016 following an addition to these reserves of €2.1 billion by Volkswagen Financial Services AG.

As a result of business growth and the repurchase of securities from ABS transactions, the total assets as of the reporting date amounted to €60.7 billion (previous year: €52.5 billion).

INCOME STATEMENT OF VOLKSWAGEN BANK GMBH, BRAUNSCHWEIG

€ million	2016	2015
Net interest income	1,167	1,128
Net leasing income	351	271
Net fee and commission expense	–103	–43
Administrative expenses	798	765
Other comprehensive income	–13	–76
Income from the disposal of equity investments	11	0
Provision for credit risks	62	92
Result from ordinary business activities	**553**	**423**
Extraordinary result	8	0
Tax expense	147	155
Profits transferred under a profit transfer agreement	414	268
Net income for the year	**0**	**0**
Retained profits brought forward	0	0
Net retained profits	**0**	**0**

BALANCE SHEET STRUCTURE OF VOLKSWAGEN BANK GMBH, BRAUNSCHWEIG

€ million	Dec. 31, 2016	Dec. 31, 2015
Assets		
Cash reserve	1,372	1,268
Loans to and receivables from banks	1,713	1,305
Loans to and receivables from customers	43,210	36,878
Marketable securities	12,839	11,692
Equity investments and shares in affiliated companies	77	66
Lease assets	1,004	803
Other assets	456	470
Total assets	**60,671**	**52,483**
Equity and liabilities		
Liabilities to banks	4,872	3,970
Liabilities to customers	37,417	29,831
Notes, commercial paper issued	1,815	3,666
Provisions	578	510
Subordinated liabilities	30	30
Funds for general banking risks	26	26
Equity	6,370	4,290
Other liabilities	9,563	10,160
Total equity and liabilities	**60,671**	**52,483**
Balance sheet disclosures		
Contingent liabilities	135	97
Other obligations	1,435	1,308

NUMBER OF EMPLOYEES

As of December 31, 2016, 2,786 employees (previous year: 2,638) of Volkswagen Financial Services AG were assigned to Volkswagen Bank GmbH's business units under staff leasing arrangements.

A total of 956 staff members (previous year: 855) also held direct employment contracts with Volkswagen Bank GmbH as of December 31, 2016. Of this number, 1 (previous year: 2) employee was based in Germany and 955 (previous year: 853) were based at the international branches of Volkswagen Bank GmbH.

OPPORTUNITIES AND RISKS FACING VOLKSWAGEN BANK GMBH

The business performance of Volkswagen Bank GmbH is largely subject to the same opportunities and risks as those faced by the Volkswagen Bank GmbH Group. These opportunities and risks are described in the report on opportunities and risks in the following sections of this management report.

Report on Opportunities and Risks

The proactive management of opportunities and risks is a fundamental element of the successful business model used by the Volkswagen Bank GmbH Group.

RISKS AND OPPORTUNITIES

In this section, we report on the risks and opportunities that arise in connection with our business activities. The risks and opportunities are grouped into various categories. Unless specifically stated, there were no material year-on-year changes to the individual risks or opportunities.

We use analyses of the competitive and operating environment, together with market observations, to identify not only risks but also opportunities, which then have a positive impact on the design of our products, the success of the products in the marketplace and on our cost structure. Risks and opportunities that we expect to materialize have already been taken into account in our medium-term planning and forecast. The following sections therefore describe fundamental opportunities that could lead to a positive variance from our forecast and the risk report presents a detailed description of the risks.

MACROECONOMIC OPPORTUNITIES

Against the backdrop of further economic growth, the Management of Volkswagen Bank GmbH expects to see a moderate increase in the number of vehicle deliveries to Volkswagen Group customers, enabling it to build on its position in global markets on a sustainable basis. The Volkswagen Bank GmbH Group supports this positive trend by providing financial services products designed to promote sales.

The probability of a global recession is considered to be low overall. However, diminished rates of global economic growth or a period of below-average growth rates cannot be ruled out. The macroeconomic environment could also give rise to opportunities for the Volkswagen Bank GmbH Group if actual trends turn out to be better than forecasted.

STRATEGIC OPPORTUNITIES

As well as continuing its international focus by tapping new markets, the Volkswagen Bank GmbH Group believes that developing innovative products that are tailored to customers' changing mobility requirements creates additional opportunities. Growth areas such as mobility products and service products are being systematically developed and expanded. Further opportunities may be created by launching established products in new markets.

The digitalization of our business presents a significant opportunity for the Volkswagen Bank GmbH Group. The aim is to ensure that all our products are also available online by 2025. By expanding digital sales channels, we are addressing the changing needs of our customers and strengthening our competitive position.

OPPORTUNITIES FROM CREDIT RISK

Opportunities may arise in connection with credit risk if the losses actually incurred on lending transactions turn out to be lower than the prior calculations of expected loss and the associated provisions recognized on this basis. A situation in which the incurred losses are lower than the expected losses can occur particularly in individual countries in which economic uncertainty is currently dictating the need for a higher provision for credit risks but in which the economic circumstances then stabilize, resulting in an improvement in the credit quality of the borrowers concerned.

OPPORTUNITIES FROM RESIDUAL VALUE RISK

Residual values of vehicles continuously change according to market circumstances. When vehicles are remarketed, the Volkswagen Bank GmbH Group may be presented with the opportunity to achieve a price that is higher than the calculated residual value if increasing demand raise market values higher than expected.

KEY FEATURES OF THE INTERNAL CONTROL SYSTEM AND THE INTERNAL RISK MANAGEMENT SYSTEM IN RELATION TO THE FINANCIAL REPORTING PROCESS

The internal control system (ICS) for the consolidated and annual financial statements of Volkswagen Bank GmbH, as far as it is relevant to the accounting system, is defined as the sum of all principles, procedures and activities aimed at ensuring the effectiveness, efficiency and propriety of the financial reporting and ensuring compliance with the relevant legal requirements. The internal risk management system (IRMS) related to the accounting system is concerned with the risk of misstatement in the bookkeeping systems at Bank and Group levels as well as in external financial reporting. The sections below describe the key elements of the ICS/IRMS as they relate to the financial reporting process of the Volkswagen Bank GmbH Group.

- The Management of Volkswagen Bank GmbH is the governing body with responsibility for the executive management of the business. In this role, the Management has set up accounting, customer service, treasury, risk management, controlling and compliance units, each with clearly separated functions and clearly assigned areas of responsibility and authority, to ensure that the Bank carries out accounting and financial reporting processes properly.
- Group-wide rules and regulations have been put in place as the basis for a standardized, proper and continuous financial reporting process.
- For example, the accounting policies applied by the domestic and foreign entities included in the consolidated financial statements of Volkswagen Bank GmbH are governed by the Volkswagen Financial Services AG Group's accounting policies, including the accounting requirements specified in the International Financial Reporting Standards (IFRS).
- The Volkswagen Bank GmbH Group's accounting standards also set out the specific formal requirements for the consolidated financial statements. The standards determine the basis of consolidation and also describe in detail the components of the reporting packages to be prepared by the Group companies. The formal requirements include the mandatory use of a complete, standardized set of forms. The accounting standards also include, for example, specific details relating to the recognition and processing of intragroup transactions and the associated reconciliation of balances.
- At Group level, specific control activities aimed at ensuring that the consolidated financial reporting provide a true and fair view include the analysis and any necessary adjustment of single-entity financial statements submitted by the consolidated entities, taking into account the reports submitted by the independent auditors and the related discussions concerning the financial statements.
- These activities are supplemented by the clear delineation of areas of responsibility and by various monitoring and review mechanisms. The overall aim is to ensure that all transactions are accurately recognized in the accounts, processed and evaluated, and then properly reported.
- These monitoring and review mechanisms are designed with both integrated and independent process components. For example, automated IT process controls account for a significant proportion of the integrated process activities alongside manual process controls, such as double-checking by a second person. These controls are enhanced by specific functions at Group level carried out by the parent company Volkswagen AG, for example functions within the responsibility of the Group tax department.
- Internal auditing is a key component of the Volkswagen Bank GmbH Group's monitoring and control system. The Internal Audit department carries out regular audits of accounting-related processes in Germany and abroad as part of its risk-oriented auditing activities and reports on these audits directly to the Management of Volkswagen Bank GmbH.

To summarize, the existing internal monitoring and control system of the Volkswagen Bank GmbH Group is intended to ensure that the financial position of the individual entities in the Group and the Volkswagen Bank GmbH Group itself as of the reporting date December 31, 2016 has been based on information that is reliable and has been properly recognized. No material changes were made to the internal monitoring and control system of the Volkswagen Bank GmbH Group after the reporting date.

ORGANIZATIONAL STRUCTURE OF RISK MANAGEMENT

In the Volkswagen Bank GmbH Group, risk is defined as the danger of loss or damage that could occur if an expected future development turns out to be less favorable than planned.

The Volkswagen Bank GmbH Group is exposed to a large number of risks typical for the financial services sector as part of its primary operating activities. The Group takes on these risks responsibly so that it can specifically exploit associated market opportunities.

The Volkswagen Bank GmbH Group has put a risk management system into place to identify, assess, manage, monitor and communicate risks. The risk management system comprises a framework of risk principles, organizational structures and processes for assessing and monitoring risks. The individual elements are closely aligned with the activities of the individual divisions. This structure makes it possible to identify at an early stage any trends that could represent a risk to the business as a going concern so that appropriate corrective action can then be initiated. No material changes were made to the risk management methodology in the reporting period.

Appropriate procedures are in place to ensure the adequacy of the risk management system. Firstly, the Group Risk Management unit continuously monitors the system. Secondly, the individual elements in the system are regularly reviewed on a risk-oriented basis by the Internal Audit department and as part of the audit of the annual financial statements by the independent auditors.

Within Volkswagen Bank GmbH, responsibility for risk management and credit analysis is assigned to a particular member of the Management. In this role, the Management member concerned submits regular reports to the other members and to the sole shareholder, Volkswagen Financial Services AG, on the overall risk position of the Volkswagen Bank GmbH Group.

An important feature of the risk management system at Volkswagen Bank GmbH is the clear, unequivocal separation of tasks and areas of responsibility, both organizationally and in terms of personnel, between the holding company (Group Risk Management unit) and the markets (local risk management) to ensure that the system is fully functioning at all times and regardless of any particular personnel involved.

One of the functions of the Group Risk Management unit is to provide framework constraints for the organization of the risk management system. This function includes drawing up risk policy guidelines, developing and maintaining methodologies and processes relevant to risk management as well as issuing and monitoring international framework standards for the procedures to be used around the world.

In particular, these activities involve providing models for carrying out credit assessments, quantifying the different categories of risk, determining risk-bearing capacity and measuring collateral. Group Risk Management is therefore responsible for identifying possible risks, analyzing, quantifying and assessing risks, and for determining the resulting measures to manage the risks. Group Risk Management is a neutral, independent unit and reports directly to the Management of Volkswagen Bank GmbH.

Local risk management units ensure that the requirements specified by Group Risk Management are implemented and complied with in each market.

Local risk management is responsible for the detailed design of local structures for the models and procedures used for risk measurement and management and carries out local implementation from process and technical perspectives. There is a direct line of reporting from local risk management to Group Risk Management.

To summarize, continuous monitoring of risks, transparent and direct communication with the Management and the integration of all information obtained into the operational risk management system form a foundation for the best possible leveraging of market potential based on conscious, effective management of the overall risk faced by the Volkswagen Bank GmbH Group.

RISK STRATEGY AND RISK MANAGEMENT

Fundamental decisions relating to strategy and the instruments of risk management are the responsibility of the Management of Volkswagen Bank GmbH.

As part of this overall responsibility, the Management of Volkswagen Bank GmbH has introduced a MaRisk-compliant strategy process and drawn up a business and risk strategy. The ROUTE2025 business strategy sets out the fundamental views of the Management of Volkswagen Bank GmbH on key matters relating to business policy. It includes the objectives for each major business activity and the strategic areas for action to achieve the relevant objectives. The business strategy also serves as the starting point for creating a consistent risk strategy.

The risk strategy is reviewed each year and as required on the basis of a risk inventory, risk-bearing capacity and legal requirements. It is adjusted where appropriate and discussed at the Annual General Meeting of Volkswagen Bank GmbH. The risk strategy describes the main risk management goals and action plans for each category of risk taking into account the business policy focus (business strategy), risk tolerance and risk appetite. A review is carried out annually to establish whether the goals have been attained. The causes of any variances are analyzed and then discussed at the Annual General Meeting of Volkswagen Bank GmbH.

The risk strategy includes all material quantifiable and non-quantifiable risks. Further details and specifics for the individual risk categories are set out in risk substrategies and included in operational requirements as part of the planning round.

The Management of Volkswagen Bank GmbH is responsible for specifying and subsequently implementing the overall risk strategy in the Volkswagen Bank GmbH Group.

RISK INVENTORY

The objective of the risk inventory, which has to be carried out at least annually, is to identify the main categories of risk. To this end, all known categories of risk are investigated to establish whether they arise in the Volkswagen Bank GmbH Group. In the risk inventory, the relevant categories of risk are examined in greater detail, quantified or, if they cannot be quantified, assessed by experts, and then evaluated to determine whether they are material for the Volkswagen Bank GmbH Group.

The risk inventory carried out using the base data as of December 31, 2015 came to the conclusion that the following quantifiable categories of risk should be classified as material: counterparty default risk, earnings risk, direct residual value risk, market risk, liquidity risk and operational risk; it also concluded that reputational risk and strategic risk, which are not quantifiable, should also be considered material. Indirect residual value risk was classified as immaterial because it accounted for a low proportion of the overall risk. Other existing subcategories of risk are taken into account within the categories specified above.

RISK-BEARING CAPACITY, RISK LIMITS AND STRESS TESTING

A system has been set up to determine the risk-bearing capacity of the Volkswagen Bank GmbH Group. This system compares the economic risk against available financial resources referred to as the risk-taking potential. An institution has the capacity to bear its risk if, as a minimum, all material risks to which the institution is exposed are covered at all times by the institution's risk-taking potential.

The results from the risk inventory provide the basis for the level of detail in the design of the risk management process and for inclusion in risk-bearing capacity. In line with standard banking practice, risks are assessed using the net method.

The main risks are quantified as part of the risk-bearing capacity analysis using a going concern approach with a standard confidence level of 90% (exception: liquidity risk [funding risk] with a confidence level of 99%) and a time horizon of one year. Risk-bearing capacity is also analyzed using the gone concern approach in addition to the going concern approach.

In addition, the Volkswagen Bank GmbH Group uses a system of limits derived from the risk-bearing capacity analysis to specifically manage risk cover capital in accordance with the level of risk tolerance determined by the Management.

The establishment of the risk limit system as a core component of capital allocation limits the risk at different levels, thereby safeguarding the economic risk-bearing capacity of the Volkswagen Bank GmbH Group. Risk-taking potential is determined from the available equity and earnings components subject to various deductions. In line with the risk tolerance of the Management of Volkswagen Bank GmbH, only a portion of this risk-taking potential is specified as a risk ceiling in the form of an overall risk limit. The overall risk limit is apportioned to counterparty default risk, residual value risk, market risk, liquidity risk and operational risk for the purposes of operational monitoring and control. In this process, the limit allocated to counterparty default risk, itself an overarching category of risk, is subdivided into individual limits for credit risk, shareholder risk, issuer risk and counterparty risk.

In a second step, the limits for the risk categories (with the exception of those for shareholder risk, issuer risk, counterparty risk and liquidity risk [funding risk]) are broken down and allocated at the level of the branches and Volkswagen Bank Polska S.A.

The limit system provides the Management with a tool that enables it to meet its strategic and operational corporate management responsibilities in accordance with statutory requirements.

The overall economic risk of the Volkswagen Bank GmbH Group as of September 30, 2016 amounted to €982 million. The apportionment of this total risk by individual risk category was as follows:

DISTRIBUTION OF RISKS BY TYPE OF RISK

as of September 30, 2016

	€ MILLION		PROPORTION (PERCENT)	
	Sept. 30, 2016	Dec. 31, 2015	Sept. 30, 2016	Dec. 31, 2015
Risk category				
Credit risk	540	493	55	57
Shareholder, issuer and counterparty risk	3	4	0	1
Residual value risk	4	2	0	0
Earnings risk	231	216	24	25
Market risk	15	13	2	2
Liquidity risk (funding risk)	0	0	0	0
Operational risk	140	89	14	10
Other risks[1]	49	44	5	5
Total	982	861	100	100

1 Global amount for material non-quantifiable risks: reputational risk and strategic risk.

The risk-taking potential of €3.0 billion as of September 30, 2016 comprised reported equity plus the forecast result for the next twelve months (overall €7.3 billion) less regulatory minimum own funds requirements (€3.9 billion) and other adjustment items (€0.4 billion). As of September 30, 2016, 33% of risk-taking potential was utilized by the risks outlined above. In the period January 1, 2016 to September 30, 2016, the maximum utilization of the risk-taking potential in accordance with Pillar II was 54%.

Up to December 31, 2016, there were no indications of any material changes in the utilization of the risk-taking potential.

In addition to determining the risk-bearing capacity in a normal scenario, the Volkswagen Bank GmbH Group also conducts bank-wide stress tests and reports the results directly to the Management. Stress tests are used to examine the potential impact from exceptional but plausible events on the risk-bearing capacity and earnings performance of Volkswagen Bank GmbH. The purpose of these scenarios is to facilitate early identification of those risks that would be particularly affected by the trends simulated in the scenarios so that any necessary corrective action can be initiated in good time. The stress tests include both historical scenarios (such as a repeat of the financial crisis in the years 2008 to 2010) and hypothetical scenarios (such as a global economic downturn or a sharp drop in sales in the Volkswagen Group). In addition, inverse stress tests are used to identify what events could represent a threat to the ability of the Volkswagen Bank GmbH Group to continue as a going concern.

The calculations of risk-bearing capacity confirmed that all material risks that could adversely impact the financial position or financial performance were adequately covered by the available risk-taking potential at all times. In the reporting period, the Volkswagen Bank GmbH Group managed risk such that the utilized risk cover capital was below the overall risk limit set internally. The stress tests did not indicate any need for action.

RISK CONCENTRATIONS

The Volkswagen Bank GmbH Group is a captive financial services provider in the automotive sector. The business model, which focuses on promoting vehicle sales for the different brands in the Volkswagen Group, causes concentrations of risk, which can take various forms.

Concentrations of risk can arise from an uneven distribution of activity in which

- just a few borrowers/contracts account for a large proportion of the loans (counterparty concentrations)
- a small number of sectors account for a large proportion of the loans (sector concentrations)
- many of the loans are to businesses within a defined geographical area (regional concentrations)
- loans/receivables are secured by just one type of collateral or by a limited range of collateral types (collateral concentrations)
- residual values subject to risk are limited to a small number of vehicle segments or models (residual value concentrations), or
- Volkswagen Bank GmbH's income is generated from just a few sources (income concentrations).

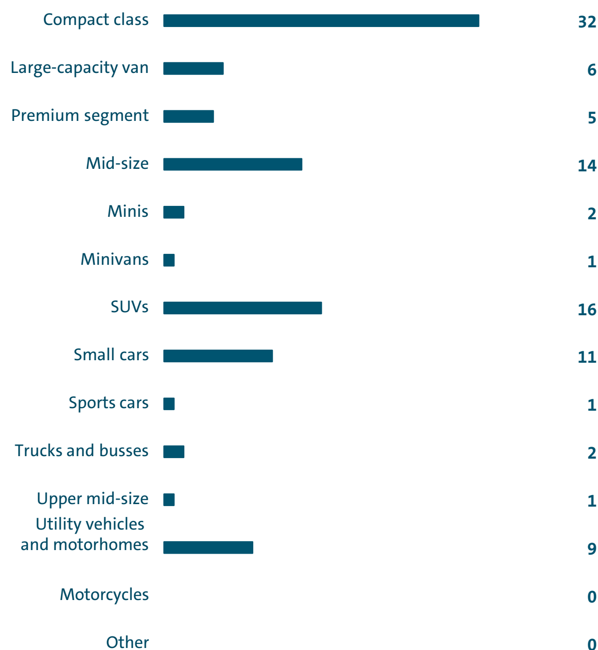
One of the objectives of the Volkswagen Bank GmbH Group's risk policy is to reduce such concentrations by means of broad diversification.

Counterparty concentrations from customer business are only of minor significance in the Volkswagen Bank GmbH Group because of the large proportion of business accounted for by retail lending. From a regional perspective, the Volkswagen Bank GmbH Group has a concentration of business in the German market, but looks to achieve broad nationwide diversification within the country.

In contrast, sector concentrations in the dealer business are part of the nature of the business for a captive provider and these concentrations are therefore individually analyzed. Overall, no particular impact has been identified, even in periods of economic downturn like the crisis experienced in recent years.

Likewise, a captive provider cannot avoid collateral concentrations because the vehicle is the predominant collateral asset by virtue of the business model. Risks can arise from concentrations of collateral if downward pricing trends in used vehicle markets or segments lead to lower proceeds from the recovery of assets and, as a consequence, there is a fall in the value of the collateral. Nevertheless, in terms of the vehicles used as collateral, Volkswagen Bank GmbH Group enjoys a broad diversification across all vehicle segments (see following diagram) based on a large range of vehicles from the different brands in the Volkswagen Group.

COLLATERAL STRUCTURE AS OF SEPTEMBER 30, 2016
figures in %



This broad vehicle diversification also means that there is no residual value concentration in the Volkswagen Bank GmbH Group.

Income concentration arises from the very nature of the business model. The Volkswagen Bank GmbH Group's particular role in which it helps to promote sales in the Volkswagen Group gives rise to certain dependencies that directly affect income growth.

RISK REPORTING

A detailed risk management report is submitted to the Management of Volkswagen Bank GmbH on a quarterly basis and to the Annual General Meeting. The starting point for the risk management report is risk-bearing capacity because of its importance from a risk perspective for the successful continued existence of the business as a going concern. To this end, the derivation of the available risk-taking potential, the utilization of limits and the current percentage allocation of the overall risk to the individual risk categories is also presented. In addition, Group Risk Management reports on counterparty default risk, direct residual value risk, market risk, liquidity risk and operational risk, both at an aggregate level and – mostly for markets – in detail. These reports include quantitative information (financial data) and also qualitative elements in the form of an assessment of the current situation and expected developments, including recommendations for action where appropriate. Additional reports are produced for specific risk categories. Ad hoc reports are generated as needed to supplement the system of regular reporting.

The high quality of the information contained in the risk management reports about structures and trends in the portfolios is maintained by a process of constant refinement and ongoing adjustment in line with current circumstances.

NEW PRODUCT AND NEW MARKET PROCESS

Before launching new products or commencing activities in new markets, the Volkswagen Bank GmbH Group first runs through its new product and new market process. All the units involved (such as Risk Management, Controlling, Accounting, Legal Affairs, Compliance, Treasury, IT) are integrated into the process. The process for every new activity involves the preparation of a written concept, which includes an analysis of the risks associated with the new product or market and a description of the possible implications for management posed by the risks. Responsibility for approval or rejection lies with the relevant members of the Management of Volkswagen Bank GmbH, the Board of Management of Volkswagen Financial Services AG and, in the case of new markets, also with the members of the Supervisory Board of Volkswagen Financial Services AG.

OVERVIEW OF RISK CATEGORIES

Financial risks	Non-financial risks
Counterparty default risk	Operational risk
Market risk	Compliance and conduct risk
Liquidity risk	Outsourcing risk
Residual value risk	Model risk
Earnings risk	Strategic risk
	Reputational risk

FINANCIAL RISKS

Counterparty Default Risk

Counterparty default risk refers to a potential negative variance between actual and forecast counterparty risk outcomes. The forecast outcome is exceeded if the loss incurred as a consequence of defaults or changes in credit rating is higher than the expected loss.

In the Volkswagen Bank GmbH Group, counterparty default risk encompasses the following risk categories: credit risk, counterparty risk, issuer risk, country risk and shareholder risk.

Credit Risk

Credit risk is defined as the danger of incurring losses as a result of defaults in customer business, specifically the de-

fault of the borrower or lessee. Loans to and receivables from entities in the Volkswagen Group are also included in the analysis. The default is caused by the borrower's or lessee's insolvency or unwillingness to pay. This includes a situation in which the counterparty does not make interest payments or repayments of principal on time or does not pay the full amounts.

Credit risk, which also includes counterparty default risk in connection with leases, accounts for the greatest proportion of risk exposures in the counterparty default risk category by some distance.

The aim of a systematic credit risk monitoring system is to identify potential borrower or lessee insolvencies at an early stage, initiate any corrective action in respect of a potential default in good time and anticipate possible losses by recognizing appropriate write-downs or provisions.

If a loan default materializes, this represents the loss of a business asset, which has a negative impact on financial position and financial performance, depending on the amount of the loss. If, for example, an economic downturn leads to a higher number of insolvencies or greater unwillingness of borrowers or lessees to make payments, the recognition of a higher write-down expense is required. This in turn has an adverse effect on operating profit.

Risk identification and assessment

Lending or credit decisions at Volkswagen Bank GmbH are made primarily on the basis of the borrower credit check. These credit checks use rating or scoring systems, which provide the relevant departments with an objective basis for reaching a decision on a loan or a lease.

A set of procedural instructions outlines the requirements for developing and maintaining the rating systems. The Bank also has a rating manual which specifies how the rating systems are to be applied as part of the loan approval process. Similarly, other written procedures specify the parameters for developing, using and validating the scoring systems in the retail business.

To quantify credit risk, an expected loss (EL) and an unexpected loss (UL) are determined at portfolio level for each entity. The UL is the value at risk (VaR) less the EL. The calculations use an asymptotic single risk factor model (ASRF model) in accordance with the capital requirements specified by the Basel Committee on Banking Supervision (Gordy formula) taking into account the credit quality assessments from the individual rating and scoring systems used.

Rating systems for corporate customers

The Volkswagen Bank GmbH Group uses rating systems to assess the credit quality of corporate customers. These assessments take into account both quantitative factors (mainly data from annual financial statements) and qualitative factors (such as the prospects for future business growth, quality of management, market and industry environment, and the customer's payments record). When the credit assessment has been completed, the customer is assigned to a rating class, which is linked to a probability of default. A centrally maintained, workflow-based rating application is used for the most part to support this analysis of credit quality. The rating determined for the customer serves as an important basis for decisions on whether to grant or renew a loan and for decisions on provisions.

Scoring systems in the retail business

For the purposes of determining the credit quality of retail customers, scoring systems are incorporated into the processes for credit approval and for evaluating the existing portfolio. These scoring systems provide an objective basis for credit decisions. The systems use information about the borrower available internally and externally and estimate the probability of default for the requested loan, generally with the help of statistical methods based on historical data covering a number of years. An alternative approach adopted for smaller or low-risk portfolios also uses generic, robust scorecards and expert systems to assess the risk involved in credit applications.

To classify the risk in the credit portfolio, both behavioral scorecards and straightforward estimation procedures at risk pool level are used, depending on portfolio size and the risk inherent in the portfolio.

Supervision and review of retail and corporate systems

The models and systems supervised by Group Risk Management are regularly validated and monitored using standardized procedural models for validating and monitoring risk classification systems. The models and systems are adjusted and refined, as required. These review procedures are applied to models and systems for assessing credit quality and estimating the probability of default (such as rating and scoring systems) and to models used for estimating loss given default and estimating credit conversion factors.

In the case of the retail models and systems for credit assessment supervised by local risk management units outside Germany, Group Risk Management reviews the quality of these models and systems on the basis of the locally implemented validation processes, determines action plans in collaboration with the local risk management units if a need for action is identified and monitors the implementation of the action plans. In the validation process, particular attention is paid to a review of the discriminant power of the models and an assessment of whether the model calibration is appropriate to the risk. The models and systems for corporate customers are handled in the same way, although a centralized approach is used for their supervision and validation.

Collateral

The general rule is that credit transactions are secured by collateral to an extent that is commensurate with the risk. In

addition, overarching rules specify the requirements that must be satisfied by collateral, the evaluation procedures and the evaluation bases. Further local regulations (collateral policies) set out specific values and special regional requirements that must be observed.

The values in the collateral policies are based on historical data and experience accumulated by experts over many years. As the operating activities of the Volkswagen Bank GmbH Group are focused on retail financing, dealer financing and the leasing of vehicles, the vehicles themselves are hugely important as collateral assets. For this reason, trends in the market values of vehicles are closely monitored and analyzed. Procedures provide for adjustments to evaluation systems and vehicle remarketing processes if there are substantial changes in the market values of vehicles.

Group Risk Management also carries out regular quality assurance tests on local collateral policies. This includes a review of collateral values and implementation of any necessary adjustments.

Provisions

The calculation of provisions is based on the incurred loss model in accordance with IAS 39 and is also derived from the rating and scoring processes.

With regard to impaired loans and receivables, a distinction is also made between significant and insignificant loans and receivables. Specific provisions are recognized for significant impaired loans and receivables, whereas specific provisions evaluated on a group basis are recognized for insignificant impaired loans and receivables. Portfolio (global) provisions are recognized to cover impaired loans or receivables for which no specific provisions have been recognized.

The following average values have been determined for the aggregate active portfolio (i.e. portfolio of loans and receivables not in default) based on a time horizon of twelve months: probability of default (PD) of 2.9% (previous year: 3.4%); loss given default (LGD) of 23.7% (previous year: 23.4%); and total volume of loans and receivables based on the active portfolio of €38.6 billion (previous year: €36.0 billion).

Risk monitoring and control

Group Risk Management sets framework constraints for the management of credit risk. These constraints form the mandatory outer framework of the central risk management system, within which the divisions/markets can operate in terms of their business policy activities, planning, decisions, etc. in compliance with their assigned authority.

Appropriate processes are used to monitor all lending in relation to financial circumstances, collateral and compliance with limits, contractual obligations and internal and external conditions. To this end, exposures are transferred to a suitable form of supervision or support depending on risk content (normal, intensified or problem loan management). Approval limits determined by the Volkswagen Bank GmbH Group are also used to manage credit risk. These limits are specified separately for each individual branch and Volkswagen Bank Polska S.A.

A credit risk portfolio rating, together with analyses of the breakdown of expected and unexpected risk, are used to monitor risk at portfolio level. This rating brings together various risk measures into one indicator, facilitating comparability between the international portfolios in the Volkswagen Bank GmbH Group. The Group Risk Management and Credit Analysis units also conduct risk reviews in the companies if any problems become apparent.

Trends

Retail portfolio

In fiscal year 2016, further growth was achieved in the volume of loans and receivables in the Volkswagen Bank GmbH Group's retail business on the back of the established sales promotion program with the brands and continuous expansion of the fleet business. As in the previous year, the Germany portfolio was instrumental in driving growth based on its stable vehicle market environment. Overall, the credit risk in the retail portfolio of the Volkswagen Bank GmbH Group remained stable. The diesel issue in the Volkswagen Group did not have any impact on the retail portfolio of the Volkswagen Bank GmbH Group in 2016.

Corporate portfolio

The sustained economic recovery in European markets and a corresponding stabilization of vehicle markets had a positive effect on the corporate portfolio of the Volkswagen Bank GmbH Group in 2016. This trend is reflected in a rising volume of loans and receivables. In the UK branch, the fall in the value of the pound sterling led to a sharper contraction in the volume of loans and receivables measured in euros than in the equivalent volume figure in local currency. Overall, the credit risk in the corporate portfolio of the Volkswagen Bank GmbH Group remained stable. The diesel issue in the Volkswagen Group did not have any impact on the corporate portfolio of the Volkswagen Bank GmbH Group in 2016.

BREAKDOWN OF CREDIT VOLUME BY REGION
in € million

1 Europe excluding Germany

Counterparty/Issuer Risk

The Volkswagen Bank GmbH Group defines counterparty risk as the risk of financial loss that could arise from monetary investments or investments in marketable securities or notes if the counterparty fails to make payments of interest or repayments of principal as contractually required.

Similarly, issuer risk is the risk that the issuer of a financial product could become insolvent during the maturity of the product and, as a consequence, some or all of the invested capital, including the expected interest payments, has to be written off.

Counterparty risk arises in connection with interbank overnight and term deposits, derivatives and the purchase of pension fund units as part of the provision of pensions benefits for employees. Issuer risk results from the purchase of securities to optimize liquidity management and to fulfill statutory and/or regulatory requirements. The primary objective in the management of counterparty and issuer risk is to identify potential defaults in a timely manner, so that corrective action can be initiated at an early stage as far as possible. Another important objective is to ensure that the Bank only takes on risks within the approved limits.

If a counterparty or issuer risk were to materialize, this would represent the potential loss of a business asset, which would have a negative impact on financial position and financial performance, depending on the amount of the loss.

Risk identification and assessment

Both counterparty risk and issuer risk are recorded as components of counterparty default risk. Both risk categories are determined by using a Monte Carlo simulation to calculate the unexpected loss (value at risk and expected shortfall) and the expected loss from a normal scenario and stress scenarios.

Risk monitoring and control

To establish effective monitoring and control, volume limits are specified in advance for each counterparty and issuer. The Treasury Backoffice unit is responsible for monitoring compliance with these limits on a day-to-day basis. The volume limit is set at an appropriate, needs-driven level and is based on the credit assessment. The Credit Analysis department is responsible for the initial classification and then regular reviews. The Group Risk Management unit assesses counterparty and issuer risk on a monthly basis. The reporting of counterparty and issuer risk to the Management is included in the monthly market risk report and in the quarterly risk management report.

Country Risk

Country risk refers to risks in international transactions that are not attributable to the counterparty itself but that arise because of the counterparty's domicile in a country outside Germany. For example, political or economic trends caused by a crisis or difficulties affecting the entire financial system in the country concerned may mean that cross-border services involving the movement of capital cannot be carried out because of transfer problems attributable to action implemented by the foreign government in question. The Volkswagen Bank GmbH Group would need to take into account country risk, in particular in connection with funding and equity investment activities involving foreign companies and in connection with the lending business operated by the Bank's branch offices. Given the focus of business activities in Volkswagen Bank GmbH, there is little chance that country risk (such as foreign exchange risk or legal risk) will arise.

Volkswagen Bank GmbH is not usually involved in cross-border lending business, except in the case of intercompany loans. The conventional country risk analysis is not applicable to intercompany lending because, if the difficulties described above were to occur, the funding of the entities through lending could be extended if necessary, thereby ensuring that the entities could continue to operate in the strategic market concerned. For these reasons, there has been no need to establish limits related to the overall level of busi-

ness for countries or regions, for example, to limit transfer risk.

Shareholder Risk

Shareholder risk refers to the risk that losses with a negative impact on the carrying amount of an equity investment could be incurred after the contribution of capital or loans regarded as equity (e.g., silent contributions). In principle, the Volkswagen Bank GmbH Group only makes such equity investments to help it achieve its corporate objectives. The investments must therefore support its own operating activities and are intended to be held on a long-term basis.

If shareholder risk were to materialize in the form of a loss of fair value or even the complete loss of an equity investment, this would have a direct impact on relevant financial data. The net assets and financial performance in the Volkswagen Bank GmbH Group would be adversely affected by write-downs recognized in profit or loss.

Risk identification and assessment

Shareholder risk is quantified on the basis of the carrying amounts of the equity investments and a probability of default and loss given default assigned to each equity investment using an ASRF model. Simulations are also carried out involving stress scenarios with rating migrations (upgrades and downgrades) or complete loss of equity investments.

Risk monitoring and control

Equity investments are integrated into the annual strategy and planning process of the Volkswagen Bank GmbH Group. It exercises influence over the business and risk policies of the equity investments through its representation on the relevant ownership or supervisory bodies. However, responsibility for the operational use of the risk management tools lies with the entities themselves.

Market Risk

Market risk refers to the potential loss arising from adverse changes in market prices or parameters that influence prices. The Volkswagen Bank GmbH Group is exposed to significant market risk arising from changes in market prices that trigger a change in the value of open interest rate or currency transactions.

The objective of market risk management is to keep the financial losses arising from this category of risk as low as possible. With this in mind, the Management has agreed limits for this category of risk. If limits are exceeded, the situation is escalated on an ad hoc basis to the Management and the Asset Liability Management Committee (ALM Committee). Action to reduce risk is discussed and initiated by the ALM Committee.

As part of risk management activities, market risk is included in the monthly risk report with a transparent analysis based on value at risk (VaR), a calculation offsetting the total market risk against the loss ceiling set for the Volkswagen Bank GmbH Group and recommendations for targeted measures to manage the risk.

Interest Rate Risk

Interest rate risk refers to potential losses that could arise as a result of changes in market interest rates. It occurs because of interest rate mismatches between asset and liability items in a portfolio or on the balance sheet. The Volkswagen Bank GmbH Group is exposed to interest rate risk in its banking book.

Changes in interest rates that cause interest rate risk to materialize can have a negative impact on financial performance.

Risk identification and assessment

Interest rate risk for the Volkswagen Bank GmbH Group is determined as part of the monthly monitoring process using the value at risk (VaR) method with a 40-day holding period and a confidence level of 99%.

The model is based on a historical simulation and calculates potential losses taking into account 1,000 historical market fluctuations (volatilities). Negative interest rates can also be processed in the historical simulation and are factored into the risk assessment.

The VaR calculated for operational management purposes estimates potential losses under historical market conditions, but stress tests are also carried out for forward-looking situations in which interest rate exposures are subject to exceptional changes in interest rates and worst-case scenarios. The results from the simulations are analyzed to assess whether any of the situations could represent a serious potential risk. This process also includes the monthly quantification and monitoring of the changes in present value resulting from the interest rate shock scenarios of +200 basis points and –200 basis points, as specified by the German Federal Financial Supervisory Authority (BaFin).

The calculation of interest rate risk uses notional maturities to take into account early repayments under termination rights. The behavior of investors with indefinite deposits is analyzed using internal models and methods for managing and monitoring interest rate risk.

Risk monitoring and control

Treasury is responsible for the management of this risk on the basis of decisions made by the ALM Committee. Interest rate risk is managed by using interest rate derivatives at both micro and portfolio levels. The derivatives are recognized in the banking book. Group Risk Management is responsible for monitoring and reporting on interest rate risk.

A separate report on the latest position regarding interest rate risk in the Volkswagen Bank GmbH Group is submitted to the Management each month.

Currency Risk

Currency risk arises from mismatches between the amounts of asset and liability items denominated in foreign currency. However, open-ended foreign currency exposures of this nature are only permitted in individual cases.

If currency risks were to materialize, this could lead to losses in all items affected by a foreign currency.

Fund Price Risk

The risk in connection with fund investments arises from possible changes in market prices. Fund price risk describes the risk that changes in market prices will cause the value of portfolios of securities to fall, thereby giving rise to a loss.

The Volkswagen Bank GmbH Group is exposed to fund price risk arising from its employee post-employment benefit arrangements that are funded by pension plan assets consisting of fund investments. The Volkswagen Bank GmbH Group has undertaken to meet these pension obligations if the employees' guaranteed entitlements can no longer be satisfied from the pension fund.

Trends

Overall, market risk remained stable during the reporting period. The quantified risk remained within the specified limits at all times.

Liquidity Risk

Liquidity risk is the risk of a negative variance between actual and expected cash inflows and outflows.

Liquidity risk is defined as the risk of not being able to meet payment obligations in full or when due, or – in the event of a liquidity crisis – the risk of only being able to raise funding at higher market rates or only being able to sell assets at a discount to market prices. This results in a distinction between illiquidity risk (day-to-day cash flow risk including deposit withdrawal/commitment drawdown risk and the risk of delayed repayment of loans on maturity), funding risk (structural liquidity risk) and market liquidity risk.

The primary objective of liquidity management in the Volkswagen Bank GmbH Group is to safeguard the ability of the Group to meet its payment obligations at all times. To this end, Volkswagen Bank GmbH holds liquidity reserves in the form of securities deposited in its operational safe custody account with Deutsche Bundesbank. Standby lines of credit at other banks are also available to protect against unexpected fluctuations in cash flows. There are no plans to make use of these standby lines of credit; their sole purpose is to serve as backup to safeguard liquidity.

If liquidity risk were to materialize, funding risk would result in higher costs and market liquidity risk would result in lower selling prices for assets, both of which would have a negative impact on financial performance. The consequence of illiquidity risk in the worst-case scenario is insolvency caused by illiquidity. Liquidity risk management in the Volkswagen Bank GmbH Group ensures that this situation does not arise.

Risk identification and assessment

The expected cash flows in the Volkswagen Bank GmbH Group are brought together and evaluated by the Treasury unit.

The Group Risk Management unit is responsible for identifying and recording liquidity risk. Stress tests are applied to funding matrices using a scenario approach with scenario triggers from the Bank itself or the market, or a combination of the two. Two approaches are used to determine the parameters for these stress scenarios. The first approach uses observed historical events and specifies different degrees of impact from hypothetical, but conceivable events. To quantify the funding risk, this approach takes into account the relevant aspects of illiquidity risk and changes in spreads driven by credit ratings or the market. In the second approach, to ensure there is appropriate liquidity management, Treasury also prepares four different funding matrices, carries out cash flow forecasts and uses this information to determine the relevant range of liquidity coverage.

Risk monitoring and control

To manage liquidity, the Operational Liquidity Committee (OLC) holds meetings every two weeks at which it monitors the current liquidity situation and the range of liquidity coverage. It decides on funding measures and prepares any necessary decisions for the decision-makers.

Group Risk Management communicates the main risk management information and relevant early warning indicators relating to illiquidity risk and funding risk. As far as illiquidity risk is concerned, these indicators involve appropriate threshold values for determined degrees of utilization over various time horizons, taking into account access to relevant sources of funding. The indicators relating to funding risk are based on potential funding costs, which are monitored using a system of limits.

A further strict requirement imposed under banking regulation is the need to provide a highly liquid cash buffer and appropriate liquidity reserves to cover any liquidity requirements over seven-day and thirty-day time horizons. For this reason, a contingency plan with an appropriate list of action points for obtaining liquidity has already been drawn up so that it can be implemented in the event of any liquidity squeeze.

Risk communication

As part of risk communications, the members of the Management of Volkswagen Bank GmbH are informed on a daily basis of the outstanding funding, open confirmed bank credit lines and the value of the securities in the operational safe custody account held with Deutsche Bundesbank.

The Management of Volkswagen Bank GmbH is informed of the prevailing liquidity position on a monthly basis.

Trends
Liquidity risk has been significantly affected by the diesel issue, which has been to the fore since September 2015. Nevertheless, liquidity risk at the level of Volkswagen Bank GmbH has remained stable overall.

Funding risk always remained within the specified limits.

Residual Value Risk

Residual value risk arises from the fact that the actual market value for a lease asset at the time of remarketing could be lower than the residual value calculated at the inception of the lease. On the other hand, there is an opportunity in that the remarketing could generate proceeds greater than the calculated residual value.

A distinction is made between direct and indirect residual value risk in relation to the bearer of this risk. Direct residual value risk refers to residual value risk borne directly by the Volkswagen Bank GmbH Group (contractually determined). An indirect residual value risk arises if the residual value risk has been transferred to a third party (such as a dealer) on the basis of a residual value guarantee. In such cases, the initial risk is a counterparty default risk in respect of the residual value guarantor. If the residual value guarantor defaults, the residual value risk reverts to the Volkswagen Bank GmbH Group.

The objective of residual value risk management is to keep the risks within the agreed limits. If a residual value risk materializes, the Bank may have to recognize an exceptional write-down or a loss on disposal of the asset concerned, resulting in a negative impact on financial performance.

Risk identification and assessment
Direct residual value risks are quantified on the basis of expected loss (EL) and unexpected loss (UL). The EL equates to the difference between the latest forecast remarketing proceeds as of the measurement date and the contractual residual value specified at the inception of the lease for each vehicle. Other parameters such as remarketing costs are also taken into account in the calculation. The portfolio EL is calculated by aggregating the individual ELs for all the vehicles.

To determine the UL, the change is measured between the projected residual value one year before the end of the lease and the actual selling price achieved (adjusted for damage and mileage variances). In a first step, the change in value is determined for each individual lease for each period. However, given the size of the portfolio and the huge number of vehicles, systematic risk is significant and a second step is therefore carried out in which the average change in value compared with projected residual values is determined over several periods. The resulting markdown is calculated using the quantile function of the normal distribution with a specified confidence level.

The UL is calculated by multiplying the latest projected residual value by the markdown. This value is calculated independently of the EL and at individual lease level for each vehicle in the portfolio. As in the calculation of the EL, the portfolio UL is determined by aggregating the ULs for all the vehicles. This figure is generated quarterly. The results from the calculation of the EL and UL are fed in to the assessment of the risk situation, e.g. they are one of the factors used in assessing the adequacy of the provisions for risks and are included in the calculation of risk-bearing capacity.

In the case of indirect residual value risk, the method used to quantify the risk is generally similar to that used for direct residual value risk but also takes into account further risk parameters (dealer default and other factors specific to this category of risk).

The general requirements for developing, using and validating the risk parameters for direct and indirect residual value risk are laid down in a set of procedural instructions.

Risk monitoring and control
Group Risk Management monitors residual value risk within the Volkswagen Bank GmbH Group.

As part of risk management procedures, the adequacy of the provision for risks and the potential residual value risk are regularly reviewed in respect of direct residual value risk; residual value opportunities are disregarded in the recognition of the provision for risks.

Because of the distribution of the risks, an analysis based on individual leases does not always fully cover the assumed risks during the term of the lease. This is because of the difference between the residual value curve (degressive) and the incoming payments curve (linear). As a result, where risks have already been identified, the risk amounts allocated to the residual maturity must still be earned in the future and added to impairment losses (in accordance with IAS 36).

Based on the resulting potential residual value risk, various measures are initiated as part of a proactive risk management approach to limit the residual value risk. Residual value recommendations for new lease originations must take into account prevailing market circumstances and future influences. There are also a number of stress tests for direct residual value risks for creating a comprehensive picture of the risk sensitivity of residual values. These stress tests are carried out by experts with the involvement of risk specialists at head office and in the local units. Indirect residual value risks faced by the Volkswagen Bank GmbH Group are subject to plausibility checks and are assessed from the perspectives of risk amount and significance.

As part of risk management activities, Group Risk Management regularly reviews the potential indirect residual value risk and the adequacy of the associated provision for risks. Based on the potential indirect residual value risk de-

termined by these activities, various measures are initiated in close collaboration with the brands and the dealer organization to limit the risk.

Trends

Within the Volkswagen Bank GmbH division, residual value risks arise at the branches in France, Italy, Ireland and Portugal and at Volkswagen Bank Polska S.A. Steady year-on-year growth in the number of contracts was evident in almost all markets, driven by the recovery in vehicle markets in Europe. The most significant growth driver was the Ireland market. However, there are only material direct residual value risks at the branch in France because the volume in the other branches is still very low or the residual values have been set at such a conservative level that it can be assumed the customers will take over the vehicle at the end of the lease term. The diesel issue at the Volkswagen Group only had a marginal impact on the residual value portfolio of the Volkswagen Bank GmbH Group.

Earnings Risk (Specific Profit or Loss Risk)

Earnings risk refers to the risk that actual values will vary from the budgeted values for certain items on the income statement that are not already covered by the other categories of risks described elsewhere. Earnings risk includes the following risks:

- unexpectedly low fees and commissions (fee and commission risk);
- unexpectedly high costs (cost risk);
- excessively high income targets for new and existing business volume (sales risk); and
- unexpectedly low investment income.

The objective is to regularly analyze and monitor the potential risk associated with earnings risk to ensure that variances compared with budgeted values are identified at an early stage and any necessary corrective action is initiated. If the risk were to materialize, this would reduce income or increase costs and thereby also adversely impact operating profit.

Risk identification and assessment

The Volkswagen Bank GmbH Group quantifies earnings risk using a parametric earnings at risk (EaR) model with the confidence level specified in the calculation of risk-bearing capacity and a one-year forecast period.

The relevant income statement items provide the basis for these calculations. The estimates for earnings risk are then based on two perspectives: firstly, the observed, relative variances between target and actual values; secondly, the volatility and interdependencies between the individual items. Both components are incorporated into the EaR calculation.

Risk monitoring and control

During the course of the year, changes in the actual values at market level for the earnings risk exposures are compared against the forecast values. This comparison is included in the standard reporting procedure carried out by Controlling.

The results from the quarterly quantification of earnings risk are fed into the calculation of risk-taking potential as a deduction from risk-bearing capacity. The results are monitored by Group Risk Management.

NON-FINANCIAL RISKS

Operational Risk

Operational risk (OpR) is defined as the risk of loss resulting from inadequate or failed internal processes (process risk), people (HR risk) or systems (technological risk), or resulting from external events (third-party risk). This definition includes legal risk.

Other categories of risk, such as reputational or strategic risk, do not fall within the scope of operational risk because they are analyzed separately.

The objective of operational risk management is to present operational risks transparently and initiate precautionary or corrective measures with a view to preventing or, when this is not possible, mitigating the risks or losses. If an operational risk materializes, this represents an operational loss with the resulting loss of a business asset, which has a negative impact on financial position and financial performance, depending on the amount of the loss.

The operational risk strategy specifies the focus for the management of operational risk; the operational risk manual sets out the implementation process and allocates responsibilities.

Risk identification and assessment

Operational risks or losses are identified and assessed by local experts working in pairs (assessor and approver) with the help of two operational risk tools: a risk self-assessment and a loss database.

The risk self-assessment is used to determine a monetary assessment of future potential risks. A standardized risk questionnaire is provided once a year for this purpose. The local experts use these questionnaires to determine and record the details for various risk scenarios. The details include the possible amount of the risk and the probability of occurrence, in each case with typical and maximum figures.

The central loss database is used to ensure that information about monetary operational losses is collected internally on an ongoing basis and the relevant data is stored. A standardized loss form is made available to the local experts to aid this process. The experts use this form to determine and record the relevant data, including the amount and cause of the loss.

Risk monitoring and control

Operational risk is managed by the companies/divisions (operational risk units) on the basis of the guidelines in force and the requirements laid down by the special operational risk units responsible for specific risk categories. To this end, local management decides whether future risks or losses are to be ruled out (risk prevention), mitigated (risk mitigation), consciously accepted (risk acceptance) or transferred to third parties (risk transfer).

The Group Risk Management unit checks the plausibility of the information provided by the companies/divisions in the risk self-assessments, reviews the reported loss events and then initiates any necessary corrective action, reviews the operational risk system to ensure it is fully functioning and instigates appropriate modifications as required. This includes, in particular, the integration of all operational risk units, a review to check compliance with the risk sub-strategies for operational risks and a review of the methods and procedures used for risk measurement.

Communications relating to operational risks are provided quarterly as part of the risk management reports. The quarterly details are supplemented by an annual operational risk report in which the main events in the year are presented and assessed again on a coherent basis. Ad hoc reports are issued in addition to the regular reports provided that the relevant specified criteria are satisfied.

Trends

The increase in operational risk in the past was based on a number of factors, including the growth in the business of Volkswagen Bank GmbH, also after taking legal risk into account. As of November 2016, an amount of €257 million had been recognized as provisions for legal risks.

Training and briefing sessions were carried out to continue to raise awareness of operational risk in Volkswagen Bank GmbH. These activities led to better recording of loss events. Experience and information gained about past loss events also means that potential future risks can be assessed more completely and more accurately.

Compliance and Conduct Risk

At Volkswagen Financial Services AG, compliance risk encompasses all risks that could arise from non-compliance with statutory rules and regulations or other official or regulatory requirements, or that could be caused by a breach of internal company regulations.

Separately from compliance risk, conduct risk is defined as the risk arising from inadequate conduct by the institution toward the customer, unreasonable treatment of the customer or provision of advice using products that are not suitable for the customer.

Volkswagen Financial Services AG is taking account of both categories of risk by setting up a local compliance function and this function is working toward specifying and implementing risk-mitigating measures.

To counter compliance and conduct risks, the compliance function is committed to ensuring compliance with laws, other legal requirements, internal rules and self-proclaimed values, and fostering an appropriate compliance culture.

As a component of the compliance function, the role of the compliance officer is to work toward implementing effective procedures to ensure compliance with key and core legal rules and regulations for the institution and toward establishing appropriate controls. This will be achieved, in particular, by specifying mandatory compliance requirements for legal stipulations classified as material. These requirements include documenting responsibilities and processes, establishing controls to the extent required and raising employee awareness of pertinent rules so that employees comply with the rules as a matter of course, reflecting a fully functioning compliance culture.

Further regular activities are also nurturing the emergence of a compliance culture. These activities include, in particular, constantly promoting the Volkswagen Group's Code of Conduct, raising employee awareness on a risk-oriented basis (e.g. tone from the top, face-to-face training, e-learning programs, other media-based activities), carrying out communications initiatives, including distributing guidelines and other information media, and participating in compliance programs.

The compliance function has been set up on a decentralized basis. The departments are responsible for complying with the rules and regulations in their respective areas of activity. A compliance theme coordinator is being appointed for all key and core rules and regulations. The coordinator is responsible for adhering to and implementing the defined compliance requirements (such as documenting responsibilities, setting up controls, raising awareness and training employees).

Using the control plans and control documentation as a basis, the compliance function checks whether the implemented controls are appropriate. In addition, the findings from various audit activities will be used to evaluate whether there are indications that the implemented compliance requirements are ineffective, or whether the audits have identified material residual risks on the basis of which further action needs to be determined.

The compliance officer is responsible for coordinating ongoing legal monitoring, the purpose of which is to ensure that new or amended legal regulations and requirements are identified promptly. For their part, the compliance theme coordinators must work in collaboration with the legal department and the various other departments to implement measures aimed at identifying new or amended regulations and requirements relevant to their areas of responsibility at an early stage and, if such relevance is established, furnishing an analysis of materiality for the Company. The compliance

theme coordinators notify the compliance officer of any regulations and requirements that have been identified immediately.

The internal Compliance Committee will regularly conduct a materiality analysis on the basis of the outcomes from this legal monitoring. After taking into account the evaluated compliance risks, the Compliance Committee will make a decision on the materiality of new legal requirements applicable to the Bank. Compliance risk primarily includes the risk of a loss of reputation vis-à-vis the general public or supervisory authorities and the risk of material financial loss.

Currently, the following specific legal fields have been determined as being generally material from the perspective of the Group:

- prevention of money laundering and terrorist financing,
- prevention of corruption and other criminal acts,
- data protection,
- consumer protection,
- securities trading law,
- banking supervisory law, and
- antitrust law.

The compliance requirements for the corporate group are specified centrally and must be implemented autonomously in the local companies. Any deviation from the minimum requirements or guidelines is only possible if accompanied by a description of the reasons (such as local statutory requirements) and only in consultation with, and with the consent of, the holding company compliance function.

The holding company compliance function will receive regular reports and carry out on-site visits on a risk-oriented basis to ensure that the local compliance units are meeting their responsibilities.

To meet the statutory reporting requirements of the compliance function, the compliance officer must submit to the Management both regular reports on the outcome of the meetings of the Compliance Committee and ad hoc reports as necessary (for example, if control plans are not prepared by the required deadline).

The Management will also receive an annual compliance report and other comparable reports on an ad hoc basis, as required. The annual compliance report will contain a presentation of the appropriateness and effectiveness of the compliance requirements implemented to ensure compliance with key and core legal regulations and requirements.

Risk from Outsourcing Activities

Outsourcing describes a situation in which another entity (the outsourcee) is engaged to carry out activities and processes in connection with the provision of services that would otherwise be carried out by the outsourcing entity itself.

A distinction needs to be made between outsourcing and one-time or occasional procurement from third parties of goods or services, or services that are typically obtained from a supervised entity and, because of the actual circumstances involved or legal requirements, cannot usually be supplied by the buying entity itself, either at the time of the purchase from the third party or in the future.

The objective of outsourcing risk management is to identify and minimize the risks from all outsourcing. As part of outsourcing management and detailed monitoring, measures may be initiated, where appropriate, to monitor a variance from an identified risk and ensure that the original risk position associated with an outsourced activity can be restored.

Ultimately, a variance from a determined risk may mean that the service provider has to be changed or, if possible and strategically desirable, the outsourcing arrangement ended. In this case, the activities may be performed by the Bank itself or may be eliminated entirely.

Risk identification and assessment

Risks arising in connection with outsourced activities are identified by examining the circumstances and performing a risk analysis. In the first step, an examination of the circumstances is used to establish whether the planned activity constitutes procurement from a third-party supplier or an outsourcing arrangement. The risk analysis uses various criteria to determine the risk content in an outsourcing arrangement. The outcome is the classification of the outsourcing arrangement as material or immaterial. Material outsourcing arrangements are subject to more stringent levels of monitoring and control as well as special and stricter contractual provisions.

Risk monitoring and control

The risks from outsourcing activities are documented as part of operational risk. To ensure effective management of outsourcing risk, the Volkswagen Bank GmbH Group has issued a framework policy specifying the constraints that outsourcing arrangements must observe. Before any activity is outsourced, a risk analysis must be prepared to determine the risk in each case. This analysis procedure is one of the components of the constraints and ensures that an adequate level of monitoring and control is applied. The framework policy also specifies that all outsourced activities must be agreed with the Group Outsourcing Coordination unit. This coordination unit is therefore informed about all outsourcing activities and the associated risks and communicates quarterly on the risks to the Management.

In addition, all risks arising from outsourcing activities are subject to risk monitoring and control through the operational risk loss database and the annual risk self-assessment.

Model Risk

Model risk arises from inaccuracies in the risk values and must be taken into account, particularly in the case of underestimated risk and complex models.

Depending on the complexity of the model, model risk can occur in a number of areas of model development and application.

Potential model risks in the risk models are assessed by the model coordinator on a qualitative basis in an annual model risk process. The objective is to verify that the risks are covered by own funds.

The assessment is carried out using the following criteria: “simple”, “transparent”, “conservative”. If the presence of model risk is demonstrated, the model risk drivers are identified using a further qualitative assessment. A review is then carried out to establish whether the risk drivers can be minimized with appropriate action and/or whether quantitative backing with own funds is required.

Strategic Risk

Strategic risk is the risk of a direct or indirect loss arising from strategic decisions that are flawed or based on false assumptions.

Strategic risk also includes all risks that result from the integration/reorganization of technical systems, personnel or corporate culture (integration/reorganization risk). These risks may be caused by fundamental decisions about the structure of the business made by the Management in relation to the positioning of the company in the market.

The objective of the Volkswagen Bank GmbH Group is to manage its acceptance of strategic risk enabling it to systematically leverage earnings potential in its core business. In the worst-case scenario, a materialization of strategic risk could jeopardize the continued existence of the Bank as a going concern.

Strategic risk is recognized quantitatively by applying a deduction to aggregate risk cover in the calculation of risk-bearing capacity.

Reputational Risk

Reputational risk refers to the risk that an event or several successive events could cause reputational damage (in the eyes of the general public), which in turn could limit current and future business opportunities or activities (potential earnings), thereby leading to an indirect adverse financial impact (customer base, sales, funding costs, etc.) and/or direct financial losses such as penalties, litigation costs, etc.

The responsibilities of the Corporate Communications unit include avoiding negative reports in the press or similar announcements that could inflict damage on the reputation of the Company. If this is unsuccessful, the unit is then responsible for assessing the situation and initiating appropriate communications aimed at specific target groups to limit the reputational damage as far as possible. The strategic objective is therefore to prevent or reduce any negative variance between actual reputation and the level of reputation the Bank expects. A loss of reputation or damage to the Bank’s image could have a direct impact on financial performance.

Reputational risk is recognized quantitatively by applying a markdown in the calculation of risk-bearing capacity. This global approach is reassessed each year from a qualitative perspective.

SUMMARY

The Volkswagen Bank GmbH Group accepts risks on a responsible basis as part of its operating activities. This approach is based on a comprehensive system for identifying, measuring, analyzing, monitoring and controlling risks, which is part of a holistic risk- and return-oriented management system. Risk-bearing capacity was maintained at all times in 2016. We do not believe that there are any risks to the continued existence of our business as a going concern.

The system was once again subject to a process of continuous refinement in 2016, for example by adjusting methods, models, systems, processes and IT.

The Volkswagen Bank GmbH Group will continue to invest in optimizing its comprehensive control system and risk management systems in order to meet the business and statutory requirements for the management and control of risks.

FORECAST OF MATERIAL RISKS

Credit Risk Forecast

A stable risk position is predicted for 2017 overall. This steady position should be supported by a further stabilization in the economic environment and the continued recovery in European markets. We do not anticipate any impact from the diesel issue on credit risk.

Market Risk Forecast

We are expecting a generally stable market price risk situation for fiscal year 2017, based on the expected relatively stable interest rate environment in the eurozone.

Liquidity Risk Forecast

The future risk trend very much depends on how the diesel issue evolves and on how the Bank refines the management approach in connection with the funding structure. If, for example, the capital market cannot be used as currently planned, it will be necessary to switch to other, generally shorter-term, sources of funding. This could then be reflected in a higher funding cost risk and also in a higher insolvency risk.

Residual Value Risk Forecast

We expect the volume of contracts to continue to grow in fiscal year 2017. The main drivers behind this are the implemented growth program, continued economic recovery in the markets and further expansion in the fleet business. The diesel issue should not affect the residual value portfolio in 2017.

Operational Risk Forecast

Based on future business growth and the trend in operational risk as described in the risk report, we anticipate a constant to moderately rising level of risk. In this context, we expect the effectiveness of fraud protection to remain stable and the high level of quality in processes and in staff skills and qualifications to be maintained.

Human Resources Report

Promoting a culture of open feedback and discussion is a key priority in the ROUTE2025 corporate strategy.

HEADCOUNT

As of December 31, 2016, 2,786 employees (previous year: 2,638) of Volkswagen Financial Services AG were assigned to Volkswagen Bank GmbH's business units under staff leasing arrangements.

Other personnel continue to be employed directly by Volkswagen Bank GmbH under legacy employment contracts. These employees numbered 1 in Germany as of December 31, 2016 (previous year: 2). The branches of Volkswagen Bank GmbH employed 955 staff (previous year: 853); Volkswagen Bank Polska S.A. had 337 employees (previous year: 307).

EMPLOYEES

We believe it is a responsibility of Volkswagen Financial Services AG to offer our employees the environment you would expect of a first-rate employer. The elements we think are important primarily include a wide range of attractive tasks, a comprehensive range of opportunities for personal and professional development, options for international assignments and working conditions that enable employees to achieve a good work-life balance. We also offer fair remuneration commensurate with the work performed, profit-sharing and numerous social benefits.

We expect our top employees to demonstrate a high level of professional competence, deliver excellent quality of work, be prepared to embrace change and accept flexibility in their deployment, be keen to develop their skills and qualifications (especially in relation to future customer requirements, including those involving digitalization), be willing to continuously improve productivity and pursue their chosen career with commitment and passion. The long-term success of our Company will only be made possible by the outstanding performance of our employees, taking an agile approach to collaboration and using innovative methods.

Our HR Strategy

The Human Resources unit of Volkswagen Financial Services AG has overarching responsibility for human resources in all the German companies in the Volkswagen Financial Services Group.

The ROUTE2025 program has created new areas of focus in terms of HR strategy. Six strategic areas for action are listed under the heading “Top Employer/Top Employees”. These areas for action are helping Volkswagen Financial Services AG to position itself as “the key to mobility”. With the support of the best employees, our objective is to continue to drive forward development around the strategic cornerstones of customers, volume, profitability and operational excellence. Based on specific activities to develop and retain personnel, coupled with profit-sharing arrangements commensurate with the work performed, we aim to encourage top performance and ensure we provide outstanding customer service with top employees, but also, as a first-rate employer, take our excellent globally recognized reputation to yet another level. One of the factors that will help us achieve this objective is to give more attention to a culture of feedback, open discussion and appreciative cooperation.

Initially, the key priority is to promote a culture of open feedback and discussion and of customer- and service-oriented cooperation. This includes not only cooperation between departments within the Company, but equally collaboration between the head office and the branches, between the branches themselves and cooperation with the customer.

Volkswagen Financial Services AG and the Volkswagen Bank GmbH Group are already offering competitive, performance-related remuneration.

As the parent of the financial holding company group, Volkswagen Financial Services AG is subject to direct supervision by the European Central Bank and is required to implement the Institutsvergütungsverordnung (InstitutsVergV – German Regulation Governing Remuneration at Institutions) of December 16, 2013 throughout the Group. Under the amended provisions in this regulation, banks must satisfy the special regulatory requirements for remuneration systems as well as comply with the re-drafted and tighter general requirements. The operational implementation of the provisions of the InstitutsVergV was once again a major

feature of HR activities in fiscal year 2016. Strategies and instruments already introduced, such as the Works Council agreement on variable remuneration, the variable remuneration ceiling, national and international risk-taker identification, the InstitutsVergV-compliant bonus process and the reporting system using a remuneration report, continued to be applied. In addition, the malus (performance adjustment) concept for risk-takers was agreed with the relevant committees and put into operation as part of the first-time use of deferral payments. The Basic Principles of the Remuneration System and the Group Remuneration Strategy are reviewed each year and adjusted if required. Furthermore, special governance functions (Remuneration Committee and Remuneration Officer) ensured that the adequacy of the remuneration systems was continuously monitored.

The Human Resources Strategy Card remained the most important management tool for implementing our HR strategy. The objectives and definitions set out on the card provide uniform guidance for our local entities around the world from the two perspectives of top employer and top employees. The content is regularly reviewed to ensure it is up to date. The local entities hold regular meetings with the head office – at least twice a year – to report on their successes and share detailed information in this regard. Depending on the situation, support measures are agreed and/or highly positive examples are systematically made available to other branches so that synergies can also be leveraged between the different local companies.

We assess the extent to which we have achieved our objective of being a top employer by regularly taking part in external employer competitions. Twelve companies have now already been included in national lists of the best companies or have been certified as a “Great Place to Work”. These companies also include Volkswagen Financial Services AG in Germany which took first place in Germany for the third time in succession. In 2016, it also received accolades from Focus magazine and the employer evaluation platform kununu as a top company and in the “Best Employers in Germany” awards.

The satisfaction of our customers with the work of our employees is given top priority at Volkswagen Financial Services AG. For this reason, the results of external and internal customer satisfaction surveys are also used as indicators of target achievement.

Business units that have no direct contact with external customers have the opportunity to use the “Internal customer feedback on customer and service orientation” to invite all internal employees who are customers of the business unit concerned to express their satisfaction in an online survey on the basis of defined customer and service orientation criteria.

The results from the internal customer surveys and from the external customer survey data currently in development will in future provide the basis for calculating the top KPI “Customer satisfaction”.

HR Development

In 2016, the training team at Volkswagen Financial Services AG selected and recruited 44 new vocational trainees/dual vocational training students from a total of approximately 1,700 applicants. Training is provided in banking (for professional banking qualifications), insurance (for professional insurance and finance qualifications) and in IT (for specialist professional IT qualifications in application development). The dual approach combines vocational training with study for a university degree. The Bachelor of Arts in Business Administration is offered in collaboration with WelfenAkademie e.V; the Bachelor of Science in Business Informatics is offered in collaboration with Leibniz University of Applied Sciences.

As of December 31, 2016, Volkswagen Financial Services AG had 127 vocational trainees and trainees on dual study programs who were assigned to business units at Volkswagen Bank GmbH under staff leasing arrangements.

Report on Expected Developments

The global economy is expected to grow in 2017 at a slightly faster pace than in the previous year.
We anticipate that trends in the global demand for automobiles will vary from region to region but the rise in demand is likely to be slightly slower than in the reporting year.

The main opportunities and risks arising from the operating activities having been set out in the report on opportunities and risks, the section below now outlines the expected future developments. These developments give rise to opportunities and potential benefits that are included in our planning process on an ongoing basis so that we can exploit them as soon as possible.

Our assumptions are based on current estimates by third-party institutions. These include economic research institutes, banks, multinational organizations and consulting firms.

GLOBAL ECONOMIC DEVELOPMENT

In our forecasts, we assume that global economic growth in 2017 will be slightly above the previous year's level. We believe risks will arise from protectionist tendencies, turbulence in the financial markets and structural deficits in individual countries. In addition, growth prospects will continue to be hurt by geopolitical tensions and conflicts. We expect the economic upturn to continue in the large majority of industrialized nations, with stable rates of expansion overall. Most emerging markets will probably see faster growth than in the previous year. We expect the strongest rates of expansion in Asia's emerging economies.

Furthermore, we anticipate that the global economy will also continue to grow in the period 2018 to 2021.

Europe

In Western Europe, the economic recovery is expected to decelerate to some extent in 2017 compared with the reporting period. Resolving structural problems and the uncertain outcome of the Brexit negotiations between the EU and the United Kingdom represent major challenges.

Germany

In Germany, GDP is slated to rise in 2017 at a similar pace as in the reporting period. The situation in the labor market is expected to remain stable, bolstering consumer spending.

FINANCIAL MARKETS

We predict that economic growth in 2017 will be slightly higher than in the previous year. Geopolitical tensions, uncertainty in financial markets and structural deficits in individual countries will have an adverse impact. Trends in capital markets will continue to maintain downward pressure on returns because of the loose monetary policy that is being sustained in the eurozone and in Japan. The ECB will continue its bond-buying program because core inflation is still rising too slowly and the structural deficits in southern European countries have not yet been eliminated. Interest rate rises by the Federal Reserve in the USA could have a negative impact on a weakening global economy.

Europe

Further economic recovery is anticipated in Europe. Challenges will be presented by the negotiations for the UK's exit from the EU and by structural problems in some European countries. Regardless of the conflict with Ukraine, the Russian economy is likely to grow slightly. The ECB's decision in December to maintain its loose monetary policy will continue to exacerbate the problems caused by the scarcity of available bonds.

Germany

Economic growth in Germany is expected to remain at the level of the previous year overall. Although there is likely to be a slowdown in export growth in 2017, the rise in the statu-

tory minimum wage will give a clear boost to macroeconomic wage growth during the year.

TRENDS IN THE PASSENGER CAR MARKETS

We expect trends in the passenger car markets in the individual regions to be mixed in 2017. Overall, growth in global demand for new vehicles will probably be slower than in the reporting period.

The Volkswagen Group is well positioned to deal with the mixed developments in automotive markets around the world. Our broad, selectively expanded product range featuring the latest generation of engines as well as a variety of alternative drives puts us in a good position globally compared with our competitors. Our goal is to offer all customers the mobility and innovations they need, sustainably strengthening our competitive position in the process.

We estimate that demand for passenger cars worldwide will continue to increase in the period 2018 to 2021.

Europe

For 2017, we anticipate that unit sales volumes in Western Europe will fall somewhat short of the level seen in the reporting period. Pre-crisis levels are not expected to be reached, even in the medium term. The continuing uncertainty among consumers precipitated by the debt crisis is likely to be exacerbated by the uncertain outcome of the Brexit negotiations between the EU and the UK, putting a damper on demand. In Italy and Spain, the recovery will probably continue in 2017 but at a much slower pace; for France, we expect growth to be only slightly positive. We anticipate that the market volume in the United Kingdom will be considerably lower than the high level seen in the previous year.

Germany

Following the positive trend of recent years, we forecast that the volume of the German passenger car market in 2017 will be slightly lower than in the previous year.

TRENDS IN THE MARKETS FOR COMMERCIAL VEHICLES

We expect trends in the markets for light commercial vehicles in the individual regions to be mixed again in 2017. Overall, we envisage modest growth in demand, a trend that is likely to continue in the period 2018 to 2021.

Due to the uncertainty caused by the United Kingdom's European Union membership referendum in June 2016, we estimate that demand for light commercial vehicles in Western Europe in 2017 will be slightly below the previous year's level. The United Kingdom is expected to register the biggest decline in the region. We anticipate that registrations in Germany will be around the previous year's level.

In the markets for mid-sized and heavy trucks that are relevant for the Volkswagen Group, new registrations in 2017 are set to be somewhat up on the level in 2016. For the period 2018 to 2021 we anticipate a positive trend.

We expect to see demand in Western Europe and Germany decrease slightly year-on-year in 2017.

INTEREST RATE TRENDS

In 2016 and also into the beginning of the current fiscal year, central banks continued to support the global economy and the financial system with an expansionary monetary policy. This is reflected in the sustained period of historically low interest rates. Uncertainty about the growth in the global economy is gradually dissipating and this could mean that the central banks decide to scale back their monetary policy stimulus. However, the European Central Bank will certainly maintain its policy of low interest rates throughout the whole of 2017. There is now greater uncertainty – mainly caused by Brexit – about when the Bank of England will bring the period of low interest rates in the UK to an end. In the USA, the key interest rate was raised by 25 basis points in December 2016 and further rate rises are anticipated during the course of 2017.

MOBILITY CONCEPTS

Social and political factors are increasingly having an impact on many people's individual mobility behavior. New challenges in connection with the design of an intelligent mobility mix comprising public transport combined with motorized and non-motorized personal transport are appearing, primarily in large metropolitan areas. Mobility is being redefined in many respects.

In collaboration with the automotive brands in the Volkswagen Group, Volkswagen Bank GmbH is devoting a great deal of time and effort to pioneering work on the development of new mobility concepts, as has been the case in the conventional automotive business for many years.

New mobility solutions will enhance the traditional idea of owning a vehicle. Simple, transparent, safe, reliable, affordable and flexible – these are the key requirements that our business must satisfy in the future. Volkswagen Bank GmbH Group continues to closely monitor developments in the mobility market and is already working on new models to support alternative types of marketing and establish new mobility concepts that will safeguard and expand on its existing business model.

In this way, we will continue to make good on the essence of our brand promise in the future and remain "The Key to Mobility" over the long term.

SUMMARY OF EXPECTED DEVELOPMENTS

The Volkswagen Bank GmbH Group expects its growth in the next fiscal year to be linked to the growth in unit sales of Volkswagen Group vehicles. It aims to boost its business volume by increasing the penetration rate and by expanding the product range in existing markets. Please refer to the

statements in the opportunities and risks report for information on the trends in credit risk, liquidity risk, and residual value risk.

Sales activities related to the Volkswagen Group brands will be further intensified, particularly through joint strategic projects.

The Volkswagen Bank GmbH Group also intends to continue implementing its measures aimed at improving its leverage of the potential available along the automotive value chain. Our aim is to satisfy the wishes and needs of our customers in the most efficient manner in cooperation with the Group brands. Our end customers are looking, in particular, for mobility with predictable fixed costs. In addition, we intend to further expand the digitalization of our business.

The product packages and mobility solutions successfully launched in the last few years will be refined in line with customer needs.

In parallel with its market-based activities, the position of the Volkswagen Bank GmbH Group vis-à-vis its global competitors will be further strengthened through strategic investment in structural projects as well as through process optimization and productivity gains.

OUTLOOK FOR 2017

When the above factors and the market trends are considered, the following overall picture emerges, as applicable to Volkswagen Bank GmbH, from both single entity and Group perspectives: our earnings expectations assume stable funding costs, greater levels of cooperation with the individual Group brands, increased cost optimization under our efficiency program and a continued high degree of uncertainty about macroeconomic conditions in the real economy and the impact of this uncertainty on factors such as risk costs. Assuming that margins remain stable in the coming year, the operating profit in fiscal year 2017 would be slightly above the level achieved in fiscal year 2015. The diesel issue is not expected to result in any additional effects that would have a negative impact on operating profit for fiscal year 2017.

We expect the trend toward a slight increase in new contracts and modest growth in the portfolio of current contracts from previous years to continue. In addition, we assume that in 2017 we will again be able to boost our penetration rate slightly in an overall growing vehicle market. We expect to see a further slight increase in business volume in 2017. The volume of deposits is projected to contract year-on-year in 2017. Based on these trends, we forecast that operating profit in 2017 will be slightly above the 2015 level in spite of greater pressure on margins. The tighter capital requirements and the resulting greater capital adequacy will probably lead to a slight decline in return on equity in 2017 compared with the previous year. Based on the forecast profit for the year, we expect the cost/income ratio in 2017 to be at or slightly below the level of the previous year.

FORECAST CHANGES IN KEY PERFORMANCE INDICATORS FOR FISCAL YEAR 2017 COMPARED WITH PRIOR-YEAR FIGURES

	Actual 2015	Actual 2016	Forecast for 2017
Nonfinancial performance indicators			
Penetration	17.7%	17.6%	Slight increase
Current contracts (thousands)[1]	2,821	3,002	Slight increase
New contracts (thousands)[1]	1,017	1,081	Slight increase
Financial performance indicators			
Volume of business (€ million)	36,330	38,748	Slight increase
Volume of deposits (€ million)	27,877	35,666	Volume reduction
Operating profit (€ million)	539	645	Slightly higher than in 2015

1 Since January 1, 2016, a new method has been used to determine the contract figures. The figures for the previous year 2015 have been restated accordingly.

Braunschweig, February 14, 2017
The Management

Anthony Bandmann

Harald Heßke

Jens Legenbauer

Torsten Zibell

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Income Statement

of the Volkswagen Bank GmbH Group

€ million	Note	Jan. 1 – Dec. 31, 2016	Jan. 1 – Dec. 31, 2015	Change in percent
Interest income from lending transactions before provision for credit risks	(20)	1,336	1,307	2.2
Net income from leasing transactions before provision for credit risks	(15)	170	128	32.8
Interest expense		–207	–194	6.7
Net income from lending and leasing transactions before provision for credit risks	(5, 20)	1,299	1,241	4.7
Provision for credit risks from lending and leasing business	(9, 21, 30)	–38	–71	–46.5
Net income from lending and leasing transactions after provision for credit risks		1,261	1,169	7.9
Net fee and commission income	(5, 22)	–30	39	X
Net gain/loss on the measurement of derivative financial instruments and hedged items	(10, 23)	–9	10	X
Net gain/loss on marketable securities and miscellaneous financial assets[1]	(5, 32)	20	14	42.9
General and administrative expenses	(5, 6, 13, 14, 15, 24, 61)	–829	–794	4.4
Net other operating income/expenses	(5, 25)	255	138	84.8
Profit before tax		**669**	**575**	**16.3**
Income tax expense	(6, 26)	–186	–157	18.5
Profit after tax		**482**	**418**	**15.3**
Profit after tax attributable to Volkswagen Financial Services AG		482	418	15.3

1 This item includes income of €14 million from the disposal of noncurrent assets that had been classified in the previous year as held for sale.

Statement of Comprehensive Income

of the Volkswagen Bank GmbH Group

€ million	Note	Jan. 1 – Dec. 31, 2016	Jan. 1 – Dec. 31, 2015
Profit after tax		**482**	**418**
Pension plan remeasurements recognized in other comprehensive income	(17, 44)		
Pension plan remeasurements recognized in other comprehensive income, before tax		–5	3
Deferred taxes relating to pension plan remeasurements recognized in other comprehensive income	(6, 26)	1	–1
Pension plan remeasurements recognized in other comprehensive income, net of tax		–3	2
Share of other comprehensive income of equity-accounted investments that will not be reclassified to profit or loss, net of tax		–	–
Items that will not be reclassified to profit or loss		**–3**	**2**
Exchange differences on translating foreign operations	(4)		
Gains/losses on currency translation recognized in other comprehensive income		–42	10
Reclassified to profit or loss		–	–
Exchange differences on translating foreign operations, before tax		–42	10
Deferred taxes relating to exchange differences on translating foreign operations		–	–
Exchange differences on translating foreign operations, net of tax		–42	10
Cash flow hedges	(10, 23, 31)		
Fair value changes recognized in other comprehensive income		1	0
Reclassified to profit or loss		0	–3
Cash flow hedges, before tax	(6, 26)	1	–3
Deferred taxes relating to cash flow hedges		0	1
Cash flow hedges, net of tax		1	–2
Available-for-sale financial assets	(11, 32, 50)		
Fair value changes recognized in other comprehensive income		45	7
Reclassified to profit or loss		–16	–5
Available-for-sale financial assets, before tax	(6, 26)	29	2
Deferred taxes relating to available-for-sale financial assets		–11	2
Available-for-sale financial assets, net of tax		19	4
Share of other comprehensive income of equity-accounted investments that may be reclassified subsequently to profit or loss, net of tax		–	–
Items that may be reclassified subsequently to profit or loss		**–23**	**11**
Other comprehensive income, before tax		–17	12
Deferred taxes relating to other comprehensive income		–10	2
Other comprehensive income, net of tax		**–26**	**14**
Total comprehensive income		**456**	**432**
Total comprehensive income attributable to Volkswagen Financial Services AG		456	432

Balance Sheet

of the Volkswagen Bank GmbH Group

Assets (€ million)	Note	Dec. 31, 2016	Dec 31, 2015	Change in percent
Cash reserve	(7, 28)	1,457	1,352	7.8
Loans to and receivables from banks	(8)	1,944	1,501	29.5
Loans to and receivables from customers attributable to				
Retail financing		24,940	23,312	7.0
Dealer financing		10,538	10,302	2.3
Leasing business	(15)	3,014	2,502	20.5
Other loans and receivables		7,175	4,690	53.0
Total loans to and receivables from customers	(8, 9, 29, 30)	45,667	40,806	11.9
Derivative financial instruments	(10, 31)	221	153	44.4
Marketable securities[1]	(11, 32)	4,455	2,557	74.2
Miscellaneous financial assets	(12, 33)	3	3	0.0
Intangible assets	(13, 34)	39	43	–9.3
Property and equipment	(14, 35)	9	10	–10.0
Lease assets	(15, 36)	877	710	23.5
Investment property	(15, 36)	1	1	0.0
Deferred tax assets	(6, 37)	1,212	1,431	–15.3
Current tax assets	(6)	53	50	6.0
Other assets	(38)	396	589	–32.8
Total		**56,334**	**49,206**	**14.5**

1 Securities included in the previous year noncurrent assets of €12 million classified as available for sale.

Equity and liabilities (€ million)	Note	Dec. 31, 2016	Dec 31, 2015	Change in percent
Liabilities to banks	(16, 40)	4,930	4,020	22.6
Liabilities to customers	(16, 40)	37,938	30,478	24.5
Notes, commercial paper issued	(41, 42)	4,311	7,604	–43.3
Derivative financial instruments	(10, 43)	43	46	–6.5
Provisions	(17, 18, 44)	425	376	13.0
Deferred tax liabilities	(6, 45)	1,070	1,237	–13.5
Current tax liabilities	(6)	89	39	X
Other liabilities	(46)	217	150	44.7
Subordinated capital	(47)	155	226	–31.4
Equity	(49)	7,156	5,030	42.3
Subscribed capital		318	318	–
Capital reserves		6,026	3,946	52.7
Retained earnings		826	757	9.1
Other reserves		–14	9	X
Total		**56,334**	**49,206**	**14.5**

Statement of Changes in Equity

of the Volkswagen Bank GmbH Group

€ million	Subscribed capital	Capital reserves	Retained earnings	OTHER RESERVES Currency translation	OTHER RESERVES Cash flow hedges	OTHER RESERVES Available-for-sale financial assets	OTHER RESERVES Equity-accounted investments	Total equity
Balance as of Jan. 1, 2015	**318**	**3,946**	**602**	**–22**	**2**	**17**	**–**	**4,864**
Profit after tax	–	–	418	–	–	–	–	418
Other comprehensive income, net of tax	–	–	2	10	–2	4	–	14
Total comprehensive income	**–**	**–**	**421**	**10**	**–2**	**4**	**–**	**432**
Capital increase	–	–	–	–	–	–	–	–
Distribution/profit transfer to Volkswagen Financial Services AG[1]	–	–	–268	–	–	–	–	–268
Other changes	–	–	1	–	–	–	–	1
Balance as of Dec. 31, 2015	**318**	**3,946**	**757**	**–12**	**0**	**21**	**–**	**5,030**
Balance as of Jan. 1, 2016	**318**	**3,946**	**757**	**–12**	**0**	**21**	**–**	**5,030**
Profit after tax	–	–	482	–	–	–	–	482
Other comprehensive income, net of tax	–	–	–3	–42	1	19	–	–26
Total comprehensive income	**–**	**–**	**479**	**–42**	**1**	**19**	**–**	**456**
Capital increase	–	2,080	–	–	–	–	–	2,080
Distribution/profit transfer to Volkswagen Financial Services AG[1]	–	–	–414	–	–	–	–	–414
Other changes	–	–	5	–	0	–	–	5
Balance as of Dec. 31, 2016	**318**	**6,026**	**826**	**–54**	**0**	**40**	**–**	**7,156**

1 The figures show the share of HGB profit attributable to Volkswagen Financial Services AG.

Cash Flow Statement

of the Volkswagen Bank GmbH Group

€ million	Jan. 1 – Dec. 31, 2016	Jan. 1 – Dec. 31, 2015
Profit after tax	**482**	**418**
Depreciation, amortization, impairment losses and reversals of impairment losses	178	227
Change in provisions	49	3
Change in other noncash items	577	–38
Gain/loss on disposal of financial assets and items of property and equipment	0	0
Net interest income and dividend income	–860	–955
Other adjustments	–6	0
Change in loans to and receivables from banks	–429	–566
Change in loans to and receivables from customers	–5,004	–3,384
Change in lease assets	–348	–387
Change in other assets related to operating activities	194	–206
Change in liabilities to banks	907	2,257
Change in liabilities to customers	7,123	3,525
Change in notes, commercial paper issued	–3,289	55
Change in other liabilities related to operating activities	65	21
Interest received	1,475	1,408
Dividends received	–408	–259
Interest paid	–207	–194
Income taxes paid	–95	–159
Cash flows from operating activities	**403**	**1,767**
Proceeds from disposal of investment property	0	–
Acquisition of investment property	–	–
Proceeds from disposal of subsidiaries	4	0
Acquisition of subsidiaries	–30	–13
Proceeds from disposal of other assets	1	2
Acquisition of other assets	–6	–6
Change in investments in securities	–2,007	–243
Cash flows from investing activities	**–2,038**	**–261**
Proceeds from changes in capital	2,080	–
Profit transfer to Volkswagen Financial Services AG	–268	–303
Change in cash funds attributable to subordinated capital	–70	–239
Cash flows from financing activities	**1,742**	**–542**
Cash and cash equivalents at end of prior period	**1,352**	**386**
Cash flows from operating activities	403	1,767
Cash flows from investing activities	–2,038	–261
Cash flows from financing activities	1,742	–542
Effect of exchange rate changes	–3	0
Cash and cash equivalents at end of period	**1,457**	**1,352**

See note 62 for disclosures on the cash flow statement

Notes to the Consolidated Financial Statements

of the Volkswagen Bank GmbH Group for the Year Ended December 31, 2016

General Information

Volkswagen Bank GmbH is a limited liability company (Gesellschaft mit beschränkter Haftung, GmbH) under German law. It has its registered office at Gifhorner Strasse, Braunschweig, Germany, and is registered in the Braunschweig commercial register (HRB 1819).

The object of the Company is to develop, sell and process its own and third-party financial services both in Germany and abroad, the purpose of such financial services being to support the business of Volkswagen AG and of Volkswagen AG's affiliated companies.

Volkswagen Financial Services AG, Braunschweig, is the sole shareholder of Volkswagen Bank GmbH. Volkswagen Financial Services AG and Volkswagen Bank GmbH have entered into a profit-and-loss transfer agreement.

The annual financial statements of Volkswagen Bank GmbH are included in the consolidated financial statements of Volkswagen AG, Wolfsburg, which are published in the electronic German Federal Gazette and Company Register.

Group Accounting Principles

Volkswagen Bank GmbH has prepared its consolidated financial statements for the year ended December 31, 2016 in accordance with International Financial Reporting Standards (IFRS), as adopted by the European Union (EU), and the interpretations issued by the IFRS Interpretations Committee as well as in accordance with the additional disclosures required by German commercial law under section 315a(1) of the Handelsgesetzbuch (HGB – German Commercial Code). All IFRS issued by the International Accounting Standards Board (IASB) up to December 31, 2016 for which mandatory application was required in fiscal year 2016 in the EU were taken into account in these consolidated financial statements.

In addition to the income statement, the statement of comprehensive income and the balance sheet, the IFRS consolidated financial statements also include the statement of changes in equity, the cash flow statement and the notes. The separate report on the risks associated with future development (report on opportunities and risks in accordance with section 315(1) of the HGB) can be found in the combined management report on pages 20 – 36. This report contains the qualitative information about the nature and extent of risks arising from financial instruments required in accordance with IFRS 7.

All estimates and assumptions required for recognition and measurement under IFRS are made in accordance with the relevant standard. They are continuously updated and are based on past experience and other factors, including expectations regarding future events that appear to be reasonable in the given circumstances. Where significant estimates have been necessary, the assumptions made by the Bank are explained in the disclosures on management's estimates and assumptions.

During the year under review, individual details were adjusted in line with the presentation in the annual report for Volkswagen Financial Services AG. Changes have been made in the disclosures covering net fee and commission income and the fair value of financial instruments. There was no impact on the balance sheet or income statement from these changes. Corresponding changes in the tables are identified by footnotes.

The Management completed the preparation of these consolidated financial statements on February 14, 2016. This date marked the end of the period in which adjusting events after the reporting period were recognized.

Significant Events

In 2016, the sole shareholder of Volkswagen Bank GmbH initiated a restructuring under company law. The objective of the restructuring is to pool the European lending and deposits business in Volkswagen Bank GmbH and separate this business from other financial services activities in the Volkswagen Financial Services AG Group. As part of this restructuring, Volkswagen AG will become the new sole shareholder of Volkswagen Bank GmbH. A new company, Volkswagen Financial Services Digital Solutions GmbH, has been established. In the future, this company will develop and make available selected, innovative services for the benefit of its shareholders, Volkswagen Bank GmbH and Volkswagen Financial Services AG. The other activities will remain in Volkswagen Financial Services AG, which will still be a direct subsidiary of Volkswagen AG. During the course of 2017, further work will be carried out on the details of the restructuring and preparations will be made for its implementation.

Effects of New and Revised IFRS

Volkswagen Bank GmbH has applied all financial reporting standards adopted by the EU and subject to mandatory application from fiscal year 2016.

A number of amendments to International Financial Reporting Standards resulting from the Annual Improvements Project 2012 and Annual Improvements Project 2014 have come into force since January 1, 2016. These amendments include changes to IFRS 3, IFRS 7, IFRS 8, IFRS 13 and IAS 24. Following the amendments to IFRS 8 “Operating Segments”, the criteria used to aggregate operating segments must now also be disclosed. These changes do not have any effect on the Volkswagen Bank GmbH Group’s segment reporting. Additional disclosure requirements regarding the derecognition of financial instruments have been added to IFRS 7. These requirements mainly affect the presentation of ABS transactions.

There has also been a requirement since January 1, 2016 to apply amendments to IAS 19. The amendments concern the accounting treatment of employee contributions to pensions. As a result of these amendments, the Volkswagen Bank GmbH Group will change its procedures so that employee contributions in which the amount is independent of the number of years of service (fixed percentage of salary) will, in the future, be deducted from the service cost in the year the amounts are paid.

As a result of the amendments to IAS 16 and IAS 38, it has been clarified with effect from January 1, 2016 that revenue-based methods of measuring depreciation and amortization will generally not be permitted. In IAS 1, clarifications and new requirements in relation to reporting were introduced with effect from January 1, 2016. The changes also specified that disclosures are only required in the consolidated financial statements if the content is material.

The amendments to the IFRS described above do not materially affect the Volkswagen Bank GmbH Group’s financial position and financial performance.

New and Revised IFRS Not Applied

In its 2016 consolidated financial statements, Volkswagen Bank GmbH has not applied the following financial reporting standards that have already been issued by the IASB but were not yet subject to mandatory application in fiscal year 2016.

Standard/ interpretation		Published by the IASB	Application requirement[1]	Adopted by EU	Expected impact
IFRS 2	Classification and Measurement of Share-based Payment Transactions	June 20, 2016	January 1, 2018	No	None
IFRS 4	Applying IFRS 9 Financial Instruments with IFRS 4 Insurance Contracts	September 12, 2016	January 1, 2018	No	None
IFRS 9	Financial Instruments	July 24, 2014	January 1, 2018	Yes	Detailed description shown below
IFRS 10 and IAS 28	Consolidated Financial Statements and Investments in Associates and Joint Ventures: Sale or Contribution of Assets between an Investor and its Associate or Joint Venture	September 11, 2014	Postponed[2]	–	None
IFRS 15	Revenue from Contracts with Customers	May 28, 2014	Jan. 1, 2018[3]	Yes	No material impact on revenue recognition, additional disclosure requirements in the notes
	Clarifications to IFRS 15 – Revenue from Contracts with Customers	April 12, 2016	January 1, 2018	No	Additional transitional exemptions, otherwise no material impact
IFRS 16	Leases	January 13, 2016	January 1, 2019	No	Detailed description shown below
IAS 7	Statement of Cash Flows: Disclosures	January 29, 2016	January 1, 2017	No	Preparation of a reconciliation for liabilities from financing activities.
IAS 12	Income Taxes: Recognition of Deferred Tax Assets for Unrealized Losses	January 19, 2016	January 1, 2017	No	No material impact
IAS 40	Transfers of Investment Property	December 8, 2016	January 1, 2018	No	No material impact
	Improvements to International Financial Reporting Standards 2016[4]	December 8, 2016	January 1, 2018	No	No material impact
IFRIC 22	Foreign Currency Transactions and Advance Consideration	December 8, 2016	January 1, 2018	No	Translation of foreign currency advances into the functional currency using the spot rate on the date of payment

1 Requirement for initial application from Volkswagen Bank GmbH's perspective.
2 On December 15, 2015, the IASB decided to postpone the date of initial application indefinitely.
3 Postponed until January 1, 2018 (IASB decision on September 11, 2015).
4 Minor changes to a number of IFRS (IFRS 1, IFRS 12, IAS 28).

IFRS 9 FINANCIAL INSTRUMENTS

IFRS 9 Financial Instruments revises the financial reporting provisions governing the classification and measurement of financial assets, impairment of financial assets and hedge accounting. A project is currently under way to evaluate the expected impact of the changes arising from IFRS 9 on the Volkswagen Bank GmbH Group and to implement the requirements. Necessary IT modifications will be carried out during the course of 2017.

Financial assets are classified and measured on the basis of the business model operated by an entity and the structure of its cash flows. On initial recognition, a financial asset is classified as “at amortized cost”, “at fair value through other comprehensive income” or “at fair value through profit or loss”. The Volkswagen Bank GmbH Group is not anticipating any material impact from the classification of financial assets under IFRS 9 because our assessments show that the main financial assets are currently measured at amortized cost under IAS 39 and will remain so under IFRS 9 in the future. At present, it is not yet possible to arrive at a definitive evaluation of the impact from the classification of financial assets because the classification will have to be carried out on the changeover date of January 1, 2018.

Under IFRS 9, the classification of financial liabilities will be largely unchanged compared with the classification under the previous financial reporting requirements in accordance with IAS 39.

The model for determining impairment and recognizing the provision for credit risks is changing from an incurred loss model to an expected loss model. The expected loss model breaks down the provision for credit

risks into three stages. Financial assets that are newly acquired or issued and that are not deemed to be underperforming or non-performing on the date of initial recognition are allocated to stage 1. Stage 1 includes expected defaults that could arise from potential default events within the subsequent 12 months. In the case of financial assets in which the credit risk has increased significantly since acquisition or issue but in which the financial asset is not underperforming (stage 2) and non-performing financial assets (stage 3), the provision for credit risks is recognized on the basis of the expected remaining maturity of the financial asset (lifetime expected loss). It is anticipated that these changes to the rules will cause an upward trend in the level of provision for credit risks. This forecast is based firstly on the requirement to recognize a provision for credit risks on the basis of expected credit losses for the first 12 months for performing financial assets that have not been affected by a significant increase in credit risk since initial recognition. Secondly, it is a result of an assessment that the portfolio of financial assets for which the provision for credit risks must be recognized on the basis of lifetime expected losses will be greater than the portfolio of financial assets for which the provision for credit risks has been recognized on the basis of incurred losses (IAS 39).

As regards hedge accounting, IFRS 9 introduces wider designation options and the need to implement more complex measurement logic. IFRS 9 also removes the quantitative limits for the effectiveness test. In particular, there will be changes to the method of reclassification under IFRS 9. Depending on market trends, hedges will be assumed to have a greater impact on operating profit. The IFRS 9 hedge accounting requirements will be applied by the Volkswagen Bank GmbH Group prospectively from the changeover date.

IFRS 7 will also give rise to more extensive disclosures in the notes.

IFRS 16 LEASES

IFRS 16 amends the requirements for the accounting treatment of leases. The objective of IFRS 16 is to ensure that all leases are recognized in the balance sheet. Accordingly, the previous requirement for lessees to classify a lease as either a finance lease or operating lease has been eliminated. Instead, for all leases, lessees will have to recognize both a right-of-use asset and a lease liability in their balance sheet in the future. There are only exemptions for short-term leases or those of low value. During the term of the lease, the right-of-use asset must be depreciated and the lease liability measured using the effective interest method, taking into account the lease payments. The new accounting treatment for lessees will tend to increase assets and financial liabilities. It is also expected to reduce general and administrative expenses and increase interest expenses in the income statement. The changes also require extensive disclosures in the notes. The required accounting treatment for leases by lessors will be largely the same as under the current provisions in IAS 17. In the future, lessors will still have to classify a lease as either a finance lease or an operating lease based on the allocation of opportunities and risks from the asset.

Accounting Policies

1. Basic Principles

All entities included in the basis of consolidation have prepared their annual financial statements to the reporting date of December 31, 2016.

Financial reporting in the Volkswagen Bank GmbH Group complies with IFRS 10 and is on the basis of standard accounting policies. The consolidated financial statements have been prepared in euros. Unless otherwise stated, amounts are shown in millions of euros (€ million). All amounts shown are rounded, so minor discrepancies may arise from addition of these amounts.

Assets and liabilities are presented broadly in order of liquidity in accordance with IAS 1.60.

2. Basis of Consolidation

In addition to Volkswagen Bank GmbH, the consolidated financial statements comprise all significant German and foreign subsidiaries, including structured entities, that are directly or indirectly controlled by Volkswagen Bank GmbH. This is the case if Volkswagen Bank GmbH obtains control over potential subsidiaries directly or indirectly due to voting rights or similar rights, is exposed, or has rights to, positive or negative variable returns from its involvement with the potential subsidiaries, and is able to influence those returns.

On April 11, 2016, MAN Financial Services S.p.A., Dossobuono di Villafranca (VR), Italy, – a subsidiary at that time – was merged into Volkswagen Bank GmbH, effective retroactively from January 1, 2016.

Volkswagen Bank GmbH acquired MAN Financial Services S.A.S., Evry Cedex, France on April 1, 2016. The acquired company was merged into Volkswagen Bank GmbH on July 28, 2016, effective retroactively from January 1, 2016.

One foreign subsidiary was fully consolidated as of the reporting date.

To fund the financial services business, the Volkswagen Bank GmbH Group makes use of asset-backed securities (ABS) transactions created using structured entities. As of the balance sheet date, 24 such structured entities (previous year: 29) were fully consolidated in the consolidated financial statements. They may be either separate legal entities or separate pools of assets of a separate legal entity (fictional structured entity). There is no equity investment in either case. However, due to the design of the contracts, Volkswagen Bank GmbH nevertheless determines the main relevant activities of the structured entity and is able to influence the variable returns accruing to it. These structured entities are therefore controlled by Volkswagen Bank GmbH and fully consolidated in the consolidated financial statements.

Subsidiaries are included in the consolidation from the date on which control comes into existence; they cease to be consolidated when control no longer exists. Subsidiaries of minor significance to the Volkswagen Bank GmbH Group are not consolidated.

Volkswagen Bank GmbH maintains nine branches abroad. The list of all shareholdings can be found in note 68.

3. Consolidation Methods

The assets and liabilities of the German and foreign entities included in the consolidated financial statements are reported in accordance with the uniform accounting policies applicable throughout the Volkswagen Bank GmbH Group.

Acquisitions are accounted for by offsetting the carrying amounts of the equity investments with the proportionate amount of the remeasured equity of the subsidiaries on the date of acquisition or initial inclusion in the consolidated financial statements and in subsequent periods.

When subsidiaries are consolidated for the first time, the assets and liabilities, together with contingent consideration, are recognized at fair value on the date of acquisition or on the date of inclusion (for newly established subsidiaries). Subsequent changes in the fair value of contingent consideration do not generally result in an adjustment of the acquisition-date measurement. Acquisition-related costs that are not equity transaction costs are not added to the purchase price, but instead recognized as expenses. Goodwill arises when the purchase price of the investment exceeds the fair value of the identifiable assets and liabilities. Goodwill is tested for impairment at least once a year and additionally if relevant events or changes in circumstances occur (impairment-only approach). If the carrying amount of goodwill is higher than the recoverable amount, an impairment loss is recognized. If this is not the case, there is no change in the carrying amount of goodwill compared with the previous year. If the purchase price of the investment is less than the identifiable assets and liabilities, the difference is recognized in profit or loss in the year of acquisition. Goodwill is accounted for at the subsidiaries in the functional currency of those subsidiaries.

The net assets recognized at fair value as part of an acquisition transaction are depreciated or amortized over their relevant useful lives. If the useful life is indefinite, any requirement for the recognition of an impairment loss is determined at individual asset level using a procedure similar to that used for goodwill. Where hidden reserves and charges in the recognized assets and liabilities are uncovered during the course of purchase price allocation, these items are amortized over their remaining maturities.

Loans/receivables, liabilities, income and expenses relating to business relationships between consolidated entities are eliminated in the consolidation.

Consolidation transactions recognized in profit or loss are subject to the recognition of deferred taxes. Investments in companies that do not meet the consolidation requirements are reported as other equity investments under miscellaneous financial assets.

Intragroup transactions are conducted on an arm’s-length basis. Any resulting intercompany profits or losses are eliminated.

The special purpose entities account for less than €0.5 million of equity and profit (minority interests) and are therefore not reported as separate items of equity and in the income statement.

4. Currency Translation

Transactions in foreign currencies are translated in the single-entity financial statements of Volkswagen Bank GmbH and its consolidated subsidiaries at the rates prevailing at the transaction date. Foreign currency monetary items are reported in the balance sheet using the middle rate at the closing date and the resulting gains or losses are recognized in profit or loss.

The foreign branches and subsidiaries forming part of the Volkswagen Bank GmbH Group are independent subunits whose financial statements are translated using the functional currency principle. Under this principle, all assets and liabilities, but not equity, are translated at the closing rate. With the exception of income and expense items recognized in other comprehensive income, equity is translated at historical rates. Until the disposal of the subsidiary concerned, the resulting exchange differences on translating foreign operations are recognized in other comprehensive income and are presented as a separate item in equity.

The transaction data in the statement of changes in noncurrent assets is translated into euros using weighted average rates. A separate “Foreign exchange differences” line is reported to reconcile the carryforwards translated at the middle spot rate on the prior-year reporting date and the transaction data translated at average rates with the final balances translated at the middle spot rate on the reporting date.

We translate the income statement items into euros using weighted average rates. The exchange rates used for currency translation are listed in the table below.

€		BALANCE SHEET, MIDDLE SPOT RATE ON DEC. 31		INCOME STATEMENT, AVERAGE RATE	
		2016	2015	2016	2015
United Kingdom	GBP	0.85850	0.73395	0.81955	0.72585
Poland	PLN	4.41530	4.26390	4.36373	4.18412

5. Recognition of Revenue and Expenses

Revenue and expenses are recognized in accordance with the accrual basis of accounting and are reported in profit or loss in the period in which the substance of the related transaction occurs.

Interest income is recognized in the income statement using the effective interest method. Income from financing and leasing transactions, together with expenses for the funding of this business, is included in net income from lending and leasing transactions. This item also includes operating lease income, which is recognized on a straight-line basis over the lease term.

Net fee and commission income includes income and expenses from insurance broking as well as fees and commissions from the financing and financial services businesses.

Dividends are reported on the date on which the legal entitlement is established, i.e. generally the date on which a dividend distribution resolution is approved.

General and administrative expenses comprise personnel expenses, non-staff operating expenses, depreciation of and impairment losses on property and equipment, amortization of and impairment losses on intangible assets, and other taxes.

The main components of net other operating income/expenses are income from cost allocations to other entities in the Volkswagen Group and income from the reversal of provisions.

6. Income Taxes

Current income tax assets and liabilities are measured using the tax rates expected to apply in respect of the refund from or payment to the tax authorities concerned. Current income taxes are generally reported on an unnetted basis. Provisions are recognized for potential tax risks.

Deferred tax assets and liabilities are recognized in respect of temporary differences between the carrying amounts of assets and liabilities in the consolidated balance sheet and those in the tax base and in respect of tax loss carryforwards. This gives rise to expected income tax income or expense effects in the future (temporary differences). Deferred taxes are measured using the domicile-specific income tax rates expected to apply in the period in which the tax benefit is recovered or liability paid.

Deferred tax assets are recognized if it is probable that in the future sufficient taxable profits will be generated in the same tax unit against which the deferred tax assets can be utilized. If it is no longer likely that it will be possible to recover deferred tax assets within a reasonable period, valuation allowances are applied. The measurement of deferred tax assets for tax loss carryforwards is generally based on planning data for taxable income within over the next five years. Deferred tax assets and liabilities with the same maturities and relating to the same tax authorities are netted.

The tax expense attributable to the profit before tax is reported in the Group's income statement under the "Income tax expense" item and a breakdown into current and deferred taxes for the fiscal year is disclosed in the notes. Other non-income-related taxes are reported as a component of general and administrative expenses.

7. Cash Reserve

The cash reserve is carried at the nominal amount.

8. Loans and receivables

Loans to and receivables from banks, and loans to and receivables from customers, originated by the Volkswagen Bank GmbH are generally recognized at amortized cost using the effective interest method. Gains or losses arising from the changes in amortized cost are recognized in profit or loss, including the effects from changes in exchange rates. For reasons of materiality, current loans and receivables (due within one year) are not discounted and no unwinding of discount is therefore recognized. Some of the loans to and receivables from customers were included in portfolio hedges in the reporting period. Loans to and receivables from customers assigned to portfolio hedges are measured at hedged fair value.

Volkswagen Bank GmbH transfers loans and receivables to special purpose entities. At the level of the Volkswagen Bank Group, these transfers represent neither the derecognition of assets nor continuing involvement, because the respective special purpose entities are fully consolidated (note 2).

9. Provision for Credit Risks

The Volkswagen Bank GmbH Group takes full account of default risk by recognizing specific and portfolio-based valuation allowances in accordance with IAS 39. These allowances are posted to valuation allowance accounts. Provisions are also recognized to take into account indirect residual value risks.

In the case of credit risk present in significant individual loans to or receivables from customers or banks (e.g. dealer financing loans/receivables and fleet customer business loans/receivables), specific valuation allowances are recognized in accordance with Group-wide standards in the amount of losses already incurred.

Potential impairment is assumed in a number of situations, such as delayed payment over a certain period, the initiation of enforcement measures, the threat of insolvency or overindebtedness, application for or the initiation of insolvency proceedings, or the failure of restructuring measures.

Insignificant loans/receivables and significant individual loans/receivables with no indication of impairment are grouped together into homogeneous portfolios using comparable credit risk features and broken down by risk category. As long as no definite information is available as to which loans or receivables are in default, average historical default probabilities for the portfolio concerned are used to calculate the amount of the valuation allowances. Regular backtesting is carried out to ensure that the valuation allowances are appropriate.

Loans and receivables are reported in the balance sheet at the net carrying amount. Disclosures relating to the provision for credit risks are presented separately in note 30.

Uncollectible loans or receivables that are already subject to a workout process and for which all collateral has been recovered and all further options for recovering the loan or receivable have been exhausted are written off directly. Any specific valuation allowances previously recognized are utilized. Income subsequently collected in connection with loans or receivables already written off is recognized in profit or loss.

10. Derivative Financial Instruments

Derivative financial instruments comprise derivatives in effective hedges and derivatives not designated as hedging instruments. All derivatives are measured at fair value and are presented separately in notes 31 and 43.

The fair value is determined with the help of measurement software in IT systems using the discounted cash flow method and taking into account credit valuation adjustments (CVAs) and debt valuation adjustments (DVAs).

Derivatives are used as hedging instruments in fair value hedges or cash flow hedges. Hedge accounting in accordance with IAS 39 is only applied in the case of highly effective hedges.

When fair value hedges are applied, changes in the fair value of the derivative designated as the instrument used to hedge the fair value of a recognized asset or liability (hedged item) are recognized in profit or loss under net gain/loss on the measurement of derivative financial instruments and hedged items. Changes in the fair value of the hedged item in connection with which the risk is being minimized are also reported in profit or loss under this item. The effects in profit or loss from the changes in the fair value of the hedging instrument and the hedged item balance each other out depending on the extent of hedge effectiveness.

IAS 39 permits the use of fair value hedging not only for individual hedged items, but also for a group of similar hedged items. In the reporting period, Volkswagen Bank GmbH used portfolio-based fair value hedges to hedge interest-rate risks. In portfolio-based hedging, the accounting treatment of changes in fair value is the same as in fair value hedging at micro level.

In the case of derivatives that are designated as hedges of future cash flows and that satisfy the relevant criteria, the effective portion of changes in the fair value of the derivative is recognized in the cash flow hedge reserve through other comprehensive income. Any effect on profit or loss arises solely from the ineffective portion of the change in fair value. The measurement of the hedged item remains unchanged.

Changes in the fair value of derivatives that do not satisfy the hedge accounting criteria in IAS 39 are recognized in profit or loss under net gain/loss on the measurement of derivative financial instruments and hedged items.

The Volkswagen Bank GmbH Group documents all relationships between hedging instruments and hedged items. Hedge effectiveness is kept under constant review. All transactions entered into in the Volkswagen Bank GmbH Group are for hedging purposes.

With the exception of derivatives not designated as hedging instruments, no financial instruments are classified as financial assets or financial liabilities at fair value through profit or loss.

11. Marketable Securities

Marketable securities are categorized as available-for-sale financial assets. They are always measured at fair value through other comprehensive income. Permanent impairment losses are recognized in profit or loss. If no price can be determined directly for securities not traded on an active market, the present value of the expected future cash flows is used for measurement, discounted to the reporting date using the risk-adjusted yield curve.

Available-for-sale financial assets are subject to the recognition of impairment losses if there is objective evidence of permanent impairment. A rise in the risk-free interest rate or an increase in credit risk premiums included in the interest rate does not, by itself, generally represent objective evidence of impairment. If the requirements for impairment are no longer met, the impairment loss is reversed.

In the case of equity instruments, indicators of impairment include a significant (more than 20%) or long-term (more than 10% of the average market price over one year) fall in fair value below cost. If such an asset is found to be impaired, the cumulative loss is posted to other reserves and recognized in profit or loss. Reversals of impairment losses on equity instruments are reported in other comprehensive income.

In the case of debt instruments, impairment losses are recognized in the event of a forecast decline in future cash flows from the financial asset. A rise in the risk-free interest rate or an increase in credit risk premiums does not, by itself, generally represent objective evidence of impairment. Reversals of impairment losses on debt instruments are recognized in profit or loss.

12. Miscellaneous Financial Assets

Equity investments are reported as miscellaneous financial assets. They are reported at fair value or at cost, if fair value cannot be reliably determined. If there is significant or permanent impairment, impairment losses are recognized through profit or loss.

13. Intangible Assets

Purchased intangible assets with finite useful lives (largely software and customer relationships) are recognized at cost and amortized on a straight-line basis over a useful life of three to five years (software) or ten years (customer relationships).

When assessing whether the development costs associated with internally generated software are to be capitalized or not, we take into account not only the probability of a future inflow of economic benefits but also the extent to which the costs can be reliably determined. Direct and indirect costs that can be assigned to the development are capitalized, whereas research costs are not capitalized at all. Amortization is on a straight-line basis over a useful life of three to five years and is reported under general and administrative expenses.

At every reporting date, intangible assets with finite useful lives are tested to establish whether there are any indications of impairment. If there are indications of impairment, the carrying amount is compared to the recoverable amount. If the recoverable amount is lower than the carrying amount, an impairment loss is recognized.

The recoverable amount is the higher of fair value less costs to sell and value in use. Fair value less costs to sell is the amount of consideration that would be agreed upon in an arm's length transaction between knowledgeable, willing parties. The value in use is defined as the net present value of future cash flows expected to be derived from the asset. The recoverable amount was determined on the basis of value in use.

The amortization expense and impairment losses are reported within general and administrative expenses. Income from the reversal of impairment losses is recognized in net other operating income/expenses.

Brand names arising from business combinations usually have indefinite useful lives. Intangible assets with indefinite useful lives are not amortized. An annual review is carried out to establish whether an asset has an indefinite useful life. In accordance with IAS 36, these assets are tested for impairment by comparing the carrying amount and recoverable amount once a year. If required, an impairment loss is recognized to reduce the carrying amount to a lower recoverable amount.

Goodwill is tested for impairment once a year or when events or circumstances occur that indicate impairment. If the carrying amount of goodwill is higher than the recoverable amount, an impairment loss is recognized.

The recoverable amount of goodwill was derived from the value in use for the relevant cash-generating unit, which is determined using the discounted cash flow method. The basis is the latest planning data prepared by management for a detailed planning horizon of five years, with growth in subsequent years estimated using a flat rate percentage. This cash flow planning is based on expectations regarding future global economic trends and on assumptions derived from these trends about markets for passenger cars and commercial vehicles, market shares and the profitability of the Volkswagen Group's products. On the basis of these expectations, the plans of the financial services unit are prepared taking the respective market penetration and regulatory requirements into account. Appropriate assumptions regarding macroeconomic trends (e.g. currency and interest rate trends) and historical time series are taken into account. Planning assumptions are adjusted in line with the latest available information. The interest rate used is based on the long-term market interest rate in relation to the cash-generating unit. The calculations use a standard Group cost of equity of 7.5% (previous year: 8.5%). Appropriate assumptions regarding macroeconomic and historical trends are taken into account. The calculation of cash flows is always based on the forecast growth rates for the relevant markets. Cash flows after the end of the planning period are estimated using a growth rate of 1% p.a. (previous year: 1% p.a.).

14. Property and Equipment

Property and equipment (land and buildings plus operating and office equipment) is carried at cost less depreciation in accordance with estimated useful lives. Depreciation is applied on a straight-line basis over the estimated useful life. Useful lives are reviewed at every reporting date and adjusted where appropriate.
Depreciation is based on the following useful lives:

Property and equipment	Useful lives
Buildings and leasehold improvements	10 to 50 years
Operating and office equipment	3 to 13 years

Impairment losses are recognized if the requirements of IAS 36 are met, if the achievable net selling price or value in use of the asset concerned has fallen below the carrying amount. If the reasons for the recognition of an impairment loss in prior years now no longer apply, an appropriate reversal of the impairment loss is recognized. The depreciation expense and impairment losses are reported within general and administrative expenses. Income from the reversal of impairment losses is recognized in net other operating income/expenses.

15. Leasing Business

GROUP AS LESSOR

The Volkswagen Bank GmbH Group operates the finance lease business and the operating lease business. Most of the lease assets are vehicles, but to a lesser extent also involve land, buildings and dealer equipment.

A finance lease is a lease that transfers beneficial ownership to the lessee. In the consolidated balance sheet, receivables from finance leases are therefore reported within loans to and receivables from customers and the net investment in the lease generally equates to the cost of the lease asset. Interest income from finance leases is recognized using the effective interest method and reported under leasing income in the income statement.

In the case of operating leases, beneficial ownership of the lease asset remains with the lessor. In the consolidated balance sheet, the assets involved are reported separately under lease assets. They are measured at cost and reduced by straight-line depreciation over the lease term to the calculated residual carrying amount. Any impairment identified as a result of an impairment test in accordance with IAS 36 using the value in use or net selling price as the recoverable amount is taken into account by recognizing an impairment loss and adjusting the depreciation rate. If the reasons for the recognition of an impairment loss in prior years no longer apply, a reversal of the impairment loss is recognized. Impairment losses and reversals of impairment losses are included in the net income from leasing transactions before provision for credit risks. The leasing revenue is recognized on a straight-line basis over the lease term.

Land and buildings held to earn rentals are reported under the “Investment property” item in the balance sheet and measured at amortized cost. The land and buildings involved are generally leased out to dealer businesses. Depreciation is applied on a straight-line basis over useful lives of ten to 33 years. Any impairment identified as a result of an impairment test in accordance with IAS 36 is taken into account by recognizing an impairment loss.

GROUP AS LESSEE

Lease payments made under operating leases are recognized under general and administrative expenses.

BUYBACK TRANSACTIONS

Leases in which the Volkswagen Bank GmbH Group has a firm agreement with the lessor regarding the return of the leased asset are recognized under other loans and receivables within loans to and receivables from customers at the amount of the resale value agreed at the inception of the lease and are also recognized under

other assets in the amount equating to the right of use. In the case of noncurrent leases (maturity of more than one year), the agreed resale value is discounted at the inception of the lease. The unwinding of the discount during the term of the lease is recognized in interest income. The right-of-use asset recognized under other assets is depreciated on a straight-line basis over the term of the lease. This depreciation is reported under expenses from the leasing business. Lease payments received under subleases are reported as income from leasing business.

16. Liabilities

Liabilities to banks and customers, notes and commercial paper issued, and subordinated liabilities are recognized at amortized cost using the effective interest method. Gains or losses arising from the changes in amortized cost are recognized in profit or loss, including the effects from changes in exchange rates. For reasons of materiality, current liabilities (due within one year) are not discounted and no unwinding of discount is therefore recognized.

17. Provisions for Pensions and Other Post-Employment Benefits

Provisions are recognized for commitments in the form of retirement, invalidity and surviving dependants' benefits payable under pension plans. The benefits provided by the Group vary according to the legal, tax and economic circumstances of the country concerned, and usually depend on the length of service and remuneration of the employees.

The Volkswagen Bank GmbH Group provides occupational pensions in the form of both defined contribution and defined benefit plans. In the case of defined contribution plans, the Company makes contributions to state or private pension schemes based on statutory or contractual requirements, or on a voluntary basis. Once the contributions have been paid, the Volkswagen Bank GmbH Group has no further obligations. Current contributions are recognized as pension expenses in the period concerned. In 2016, the total contributions made by the Volkswagen Bank GmbH Group came to €0 million (previous year: €3 million). This amount included contributions to the compulsory state pension system in Germany in an amount of €0 million (previous year: €0 million).

Most pension plans in the Volkswagen Bank GmbH Group are defined benefit plans; a distinction is made between plans without and plans with plan assets. The pension provisions for defined benefit commitments are measured by independent actuaries using the internationally accepted projected unit credit method in accordance with IAS 19, under which the future obligations are measured on the basis of the proportionate benefit entitlements earned as of the reporting date. The measurement of pension provisions takes into account actuarial assumptions as to discount rates, salary and pension trends, and employee turnover rates, which are determined for each Group company depending on the economic environment. Actuarial gains or losses arise from differences between actual trends and prior-year estimates as well as from changes in assumptions. These actuarial gains or losses are recognized in other comprehensive income, together with the associated deferred taxes, in the period in which they arise. Detailed disclosures on provisions for pensions and other post-employment benefits are set out in note 44.

18. Other Provisions

Under IAS 37, provisions are recognized if a present legal or constructive obligation to third parties has arisen as a result of a past event, it is probable that settlement in the future will result in an outflow of economic resources and the amount of the obligation can be estimated reliably. If an outflow of resources is deemed neither probable nor improbable, the amount concerned is treated as a contingent liability. In accordance with IAS 37, this contingent liability is not recognized but disclosed in note 63.

Other provisions are recognized under the relevant expense item; reversals of other provisions are recognized as other operating income.

Provisions that are not related to an outflow of resources likely to take place in the subsequent year are recognized at their settlement amount discounted to the reporting date using market discount rates. The settlement amount also includes expected cost increases.

Any rights of recourse are not offset against provisions.

19. Trust Transactions

No transactions are entered into on the basis of the administration or placement of assets for third-party accounts (trust transactions).

Estimates and Assumptions by Management

The preparation of the consolidated financial statements requires management to make certain estimates and assumptions that affect the recognition and measurement of assets, liabilities, income and expenses, and the disclosures relating to contingent assets and liabilities for the reporting period.

Assumptions and estimates are based on the latest available information. In particular, the circumstances prevailing at the time the consolidated financial statements are prepared and future trends in the global and sector environment considered to be realistic are taken into account in the projected future performance of the business. The estimates and assumptions used by management have been made, in particular, on the basis of assumptions relating to macroeconomic trends as well as trends in automotive markets, financial markets and the legal framework. These and other assumptions are explained in detail in the report on expected developments, which forms an integral part of the group management report.

As future business performance is subject to unknown factors that, in part, lie outside the control of the Group, our assumptions and estimates continue to be subject to considerable uncertainty. This applies especially to the cash flows predicted over the short and medium terms. The discount rates used are also affected by uncertainty caused by factors beyond the control of the Group. If changes in parameters are different from the assumptions, the amounts actually arising could differ from the estimated values originally forecast. If actual performance is at variance with the forecasts, the assumptions and, where necessary, the carrying amounts of the assets and liabilities concerned are adjusted. The assumptions and estimates largely relate to the items set out below.

RECOVERABLE AMOUNT OF NON-FINANCIAL ASSETS AND EQUITY INVESTMENTS

The impairment tests applied to non-financial assets (particularly goodwill and brand names) and equity investments measured at cost require assumptions related to the future cash flows in the planning period and, where applicable, beyond. The assumptions about the future cash flows factor in expectations regarding future global economic trends, trends in the overall markets for passenger cars and commercial vehicles and expectations derived from these trends about financial services, taking into account market penetration, risk costs, margins and regulatory requirements. For further information on the assumptions relating to the detailed planning period, please refer to the report on expected developments, which forms part of the management report. The discount rates used in the discounted cash flow method applied when testing goodwill for impairment are based on specified cost of equity rates, taking into account historical experience and appropriate assumptions regarding macroeconomic trends.

RECOVERABLE AMOUNT OF LEASE ASSETS

The recoverable amount of the lease assets in the Group mainly depends on the residual value of the lease vehicles at the end of the contractually agreed lease period because this value represents a considerable proportion of the expected cash inflows. Continuously updated internal and external information on trends in residual values – based on particular local circumstances and empirical values from the marketing of used vehicles – is factored into the forecasts of residual values. These forecasts require the Group to make assumptions, primarily in relation to future supply and demand for vehicles and in relation to trends in vehicle prices. These assumptions are based on either professional estimates or information published by third-party experts. The professional estimates are based on external data (where available), taking into account any additional infor-

mation available internally, such as values from past experience and current sales data. Forecasts and assumptions are regularly verified by a process of backtesting.

FINANCIAL INSTRUMENTS

The procedure for determining the recoverability of financial assets requires estimates about the extent and probability of occurrence of future events. As far as possible, these estimates take into account the latest market data as well as rating and scoring information based on past experience. Further details on specific and portfolio-based valuation allowances can be found in the disclosures on the provision for credit risks (notes 9 and 30).

Management estimates are necessary to determine the fair value of financial instruments. This relates to both fair value as a measurement standard in the balance sheet and fair value in the context of disclosures in the notes. Fair value measurements are categorized into a three-level hierarchy depending on the type of inputs to the valuation techniques used and each level requires different management estimates. Fair values in Level 1 are based on prices quoted in active markets. Management assessments in this case relate to determining the primary or most advantageous market. Level 2 fair values are measured on the basis of observable market data using market-based valuation techniques. Management decisions for this level relate to selecting generally accepted, standard industry models and specifying the market in which the relevant input factors are observable. Level 3 fair values are determined with recognized valuation techniques relying on some inputs that cannot be observed in an active market. Management judgment is required in this case when selecting the valuation techniques and determining the inputs to be used. These inputs are developed using the best available information. If the Company uses its own data, it applies appropriate adjustments to best reflect market conditions.

PROVISIONS

The recognition and measurement of provisions is also based on assumptions about the probability that future events will occur and the amounts involved, together with an estimation of the discount rate. Again, past experience or reports from external experts are used as far as possible.

The measurement of pension provisions is based on actuarial assumptions as to discount rates, salary and pension trends, employee turnover rates and increases in healthcare costs. It additionally depends on the estimated growth in plan assets. Remeasurements are recognized in other comprehensive income and have no impact on profit or loss.

In the case of other provisions, expected values are used as the basis for measurement, which means that changes are made on a regular basis, involving either additions to the provisions or the reversal of unused provisions. Changes in the estimates of the amounts for other provisions are always recognized in profit or loss. The recognition and measurement of provisions for legal and litigation risks included within other provisions requires predictions with regard to decisions to be made by the courts and the outcome of legal proceedings. Each case is individually assessed on its merits based on developments in the proceedings, the Company's past experience in comparable situations and evaluations made by experts and lawyers.

DEFERRED TAX ASSETS AND UNCERTAIN INCOME TAX ITEMS

When determining deferred tax assets, there is a need to make assumptions about future taxable income and the timings for any recovery of the deferred tax assets. The measurement of deferred tax assets for tax loss carryforwards is generally based on future taxable income within a planning horizon of five fiscal years. In the recognition of uncertain income tax items, the expected tax payment is used as the basis for the best estimate.

Income Statement Disclosures

20. Net Income from Lending and Leasing Transactions before Provision for Credit Risks

The breakdown of net income from lending and leasing transactions before provision for credit risks is as follows:

€ million	2016	2015
Interest income from lending and money market transactions	1,336	1,307
Income from leasing transactions and service contracts	618	454
Expenses from leasing transactions and service contracts	–262	–162
Depreciation of and impairment losses on lease assets and investment property	–186	–164
Interest expense	–207	–194
Total	**1,299**	**1,241**

Interest income from lending and money market transactions and the income from leasing transactions include interest income on impaired loans and receivables amounting to a total of €8 million (previous year: €11 million). The interest income included here that relates to financial instruments not allocated to the category of financial assets or financial liabilities measured at fair value through profit or loss amounted to €1,342 million (previous year: €1,310 million). Interest income from lending and money market transactions also included income of €1 million (previous year: €0 million) arising from short-term borrowing in the form of collateral furnished by banks for derivatives.

Income from leasing transactions includes rental income from investment property amounting to €0 million (previous year: €1 million). As in the previous year, this income does not include any amounts from reversals of impairment losses on lease assets and investment property applied in prior years.

The impairment losses recognized as a result of the impairment test on lease assets amounted to €15 million (previous year: €26 million) and are included in the depreciation of impairment losses on lease assets. Impairment losses are based on continuously updated internal and external information, which is then fed into the forecasts of residual values for vehicles. Impairment losses on lease assets in the reporting year were not impacted by the diesel issue, although this had been the case in the previous year. In the previous year, some of the impairment losses were offset by support payments from the Volkswagen Group. Income from reversals of impairment losses on lease assets applied in prior years amounted to €6 million and is included in income from leasing business.

The interest expenses include funding expenses for the lending and leasing business, and an amount of €206 million (previous year: €190 million) relates to financial instruments not measured at fair value through profit or loss. Out of this amount, €–1 million (previous year: €–4 million) was offset against the net expense arising from interest income and expenses on derivatives in ineffective hedges in the reporting period.

Interest expenses included negative interest on money market transactions in an amount of €11 million (previous year: €1 million). This resulted primarily from the Bank's reserve balance at the ECB in excess of the minimum reserve requirement and from short-term deposits with domestic banks.

21. Provision for Credit Risks from Lending and Leasing Business

The provision for credit risks primarily relates to the loans to and receivables from customers item on the balance sheet. The breakdown of the provision for credit risks recognized in the consolidated income statement is as follows:

€ million	2016	2015
Additions to provision for credit risks	–295	–262
Reversals of provision for credit risks	273	208
Direct write-offs	–40	–37
Income from loans and receivables previously written off	23	19
Total	**–38**	**–71**

The provision for additional credit risks to which the Volkswagen Bank GmbH Group is exposed as a result of critical situations (economic crises, Brexit impact, block on sales of vehicles) in some European countries was decreased by €76 million in the year under review (previous year: decreased by €9 million).

22. Net Fee and Commission Income

The breakdown of net fee and commission income is as follows:

€ million	2016	2015
Fee and commission income	315	297
of which commissions from insurance broking	240	223
Fee and commission expenses	–345	–258
of which sales commission in the financing business[1]	–296	–213
Total	**–30**	**39**

1 The prior-year figures have been restated in line with the classification used in the reporting period. The previous prior-year figure was an expense of €34 million.

23. Net Gain/Loss on the Measurement of Derivative Financial Instruments and Hedged Items

This item includes the net gains or losses on hedges, on derivatives not designated as hedging instruments and on the measurement of foreign currency loans/receivables and liabilities.

The net gain or loss on hedges comprises gains and losses arising from the fair value measurement of hedging instruments and hedged items. Gains or losses on the ineffective portion of hedges and arising from changes in the fair value of derivatives that do not satisfy the IAS 39 requirements for hedge accounting are recognized under gains/losses on other derivatives not designated as hedging instruments.

The detailed breakdown of the gains and losses is as follows:

€ million	2016	2015
Gains/losses on hedging instruments in fair value hedges and cash flow hedges	462	–76
Gains/losses on hedged items in fair value hedges	–467	67
Ineffective portion of hedging instruments in cash flow hedges	–	0
Gains/losses on the measurement of foreign currency loans/receivables and liabilities	–	1
Gains/losses on derivatives not designated as hedging instruments	–4	18
Total	**–9**	**10**

24. General and Administrative Expenses

The breakdown of general and administrative expenses is shown in the following table:

€ million	2016	2015
Personnel expenses	–96	–91
Non-staff operating expenses	–690	–677
Advertising, public relations and sales promotion expenses	–33	–15
Depreciation of and impairment losses on property and equipment, amortization of and impairment losses on intangible assets	–10	–10
Other taxes	0	0
Total	**–829**	**–794**

Non-staff operating expenses include expenses of €23 million (previous year: €20 million) for assets (vehicles and real estate) leased under operating leases.

In accordance with the requirements specified in section 314(1) no. 9 of the HGB, the general and administrative expenses for fiscal year 2016 include the fees charged by the independent auditors as shown in the following table.

€ million	2016	2015
Financial statements audit services	1	1
Other attestation services	1	1
Tax consulting services	–	–
Other services	0	0
Total	**1**	**2**

25. Net Other Operating Income/Expenses

The breakdown of the net other operating income/expenses is as follows:

€ million	2016	2015
Income from cost allocations to other entities in the Volkswagen Group	215	189
Income from the reversal of provisions and deferred income	94	52
Miscellaneous operating income	55	28
Litigation and legal risk expenses	–77	–87
Other operating expenses	–31	–44
Net other operating income/expenses	**255**	**138**

The rise in other operating income includes support payments from VW FS AG.

26. Income Tax Expense

Income tax expense includes the taxes charged in respect of the Volkswagen Financial Services AG tax group, taxes for which the foreign subsidiaries and branches are the taxpayers, and deferred taxes. The components of the income tax expense are as follows:

€ million	2016	2015
Current tax expense, Germany	101	104
Current tax expense, foreign	42	53
Current income tax expense	**142**	**157**
of which income (–)/expense (+) related to prior periods	1	–1
Deferred tax income (–)/expense (+), Germany	**26**	**2**
Deferred tax income (–)/expense (+), foreign	**19**	**–2**
Deferred tax income (–)/expense (+)	44	0
Income tax expense	**186**	**157**

The reported tax expense in 2016 of €186 million (previous year: €157 million) is €12 million (previous year: €18 million) lower than the expected tax expense of €198 million (previous year: €175 million) calculated by applying a tax rate of 29.9% (previous year: 29.8%) to the consolidated profit before tax. The following reconciliation shows the relationship between the income tax expense and the profit before tax for the reporting period:

€ million	2016	2015
Profit before tax	**669**	**575**
multiplied by the domestic income tax rate of 29.9% (previous year: 29.8%)		
= Imputed income tax expense in the reporting period at the domestic income tax rate	**–200**	**–171**
+ Effects from tax credits	–	–
+ Effects from domestic/foreign tax rates	9	16
+ Effects from changes in tax rates	1	–
+ Effects from permanent differences	0	5
+ Effects from tax-exempt income	11	2
+ Effects from loss carryforwards	2	1
+ Effects from non-deductible operating expenses	–9	–4
+ Taxes attributable to prior periods	1	3
+ Other variances	–1	–7
= Current income tax expense	**–186**	**–157**

The statutory corporation tax rate in Germany for the 2016 assessment period was 15%. Including trade tax and the solidarity surcharge, this resulted in an aggregate tax rate of 29.9%.

The effects of different income tax rates outside Germany arise because of the different income tax rates in the individual countries in which the subsidiaries and branches have their registered offices compared with the rates in Germany. The rates outside Germany vary between 12.5% and 34.4% (previous year: 12.5% and 37.9%).

As of December 31, 2016, there were unused tax loss carryforwards of €13 million (previous year: €27 million) for which deferred tax assets of €3 million (previous year: €7 million) had been recognized. Of these unused tax loss carryforwards, €13 million (previous year: €27 million) can be used without any time restriction.

There were no unusable tax loss carryforwards (previous year: €5 million). Changes in tax rates have given rise to deferred tax expenses throughout the Group of €1 million (previous year: €0 million). No deferred tax assets have been recognized in the balance sheet for deductible temporary differences of €0 million (previous year: €10 million).

The Group has recognized deferred tax assets of €2 million (previous year: €17 million) against which there are no deferred tax liabilities in an equivalent amount. The branch involved is expecting to generate profits in the future following losses in the reporting and prior periods.

In accordance with IAS 12.39, deferred tax liabilities of €1 million (previous year: €1 million) have not been recognized for temporary differences and undistributed profits of subsidiaries because Volkswagen Bank GmbH has the relevant control.

Of the deferred taxes recognized in the balance sheet, an amount of €–4 million (previous year: €6 million) relates to transactions reported in other comprehensive income. Within this figure, an amount of €11 million (previous year: €10 million) relates to actuarial gains or losses (IAS 19), €0 million (previous year: €0 million) to derivative financial instruments and another €–15 million (previous year: €–4 million) to the fair value measurement of marketable securities.

27. Further Income Statement Disclosures

The figures reported for fiscal years 2015 and 2016 do not include any commission income not accounted for using the effective interest method.

Balance Sheet Disclosures

28. Cash Reserve

The cash reserve primarily includes credit balances of €1,363 million (previous year: €1,261 million) held with Deutsche Bundesbank.

29. Loans to and receivables from customers

Loans to and receivables from customers largely comprise loans to private and commercial customers for the financing of vehicles. The vehicle itself is normally pledged to us as collateral for the financing of vehicles. Dealer financing encompasses floor plan financing as well as loans to the dealer organization for operating equipment and investment. Assets are pledged as collateral, but guarantees and charges on real estate are also used as security. Receivables from leasing transactions include receivables from finance leases and receivables due in connection with lease assets. Other loans and receivables primarily relate to lines of credit and overdrafts drawn down by customers as well as loans to and receivables from Volkswagen Group entities. They include subordinated loans in an amount of €1,148 million (previous year: €1,274 million).

Some of the fixed-income exposures under loans/receivables from retail financing have been hedged against fluctuations in the risk-free base interest rate using a portfolio fair value hedge.

The reconciliation to the balance sheet values is as follows:

€ million	Dec. 31, 2016	Dec. 31, 2015
Loans to and receivables from customers	**45,667**	**40,806**
Fair value adjustment from portfolio hedging	2	5
Loans to and receivables from customers, net of fair value adjustment from portfolio hedging	45,666	40,802

Receivables from leasing transactions include due receivables amounting to €27 million (previous year: €19 million). Of this amount, €24 million (previous year: €18 million) is attributable to finance leases and €3 million (previous year: €1 million) to operating leases. The due lease receivables are payable within three months.

The breakdown of receivables from finance leases as of December 31, 2015 and December 31, 2016 was as follows:

€ million	2016	2017 – 2020	From 2021	Total
Future payments from finance lease receivables	892	1,740	23	2,655
Unearned finance income from finance leases (discounting)	–68	–86	–1	–155
Present value of minimum lease payments outstanding at the reporting date	824	1,654	22	2,500

€ million	2017	2018 – 2021	From 2022	Total
Future payments from finance lease receivables	1,067	2,094	19	3,180
Unearned finance income from finance leases (discounting)	–73	–95	–1	–169
Present value of minimum lease payments outstanding at the reporting date	994	1,999	18	3,011

In the Volkswagen Bank GmbH Group, the present value of the minimum lease payments outstanding as of the reporting date equates to the net receivables from finance leases disclosed above. The provision for credit risks in respect of uncollectible outstanding minimum lease payments amounted to €1 million (previous year: €1 million).

30. Provision for Credit Risks from Lending and Leasing Business

The provision for credit risks from lending and leasing business is recognized in accordance with standard rules applicable throughout the Group and covers all identifiable credit risks.

The provision for credit risks has been recognized in respect of loans to and receivables from customers. At the end of the reporting period, valuation allowances of €308 million (previous year: €384 million) had been recognized in relation to loans and receivables in countries subject to additional credit risk as a result of various critical situations (economic crises, Brexit impact, block on sales of vehicles).

€ million	Specific valuation allowances	Portfolio-based valuation allowances	2016	Specific valuation allowances	Portfolio-based valuation allowances	2015
Balance as of Jan. 1	**490**	**703**	**1,193**	**486**	**709**	**1,195**
Exchange rate and other changes	–1	–2	–3	0	0	1
Changes in basis of consolidation	4	1	5	9	3	12
Additions	182	83	265	158	87	246
Utilization	50	–	50	61	–	61
Reversals	92	178	270	99	101	200
Reclassification	–1	1	–	–4	4	–
Balance as of Dec. 31	**532**	**608**	**1,140**	**490**	**703**	**1,193**

31. Derivative Financial Instruments

This item comprises the positive fair values from hedges and from derivatives not designated as a hedging instrument. The breakdown is as follows:

€ million	Dec. 31, 2016	Dec. 31, 2015
Transactions to hedge against		
currency risk on assets using fair value hedges	175	93
currency risk on liabilities using fair value hedges	–	–
interest-rate risk using fair value hedges	38	43
interest-rate risk using cash flow hedges	–	–
currency and pricing risk on future cash flows using cash flow hedges	0	0
Hedging transactions	**213**	**137**
Assets arising from derivatives not designated as hedges	8	16
	221	**153**

32. Marketable Securities

Marketable securities largely comprised purchased government bonds amounting to €2,186 million (previous year: €2,222 million) and asset-backed securities issued by special purpose entities of the following: Volkswagen Finance S.A., Madrid in the amount of €285 million (previous year: €223 million); Volkswagen Leasing GmbH, Braunschweig in the amount of €631 million (previous year: €101 million); and Volkswagen Financial Services (UK) Limited, Milton Keynes, United Kingdom in the amount of €1,348 million (previous year: none). These special purpose entities are structured entities not consolidated by Volkswagen Bank GmbH. The relevant disclosures can be found in note 69.

Marketable securities with a total value of €2,657 million (previous year: €2,106 million) have been pledged as collateral for Volkswagen Bank GmbH's own liabilities. They are deposited at Deutsche Bundesbank and are furnished as collateral in connection with open market operations.

In the prior year, an investment in Visa Europe Ltd. had been reported under marketable securities. Following the announcement of Visa Inc.'s acquisition of Visa Europe Ltd. in the second quarter of 2016, the investment was measured at fair value using an offer to buy as the basis, taking into account appropriate discounts for liquidity and the risk of potential changes in the offer to buy. The fair value was based on input factors under Level 3 of the fair value hierarchy specified in IFRS 13. The measurement of the investment at fair value in the previous year had given rise to a gain of €12 million, which had been recognized in other comprehensive income, taking into account deferred taxes. As a non-current asset within the meaning of IFRS 5, the investment had been classified as held for sale in the 2015 reporting period and allocated to the Germany segment.

Visa Inc. completed its acquisition of Visa Europe Ltd. in the reporting period. As a consequence, the investment in Visa Europe Ltd. was sold and the associated reserves in equity for available-for-sale financial assets were reversed. The consideration received gave rise to a gain of €14 million, which was reported under net gain/loss on marketable securities and miscellaneous financial assets.

The preferred shares in Visa Inc. acquired as part of the deal will be converted into ordinary shares in Visa Inc. using a predetermined ratio within a specified period. The shares were measured using the market price of shares in Visa Inc. as of the reporting date, which thus represented an input under Level 2 of the fair value hierarchy.

33. Miscellaneous Financial Assets

€ million	Miscellaneous financial assets
Gross carrying amount as of Jan. 1, 2015	**3**
Foreign exchange differences	0
Changes in basis of consolidation	–
Additions	–
Reclassifications	–
Disposals	0
Changes recognized in profit or loss	–
Dividends	–
Other changes recognized in other comprehensive income	–
Balance as of Dec. 31, 2015	**3**
Impairment losses Balance as of Jan. 1, 2015	**–**
Foreign exchange differences	–
Changes in basis of consolidation	–
Additions	–
Reclassifications	–
Disposals	–
Reversal of impairment losses	–
Balance as of Dec. 31, 2015	**–**
Net carrying amount as of Dec. 31, 2015	**3**
Net carrying amount as of Jan. 1, 2015	**3**

€ million	Miscellaneous financial assets
Gross carrying amount as of Jan. 1, 2016	**3**
Foreign exchange differences	0
Changes in basis of consolidation	–
Additions	–
Reclassifications	–
Disposals	–
Changes recognized in profit or loss	–
Dividends	–
Other changes recognized in other comprehensive income	–
Balance as of Dec. 31, 2016	**3**
Impairment losses Balance as of Jan. 1, 2016	**–**
Foreign exchange differences	–
Changes in basis of consolidation	–
Additions	–
Reclassifications	–
Disposals	–
Reversal of impairment losses	–
Balance as of Dec. 31, 2016	**–**
Net carrying amount as of Dec. 31, 2016	**3**
Net carrying amount as of Jan. 1, 2016	**3**

34. Intangible Assets

€ million	Brand names	Goodwill	Capitalized development costs for products under development	Capitalized development costs for products currently in use	Other intangible assets	Total
Cost						
Balance as of Jan. 1, 2015	**6**	**18**	**–**	**–**	**64**	**88**
Foreign exchange differences	0	0	–	–	0	0
Changes in basis of consolidation	–	–	–	–	0	0
Additions	–	–	–	–	4	4
Reclassifications	–	–	–	–	–	–
Disposals	–	–	–	–	0	0
Balance as of Dec. 31, 2015	**6**	**18**	**–**	**–**	**68**	**92**
Amortization and impairment losses						
Balance as of Jan. 1, 2015	**–**	**–**	**–**	**–**	**42**	**42**
Foreign exchange differences	–	–	–	–	–0	–0
Changes in basis of consolidation	–	–	–	–	0	0
Additions to cumulative depreciation	–	–	–	–	7	7
Additions to cumulative impairment losses	–	–	–	–	–	–
Reclassifications	–	–	–	–	–	–
Disposals	–	–	–	–	0	0
Reversal of impairment losses	–	–	–	–	–	–
Balance as of Dec. 31, 2015	**–**	**–**	**–**	**–**	**49**	**49**
Net carrying amount as of Dec. 31, 2015	**6**	**18**	**–**	**–**	**19**	**43**

€ million	Brand names	Goodwill	Capitalized development costs for products under development	Capitalized development costs for products under currently in use	Other intangible assets	Total
Cost						
Balance as of Jan. 1, 2016	**6**	**18**	**–**	**–**	**68**	**92**
Foreign exchange differences	0	–1	–	–	–1	–2
Changes in basis of consolidation	–	–	–	–	1	1
Additions	–	–	–	–	4	4
Reclassifications	–	–	–	–	–	–
Disposals	–	–	–	–	1	1
Balance as of Dec. 31, 2016	**6**	**17**	**–**	**–**	**72**	**95**
Amortization and impairment losses						
Balance as of Jan. 1, 2016	**–**	**–**	**–**	**–**	**49**	**49**
Foreign exchange differences	–	–	–	–	0	0
Changes in basis of consolidation	–	–	–	–	1	1
Additions to cumulative depreciation	–	–	–	–	7	7
Additions to cumulative impairment losses	–	–	–	–	–	–
Reclassifications	–	–	–	–	–	–
Disposals	–	–	–	–	0	0
Reversal of impairment losses	–	–	–	–	–	–
Balance as of Dec. 31, 2016	**–**	**–**	**–**	**–**	**56**	**56**
Net carrying amount as of Dec. 31, 2016	**6**	**17**	**–**	**–**	**16**	**39**

The goodwill of €17 million (previous year: €18 million) and the brand names of €6 million (previous year: €6 million) reported as of the balance sheet date resulted from the acquisition of Volkswagen Bank Polska S.A. These intangible assets have indefinite useful lives. The indefinite useful life arises because goodwill and brand names are linked to the relevant cash-generating unit and will therefore remain in existence for as long as this unit also remains in existence. The acquired customer base of Volkswagen Bank Polska S.A. is amortized over ten years.

The impairment tests for the reported goodwill are based on the value in use. The values in use determined for the reported goodwill in the impairment tests exceeded the corresponding carrying amounts, so no impairment loss requirement was identified for any of the reported goodwill. Sensitivity analyses were also carried out as part of the impairment tests. No conceivable change in a material assumption would lead to the recognition of an impairment loss for goodwill. As of the reporting date, intangible assets with indefinite useful lives amounted to €24 million (previous year: €25 million).

35. Property and Equipment

Mio. €	Land, land rights and buildings, including buildings on third-party lands	Technical equipment and machinery	Other equipment, operating and office equipment	Payments on account and assets under construction	Total
Cost					
Balance as of Jan. 1, 2015	**21**	**0**	**21**	**0**	**42**
Foreign exchange differences	0	0	0	0	0
Changes in basis of consolidation	–	0	0	–	0
Additions	0	0	2	0	2
Reclassifications	–	0	–	–	–
Disposals	–	–	3	–	3
Balance as of Dec. 31, 2015	**21**	**0**	**21**	**0**	**42**
Amortization and impairment losses					
Balance as of Jan. 1, 2015	**16**	**–**	**14**	**–**	**30**
Foreign exchange differences	0	–	0	–	0
Changes in basis of consolidation	–	–	0	–	0
Additions to cumulative depreciation	1	–	2	–	3
Additions to cumulative impairment losses	–	–	–	–	–
Reclassifications	–	–	–	–	–
Disposals	–	0	1	–	1
Reversal of impairment losses	–	0	–	–	–
Balance as of Dec. 31, 2015	**17**	**–**	**15**	**–**	**32**
Net carrying amount as of Dec. 31, 2015	**4**	**0**	**6**	**0**	**10**
of which assets leased under finance leases Carrying amount as of Dec. 31, 2015	–	–	–	–	–

€ million	Land, land rights and buildings, including buildings on third-party lands	Technical equipment and machinery	Other equipment, operating and office equipment	Payments on account and assets under construction	Total
Cost					
Balance as of Jan. 1, 2016	**21**	**0**	**21**	**0**	**42**
Foreign exchange differences	0	0	0	0	0
Changes in basis of consolidation	–	0	0	–	0
Additions	0	0	1	1	2
Reclassifications	0	0	0	0	–
Disposals	0	–	1	–	1
Balance as of Dec. 31, 2016	**21**	**0**	**21**	**1**	**42**
Amortization and impairment losses					
Balance as of Jan. 1, 2016	**17**	**–**	**15**	**–**	**32**
Foreign exchange differences	0	–	0	–	0
Changes in basis of consolidation	–	–	0	–	0
Additions to cumulative depreciation	1	–	2	–	3
Additions to cumulative impairment losses	–	–	–	–	–
Reclassifications	–	–	–	–	–
Disposals	0	0	1	–	1
Reversal of impairment losses	–	0	–	–	–
Balance as of Dec. 31, 2016	**17**	**–**	**16**	**–**	**33**
Net carrying amount as of Dec. 31, 2016	**3**	**0**	**5**	**1**	**9**
of which assets leased under finance leases Carrying amount as of Dec. 31, 2016	–	–	–	–	–

Assets under construction with a carrying amount of €1 million (previous year: €0 million) are included in land and buildings.

36. Lease Assets and Investment Property

€ million	Movable lease assets	Investment property	Total
Cost			
Balance as of Jan. 1, 2015	**636**	**3**	**640**
Foreign exchange differences	–	–	–
Changes in basis of consolidation	–	–	–
Additions	497	–	497
Reclassifications	–	–	–
Disposals	128	–	128
Balance as of Dec. 31, 2015	**1,005**	**3**	**1,008**
Depreciation and impairment losses			
Balance as of Jan. 1, 2015	**149**	**2**	**152**
Foreign exchange differences	–	–	–
Changes in basis of consolidation	–	–	–
Additions to cumulative depreciation	139	0	139
Additions to cumulative impairment losses	26	–	26
Reclassifications	–	–	–
Disposals	18	–	18
Reversal of impairment losses	–	–	–
Balance as of Dec. 31, 2015	**296**	**2**	**298**
Net carrying amount as of Dec. 31, 2015	**710**	**1**	**711**
Net carrying amount as of Jan. 1, 2015	**487**	**1**	**488**

€ million	Movable lease assets	Investment property	Total
Cost			
Balance as of Jan. 1, 2016	**1,005**	**3**	**1,008**
Foreign exchange differences	–	–	–
Changes in basis of consolidation	–	–	–
Additions	458	–	458
Reclassifications	–	–	–
Disposals	252	1	253
Balance as of Dec. 31, 2016	**1,211**	**3**	**1,213**
Depreciation and impairment losses			
Balance as of Jan. 1, 2016	**296**	**2**	**298**
Foreign exchange differences	–	–	–
Changes in basis of consolidation	–	–	–
Additions to cumulative depreciation	171	0	171
Additions to cumulative impairment losses	15	–	15
Reclassifications	–	–	–
Disposals	142	1	143
Reversal of impairment losses	6	–	6
Balance as of Dec. 31, 2016	**334**	**2**	**335**
Net carrying amount as of Dec. 31, 2016	**877**	**1**	**878**
Net carrying amount as of Jan. 1, 2016	**710**	**1**	**711**

Since the fair value of investment property could not be determined without undue cost and effort, this item is carried at amortized cost in an amount of €1 million (previous year: €1 million). Operating expenses in an immaterial amount were incurred for the maintenance of investment property in both the reporting period and in the previous year.

We expect payments from noncancelable leases and rental agreements of €154 million in 2017 and of €145 million in the period 2018 to 2021.

37. Deferred Tax Assets

The deferred tax assets comprise deferred income tax assets only, the breakdown of which is as follows:

€ million	Dec. 31, 2016	Dec. 31, 2015
Deferred tax assets	2,735	2,954
of which noncurrent	86	189
Recognized benefit from unused tax loss carryforwards, net of valuation allowances	3	5
of which noncurrent	3	5
Offset (with deferred tax liabilities)	–1,526	–1,528
Total	**1,212**	**1,431**

Deferred tax assets are recognized in connection with the following balance sheet items:

€ million	Dec. 31, 2016	Dec. 31, 2015
Loans, receivables and other assets	106	36
Marketable securities and cash	2,541	2,753
Intangible assets/property and equipment	3	8
Lease assets	–	–
Liabilities and provisions	85	156
Valuation allowances for deferred tax assets on temporary differences	–	–
Total	**2,735**	**2,954**

38. Other Assets

The details of other assets are as follows:

€ million	Dec. 31, 2016	Dec. 31, 2015
Vehicles returned for disposal	23	25
Restricted cash	193	322
Prepaid expenses	30	29
Other tax assets	50	50
Miscellaneous	101	164
Total	**396**	**589**

39. Noncurrent Assets

€ million	Dec. 31, 2016	of which noncurrent	Dec. 31, 2015	of which noncurrent
Cash reserve	1,457	–	1,352	–
Loans to and receivables from banks	1,944	322	1,501	–
Loans to and receivables from customers	45,667	22,765	40,806	20,854
Derivative financial instruments	221	150	153	61
Marketable securities	4,455	–	2,557	–
Miscellaneous financial assets	3	3	3	3
Intangible assets	39	39	43	43
Property and equipment	9	9	10	10
Lease assets	877	877	710	710
Investment property	1	1	1	1
Current tax assets	53	–	50	0
Other assets	396	29	589	29
Total	**55,122**	**24,195**	**47,775**	**21,710**

40. Liabilities to Banks and Customers

The liabilities to banks mainly comprise liabilities to Deutsche Bundesbank arising from targeted longer-term refinancing operations.

To cover the capital requirements for the leasing and financing activities, the entities in the Volkswagen Bank GmbH Group make use, among other things, of the funds provided by the Volkswagen Group.

The liabilities to customers item primarily contains customer deposits, such as overnight money and time deposits, as well as various savings bonds and savings plans. In terms of maturity, the “Direkt-Sparplan” and “Plus Sparbrief” savings products currently offer the longest investment horizon. The maximum maturity is ten years.

The reconciliation to the balance sheet values is as follows:

€ million	Dec. 31, 2016	Dec. 31, 2015
Liabilities to customers	**37,938**	**30,478**
Fair value adjustment from portfolio hedging	–	–
Liabilities to customers, net of fair value adjustment from portfolio hedging	37,938	30,478

41. Notes, Commercial Paper Issued

This item comprises bonds and commercial paper.

€ million	Dec. 31, 2016	Dec. 31, 2015
Bonds issued	4,206	7,530
Commercial paper issued	105	74
Total	**4,311**	**7,604**

42. ABS Transactions

The Volkswagen Bank GmbH Group uses ABS transactions for funding purposes. The related liabilities are recognized in the following balance sheet items:

€ million	Dec. 31, 2016	Dec. 31, 2015
Notes, commercial paper issued	2,371	3,840
Subordinated capital	120	188
Total	**2,491**	**4,028**

The asset-backed securities of Volkswagen Bank GmbH are backed exclusively by financial assets. The corresponding carrying amount of the securitized loans and receivables from retail financing is €2,404 million (previous year: €3,859 million). As of December 31, 2016, the fair value of the liabilities amounted to €2,499 million (previous year: €4,052 million). The fair value of the assigned loans and receivables that continue to be recognized, amounted to €2,477 million (previous year: €3,954 million) as of December 31, 2016. Security is provided in the form of loans and receivables from retail financing as well as cash collateral amounting to €2,482 million (previous year: €3,984 million). In these arrangements, the expected payments are assigned to special purpose entities and the ownership of the collateral in the financed vehicles is transferred. The assigned loans/receivables cannot be assigned again to anyone else or used in any other way as collateral. The rights of the bond holders are limited to the assigned loans/receivables and the payment receipts arising from these loans/receivables are used to repay the corresponding liability.

These asset-backed securities transactions did not lead to the derecognition of the loans or receivables from the financing business because the credit risk and timing risk were retained in the Group. The difference between the amount of the assigned loans/receivables and the associated liabilities results from the different terms and conditions and from the proportion of the ABSs held by Volkswagen Bank GmbH itself.

The Volkswagen Bank GmbH Group is under a contractual obligation to transfer funds in certain circumstances to the structured entities included in its consolidated financial statements. As the loans/receivables are transferred to the special purpose entity by way of undisclosed assignment, it is possible that the loan/receivable has already been reduced in a legally binding manner at the originator, for example if the debtor effectively offsets it against amounts it is owed by the Volkswagen Bank GmbH Group. In this case, collateral must be furnished for the resulting compensation claims against the special purpose entity, for example if the rating of the relevant Group company falls to a contractually specified reference value.

The ABS transactions in the Volkswagen Bank GmbH Group can be repaid early (with a clean-up call) when less than 10% of the original transaction volume remains outstanding.

43. Derivative Financial Instruments

This item comprises the negative fair values from hedges and from derivatives not designated as a hedging instrument. The breakdown is as follows:

€ million	Dec. 31, 2016	Dec. 31, 2015
Transactions to hedge against		
currency risk on assets using fair value hedges	25	3
currency risk on liabilities using fair value hedges	–	9
interest-rate risk using fair value hedges	3	21
interest-rate risk using cash flow hedges	–	–
currency and pricing risk on future cash flows using cash flow hedges	0	0
Hedging transactions	**28**	**34**
Liabilities arising from derivatives not designated as hedges	15	13
Total	**43**	**46**

44. Provisions

The provisions break down as follows:

€ million	Dec. 31, 2016	Dec. 31, 2015
Provisions for pensions and other post-employment benefits	52	49
Other provisions	372	327
of which provisions for litigation and legal risks	282	246
of which for staff	20	19
of which other	70	62
Total	**425**	**376**

PROVISIONS FOR PENSIONS AND OTHER POST-EMPLOYMENT BENEFITS

The following amounts have been recognized in the balance sheet for benefit commitments:

€ million	Dec. 31, 2016	Dec. 31, 2015
Present value of funded obligations	13	12
Fair value of plan assets	12	11
Funded status (net)	1	1
Present value of unfunded obligations	51	49
Amount not recognized as an asset because of the ceiling in IAS 19	–	–
Net liability recognized in the balance sheet	**52**	**49**
of which provisions for pensions	52	49
of which other assets	–	–

Key pension arrangements in the Volkswagen Bank GmbH Group

For the period after the active working life of employees, Volkswagen Bank GmbH offers its employees benefits under attractive, state-of-the-art occupational pension arrangements. Most of the arrangements in the Volkswagen Bank GmbH Group are pension plans for employees in Germany classified as defined benefit plans under IAS 19. The majority of these obligations are funded by provisions recognized in the balance sheet. These plans are now closed for new members. To reduce the risks associated with defined benefit plans, in particular longevity, salary increases and inflation, the Volkswagen Bank GmbH Group has introduced new defined benefit plans in recent years in which the benefits are funded by appropriate external plan assets. The risks referred to above have been significantly reduced in these pension plans. The proportion of the total defined benefit obligation attributable to pension obligations funded by plan assets will continue to rise in the future. The main pension commitments are described below.

German pension plans funded solely by provisions

The pension plans funded solely by recognized provisions comprise both defined contribution plans with guarantees and final salary plans. For defined contribution plans, an annual pension expense dependent on income and status is converted into a lifelong pension entitlement using annuity factors (guaranteed modular pension entitlements). The annuity factors include a guaranteed rate of interest. The modular pension entitlements earned annually are added together at retirement. For final salary plans, the underlying salary is multiplied at retirement by a percentage that depends on the years of service up to the retirement date. The present value of the guaranteed obligation rises as interest rates fall and is therefore exposed to interest rate risk. The pension system provides for lifelong pension payments. The companies therefore bear the longevity risk. This is accounted for by calculating the annuity factors and the present value of the guaranteed obligation using the latest generational mortality tables – the "Heubeck 2005 G" mortality tables – which already reflect future increases in life expectancy. To reduce the inflation risk from adjusting the regular pension payments by the rate of inflation, a pension adjustment that is not indexed to inflation was introduced for pension plans where this is permitted by law.

German pension plans funded by external plan assets

The pension plans funded by external plan assets are defined contribution plans with guarantees. In this case, an annual pension expense dependent on income and status is either converted into a lifelong pension entitlement using annuity factors (guaranteed modular pension entitlement) or paid out in a single lump sum or in installments. In some cases, employees also have the opportunity to provide for their own retirement through deferred remuneration. The annuity factors include a guaranteed rate of interest. The modular pension entitlements earned annually are added together at retirement. The pension expense is contributed on an ongoing basis to a separate pool of assets that is administered in trust independently of the Company and invested in the capital markets. If the plan assets exceed the present value of the obligations calculated using the guaranteed rate of interest, surpluses are allocated (modular pension bonuses). As the assets administered in trust meet the IAS 19 criteria for classification as plan assets, they are offset against the obligations.

The amount of the pension assets is exposed to general market risk. The investment strategy and its implementation are therefore continuously monitored by the trusts' governing bodies, on which the companies are also represented. For example, investment policies are stipulated in investment guidelines with the aim of limiting market risk and its impact on plan assets. In addition, asset-liability management analyses are conducted at regular intervals so as to ensure that investments are in line with the obligations that need to be covered. The pension assets are currently invested primarily in fixed-income or equity funds. The main risks are therefore interest rates and equity prices. To mitigate market risk, the pension system also provides for cash funds to be set aside in an equalization reserve before any surplus is allocated.

The present value of the obligation is reported as the maximum of the present value of the guaranteed obligation and of the plan assets. If the value of the plan assets falls below the present value of the guaranteed obligation, a provision must be recognized for the difference. The present value of the guaranteed obligation rises as interest rates fall and is therefore exposed to interest rate risk. In the case of lifelong pension payments, the Volkswagen Bank GmbH Group bears the longevity risk. This is accounted for by calculating the annuity factors and the present value of the guaranteed obligation using the latest generational mortality tables – the "Heubeck 2005 G" mortality tables – which already reflect future increases in life expectancy. In addition, independent actuaries carry out annual risk monitoring as part of the review of the assets administered by the trusts.

To reduce the inflation risk from adjusting the regular pension payments by the rate of inflation, a pension adjustment that is not indexed to inflation was introduced for pension plans where this is permitted by law. The calculation of the present value of the defined benefit obligations was based on the following actuarial assumptions:

	GERMANY		INTERNATIONAL	
Percent	Dec. 31, 2016	Dec. 31, 2015	Dec. 31, 2016	Dec. 31, 2015
Discount rate	1.80	2.70	1.60 – 2.60	2.60 – 3.60
Pay trend	3.60	3.40	–	2.00 – 3.00
Pension trend	1.50	1.70	0.80 – 3.30	2.00 – 3.10
Staff turnover rate	0.95	0.75	1.50 – 2.40	1.50 – 2.10
Annual increase in healthcare costs	–	–	–	2.00

These assumptions are averages that were weighted using the present value of the defined benefit obligation.

With regard to life expectancy, the latest mortality tables in every country are taken into account. For example, in Germany calculations are based on the "2005 G" generational mortality tables developed by Professor Dr. Klaus Heubeck. The discount rates are generally determined to reflect the yields on prime-rated corporate bonds with matching maturities and currencies. The iBoxx AA 10+ Corporates index was taken as the basis for the obligations of German Group companies. Similar indices were used for foreign pension obligations.

The pay trends cover expected wage and salary trends, which also include increases attributable to career development. The pension trends either reflect the contractually guaranteed pension adjustments or are based on the rules on pension adjustments in force in each country. The employee turnover rates are based on past experience and future expectations.

The following table shows changes in the net defined benefit liability recognized in the balance sheet:

€ million	2016	2015
Net liability recognized in the balance sheet as of January 1	**49**	**54**
Current service cost	0	0
Net interest expense	1	1
Actuarial gains (–)/losses (+) arising from changes in demographic assumptions	2	0
Actuarial gains (–)/losses (+) arising from changes in financial assumptions	5	–3
Actuarial gains (–)/losses (+) arising from experience adjustments	–1	0
Income/expenses from plan assets not included in interest income	1	0
Change in amount not recognized as an asset because of the ceiling in IAS 19	–	0
Employer contributions to plan assets	0	0
Employee contributions to plan assets	–	–
Pension payments from company assets	3	3
Past service cost (including plan curtailments)	–	0
Gains (–) or losses (+) arising from plan settlements	–	–
Changes in basis of consolidation	0	–
Other changes	0	0
Foreign exchange differences from foreign plans	0	0
Net liability recognized in the balance sheet as of December 31	**52**	**49**

The change in the present value of the defined benefit obligation is attributable to the following factors:

€ million	2016	2015
Present value of obligations as of January 1	**60**	**64**
Current service cost	0	0
Interest cost (unwinding of discount on obligations)	2	2
Actuarial gains (–)/losses (+) arising from changes in demographic assumptions	2	0
Actuarial gains (–)/losses (+) arising from changes in financial assumptions	5	–3
Actuarial gains (–)/losses (+) arising from experience adjustments	–1	0
Employee contributions to plan assets	0	0
Pension payments from company assets	3	3
Pension payments from plan assets	0	0
Past service cost (including plan curtailments)	–	0
Gains (–) or losses (+) arising from plan settlements	–	–
Changes in basis of consolidation	0	–
Other changes	0	0
Foreign exchange differences from foreign plans	–1	0
Present value of obligations as of December 31	**64**	**60**

Changes in the relevant actuarial assumptions would have had the following effects on the defined benefit obligation:

Present value of defined benefit obligation if		DEC. 31, 2016		DEC. 31, 2015	
		€ million	Change in percent	€ million	Change in percent
Discount rate	is 0.5 percentage points higher	60	–6.46	56	–6.17
	is 0.5 percentage points lower	69	7.23	64	7.05
Pension trend	is 0.5 percentage points higher	67	4.63	63	4.80
	is 0.5 percentage points lower	61	–4.32	57	–4.41
Pay trend	is 0.5 percentage points higher	64	0.01	60	0.01
	is 0.5 percentage points lower	64	–0.01	60	–0.01
Longevity	increases by one year	66	3.48	62	3.16

The sensitivity analysis shown above considers the change in one assumption at a time, leaving the other assumptions unchanged versus the original calculation. In other words, any correlation effects between the individual assumptions are ignored.

To examine the sensitivity of the present value of the defined benefit obligation to a change in assumed longevity, the estimates of mortality were reduced as part of a comparative calculation by a measure that was roughly equivalent to an increase in life expectancy of one year.

The average duration of the defined benefit obligation weighted by the present value of the defined benefit obligation (Macaulay duration) is 14 years (previous year: 13 years).

The following table shows a breakdown of the present value of the defined benefit obligation by category of plan member:

€ million	2016	2015
Active members with pension entitlements	3	3
Members with vested entitlements who have left the Company	14	12
Retirees	47	45
Total	**64**	**60**

The maturity profile of payments attributable to the defined benefit obligation is presented in the following table, which classifies the present value of the obligation by the maturity of the underlying payments:

€ million	2016	2015
Payments due within the next fiscal year	3	0
Payments due between two and five years	11	4
Payments due in more than five years	50	56
Total	**64**	**60**

Changes in plan assets are shown in the following table:

€ million	2016	2015
Fair value of plan assets as of January 1	**11**	**10**
Interest income on plan assets determined using the discount rate	0	0
Income/expenses from plan assets not included in interest income	1	0
Employer contributions to plan assets	0	0
Employee contributions to plan assets	0	0
Pension payments from plan assets	0	0
Gains (+) or losses (–) arising from plan settlements	–	–
Changes in basis of consolidation	–	–
Other changes	0	0
Foreign exchange differences from foreign plans	–1	0
Fair value of plan assets as of December 31	**12**	**11**

The investment of the plan assets to cover future pension obligations resulted in income in the amount of €1 million (previous year: €1 million). Employer contributions to plan assets are expected to amount to €1 million (previous year: €1 million) in the next fiscal year.

Plan assets are invested in the following asset classes:

€ million	DEC. 31, 2016			DEC. 31, 2015		
	Quoted prices in active markets	No quoted prices in active markets	Total	Quoted prices in active markets	No quoted prices in active markets	Total
Cash and cash equivalents	0	–	0	0	–	0
Equity instruments	2	–	2	2	–	2
Debt instruments	7	–	7	7	–	7
Direct investments in real estate	–	–	–	–	–	–
Derivatives	1	–	1	1	–	1
Equity funds	0	–	0	0	–	0
Bond funds	1	–	1	1	–	1
Real estate funds	0	–	0	0	–	0
Other funds	1	–	1	1	–	1
Asset-backed securities	–	–	–	–	–	–
Structured debt securities	–	–	–	–	–	–
Other	0	–	0	0	–	0

Of the total plan assets, 9% (previous year: 6%) is invested in German assets, 90% (previous year: 93%) in other European assets and 1% (previous year: 1%) in assets in other regions. Investments of plan assets in debt instruments issued by the Volkswagen Group are of minor significance.

The following amounts have been recognized in the income statement:

€ million	2016	2015
Current service cost	0	0
Net interest on the net defined benefit liability	1	1
Past service cost (including plan curtailments)	–	0
Gains (–) or losses (+) arising from plan settlements	–	–
Net income (–) and expenses (+) recognized in profit or loss	**1**	**1**

OTHER PROVISIONS

The following table shows the changes in other provisions, including maturities:

€ million	Employee expenses	Litigation and legal risks	Other provisions	Total
Balance as of Jan. 1, 2015	**18**	**234**	**68**	**319**
Foreign exchange differences	0	–	0	0
Changes in basis of consolidation	–	–	0	0
Utilized	11	59	14	85
Additions/new provisions	15	85	34	134
Unwinding of discount/effect of change in discount rate	–	–	–	–
Reversals	3	14	25	42
Balance as of Dec. 31, 2015	**19**	**246**	**62**	**327**
of which current	18	131	47	196
of which noncurrent	1	115	15	131
Balance as of Jan. 1, 2016	**19**	**246**	**62**	**327**
Foreign exchange differences	0	–	0	0
Changes in basis of consolidation	–	–	–	–
Utilized	14	0	4	18
Additions/new provisions	20	76	51	146
Unwinding of discount/effect of change in discount rate	–	3	–	3
Reversals	4	42	39	85
Balance as of Dec. 31, 2016	**20**	**282**	**70**	**372**
of which current	20	126	67	212
of which noncurrent	0	157	3	160

Provisions for employee expenses have been recognized for annually recurring bonuses, long-service awards and other employee expenses.

The provisions for litigation and legal risks reflect the risks identified as of the reporting date in relation to claims and legal expenses arising from the latest decisions by the courts and from ongoing civil proceedings involving dealers and other customers. Based on analysis of the individual matters covered by the provisions, we believe that the disclosure of further detailed information on individual proceedings, legal disputes or legal risks could seriously prejudice the course or initiation of proceedings.

The miscellaneous provisions also include provisions for indirect credit risks amounting to €40 million (previous year: €38 million).

The timing of the cash outflows in connection with other provisions is expected to be as follows: 57% in the next year and 43% in the years 2018 to 2021.

45. Deferred Tax Liabilities

The breakdown of the deferred tax liabilities is as follows:

€ million	Dec. 31, 2016	Dec. 31, 2015
Deferred tax liabilities	2,596	2,764
of which noncurrent	1,021	1,278
Offset (with deferred tax assets)	–1,526	–1,528
Total	**1,070**	**1,237**

The deferred tax liabilities include taxes arising on temporary differences between amounts in the IFRS financial statements and those determined in the calculation of taxable profits in the Group entities.

Deferred tax liabilities have been recognized in connection with the following balance sheet items:

€ million	Dec. 31, 2016	Dec. 31, 2015
Loans, receivables and other assets	643	979
Marketable securities and cash	70	78
Intangible assets/property and equipment	3	4
Lease assets	34	27
Liabilities and provisions	1,846	1,676
Total	**2,596**	**2,764**

46. Other Liabilities

The details of other liabilities are as follows:

€ million	Dec. 31, 2016	Dec. 31, 2015
Deferred income	97	83
Other tax liabilities	39	27
Social security and payroll liabilities	20	20
Miscellaneous	60	20
Total	**217**	**150**

47. Subordinated Capital

The breakdown of subordinated capital is as follows:

€ million	Dec. 31, 2016	Dec. 31, 2015
Subordinated liabilities	155	226
of which: to other entities in the Volkswagen Group	120	189
Total	**155**	**226**

The Bank has not entered into any agreement to convert these liabilities into equity or another form of debt, nor is it planning any such conversion.

48. Noncurrent Liabilities

€ million	Dec. 31, 2016	of which noncurrent	Dec. 31, 2015	of which noncurrent
Liabilities to banks	4,930	4,662	4,020	3,636
Liabilities to customers	37,938	3,014	30,478	2,096
Notes, commercial paper issued	4,311	2,660	7,604	4,176
Derivative financial instruments	43	13	46	23
Current tax liabilities	89	–	39	–
Other liabilities	217	32	150	7
Subordinated capital	155	103	226	158
Total	**47,683**	**10,483**	**42,563**	**10,095**

49. Equity

Volkswagen Bank GmbH's subscribed capital amounted to €318 million. There are no preferential rights or restrictions in connection with the subscribed capital.

The capital contributions made by the sole shareholder, Volkswagen Financial Services AG, are reported under the capital reserves of Volkswagen Bank GmbH. As of December 31, 2016, capital reserves amounted to €6,026 million (previous year: €3,946 million)

Retained earnings comprise undistributed profits from prior years and primarily contain other revenue reserves.

The HGB profit of €414 million (previous year: €268 million) will be transferred in accordance with the existing profit-and-loss transfer agreement with the sole shareholder, Volkswagen Financial Services AG.

The accumulated deferred taxes in equity amounted to €4 million (previous year: €6 million).

50. Capital Management

In this context, “capital” means equity as defined by IFRS. The aim of capital management in the Volkswagen Bank GmbH Group is to support the Company’s credit rating by ensuring that the Group has adequate capital backing, to obtain capital for the planned growth over the next few years and to satisfy regulatory capital requirements.

Regulatory capital is different from equity as defined by IFRS (for the components, see the statement of changes in equity). Regulatory capital consists of capital components referred to as Common Equity Tier (CET) 1 capital, Additional Tier 1 capital and Tier 2 capital net of certain deductions and adjustments and must meet specific requirements defined by law.

Corporate actions implemented by the parent company of Volkswagen Bank GmbH have an impact on both IFRS equity and regulatory capital.

Under the regulatory provisions – Capital Requirements Regulation (CRR), Kreditwesengesetz (KWG – German Banking Act), Solvabilitätsverordnung (SolvV – German Solvency Regulation) – the banking supervisor generally assumes that capital adequacy requirements are satisfied if the entity subject to supervision has a CET1 capital ratio of at least 4.5%, a Tier 1 capital ratio of at least 6.0% and a total capital ratio of at least 8.0%. In calculating these ratios, capital is measured against the own funds requirements determined in accordance with statutory provisions for counterparty risk, operational risk, market risk and credit value adjustments (CVAs). To ensure compliance with these requirements at all times, the Group has established a planning procedure that is integrated into the internal reporting system. In this procedure, the capital requirement is continuously determined based on actual and forecast business trends. This ensured that the minimum regulatory capital requirements continued to be satisfied at all times in the reporting period.

The following HGB-based amounts and ratios were determined for Volkswagen Bank GmbH under the regulatory requirements:

	Dec. 31, 2016	Dec. 31, 2015
Total risk exposure amount (€ million)[1]	44,552	38,288
of which risk-weighted exposure amounts for credit risk	41,716	35,700
of which own funds requirements for market risk *12,5	384	244
of which own funds requirements for operational risk *12,5	2,400	2,297
of which own funds requirements for credit valuation adjustments *12,5	52	47
Eligible own funds (€ million)	6,401	4,292
Own funds (€ million)	6,401	4,292
of which Common Equity Tier 1 capital	6,372	4,262
of which Additional Tier 1 capital	0	0
of which Tier 2 capital	29	30
Common Equity Tier 1 capital ratio (percent)[2]	14.3	11.1
Tier 1 capital ratio (percent)[2]	14.3	11.1
Total capital ratio (percent)[2]	14.4	11.2

1 According to Article 92(3) of the CRR
2 According to Article 92(1) of the CRR

Financial Instrument Disclosures

51. Carrying Amounts of Financial Instruments by IAS 39 Measurement Category

The measurement categories defined in IAS 39 are as follows for the Volkswagen Bank GmbH Group:

Loans and receivables are non-derivative financial instruments that are not traded in an active market and that are subject to fixed-payment agreements. The cash reserve also forms part of this category.

Financial assets and financial liabilities measured at fair value through profit or loss include derivative financial instruments. The Volkswagen Bank GmbH Group has no plans to specially allocate other financial instruments to this category.

Available-for-sale financial assets are either assets specifically allocated to this category as such or financial assets that cannot be allocated to any other category. In the Volkswagen Bank GmbH Group, marketable securities and miscellaneous financial assets are allocated to this category.

All non-derivative financial instruments are accounted for on the basis of the settlement date. Derivative financial instruments are accounted for on the basis of the trade date.

The carrying amounts of financial instruments (excluding hedge derivatives) by measurement category are as follows:

	LOANS AND RECEIVABLES		AVAILABLE-FOR-SALE FINANCIAL ASSETS		FINANCIAL LIABILITIES MEASURED AT AMORTIZED COST		FINANCIAL ASSETS AND FINANCIAL LIABILITIES MEASURED AT FAIR VALUE THROUGH PROFIT OR LOSS	
€ million	**Dec. 31, 2016**	Dec. 31, 2015	**Dec. 31, 2016**	Dec. 31, 2015	**Dec. 31, 2016**	Dec. 31, 2015	**Dec. 31, 2016**	Dec. 31, 2015
Assets								
Cash reserve	1,457	1,352	–	–	–	–	–	–
Loans to and receivables from banks	1,944	1,501	–	–	–	–	–	–
Loans to and receivables from customers	42,653	38,304	–	–	–	–	–	–
Derivative financial instruments	–	–	–	–	–	–	8	16
Marketable securities	–	–	4,455	2,557	–	–	–	–
Miscellaneous financial assets	–	–	0	0	–	–	–	–
Other assets	258	452	–	–	–	–	–	–
Total	**46,311**	**41,610**	**4,455**	**2,557**	**–**	**–**	**8**	**16**
Liabilities								
Liabilities to banks	–	–	–	–	4,930	4,020	–	–
Liabilities to customers	–	–	–	–	37,938	30,478	–	–
Notes, commercial paper issued	–	–	–	–	4,311	7,604	–	–
Derivative financial instruments	–	–	–	–	–	–	15	13
Other liabilities	–	–	–	–	60	20	–	–
Subordinated capital	–	–	–	–	155	226	–	–
Total	**–**	**–**	**–**	**–**	**47,396**	**42,348**	**15**	**13**

Receivables from leasing transactions are not allocated to any of these categories.

The net income/expense for each of the categories is as follows:

€ million	2016	2015
Loans and receivables[1]	1,358	1,281
Available-for-sale financial assets[1]	35	17
Financial liabilities measured at amortized cost[1]	–220	–173
Financial assets and financial liabilities measured at fair value through profit or loss	–11	11

1 The prior-year figures have been restated in line with the classification used in the reporting period. The previous prior-year figures were as follows: loans and receivables, €1,294 million; available-for-sale financial assets, €26 million; and financial liabilities measured at amortized cost, net expense of €175 million.

The net income/expense is determined as follows:

Measurement category	Measurement method
Loans and receivables	Interest income using the effective interest method in accordance with IAS 39 and expenses/income from the recognition of valuation allowances in accordance with IAS 39, including effects from currency translation
Available-for-sale financial assets	Changes in fair value in accordance with IAS 39 in conjunction with IFRS 13, including interest and effects from currency translation and impairment
Financial liabilities measured at amortized cost	Interest expense using the effective interest method in accordance with IAS 39, including effects from currency translation
Financial assets and financial liabilities measured at fair value through profit or loss	Changes in fair value in accordance with IAS 39 in conjunction with IFRS 13, including interest and effects from currency translation and impairment

52. Classes of Financial Instruments

Financial instruments are divided into the following classes in the Volkswagen Bank GmbH Group:

- Measured at fair value
- Assets and liabilities measured at amortized cost
- Derivative financial instruments designated as hedges
- Credit commitments and financial guarantees
- Not within scope of IFRS 7.

Loans/receivables and liabilities designated as hedges with derivative financial instruments are included in the "Assets and liabilities measured at amortized cost" class. Subsidiaries that are not consolidated for reasons of materiality are not deemed financial instruments in accordance with IAS 39 and therefore do not fall within the scope of IFRS 7. Equity investments as financial instruments in accordance with IAS 39 are reported in the class "Measured at fair value".

The following table shows a reconciliation of the relevant balance sheet items to the classes of financial instruments:

€ million	BALANCE SHEET ITEM		MEASURED AT FAIR VALUE		MEASURED AT AMORTIZED COST		DERIVATIVE FINANCIAL INSTRUMENTS DESIGNATED AS HEDGES		NOT WITHIN THE SCOPE OF IFRS 7	
	Dec. 31, 2016	Dec. 31, 2015	Dec. 31, 2016	Dec. 31, 2015	Dec. 31, 2016	Dec. 31, 2015	Dec. 31, 2016	Dec. 31, 2015	Dec. 31, 2016	Dec. 31, 2015
Assets										
Cash reserve	1,457	1,352	–	–	1,457	1,352	–	–	–	–
Loans to and receivables from banks	1,944	1,501	–	–	1,944	1,501	–	–	–	–
Loans to and receivables from customers	45,667	40,806	–	–	45,667	40,806	–	–	0	0
Derivative financial instruments	221	153	8	16	–	–	213	137	–	–
Marketable securities	4,455	2,557	4,455	2,557	–	–	–	–	–	–
Equity-accounted joint ventures	–	–	–	–	–	–	–	–	–	–
Miscellaneous financial assets	3	3	0	0	–	–	–	–	3	3
Other assets	396	589	–	–	258	452	–	–	139	137
Total	**54,143**	**46,961**	**4,463**	**2,573**	**49,326**	**44,112**	**213**	**137**	**141**	**140**
Liabilities										
Liabilities to banks	4,930	4,020	–	–	4,930	4,020	–	–	–	–
Liabilities to customers	37,938	30,478	–	–	37,938	30,478	–	–	–	–
Notes, commercial paper issued	4,311	7,604	–	–	4,311	7,604	–	–	–	–
Derivative financial instruments	43	46	15	13	–	–	28	34	–	–
Other liabilities	217	150	–	–	60	20	–	–	156	130
Subordinated capital	155	226	–	–	155	226	–	–	–	–
Total	**47,595**	**42,524**	**15**	**13**	**47,396**	**42,348**	**28**	**34**	**156**	**130**

The “Credit commitments and financial guarantees” class contains obligations under irrevocable credit commitments and financial guarantees amounting to €1,544 million (previous year: €1,386 million).

53. Measurement Hierarchy for Financial Instruments

For the purposes of fair value measurement and the associated disclosures, fair values are classified using a three-level measurement hierarchy. Classification to the individual levels is dictated by the extent to which the main inputs used in determining the fair value are observable in the market or not.

Level 1 is used to report the fair value of financial instruments such as marketable securities, for which a quoted price is directly observable in an active market.

Level 2 fair values are measured on the basis of inputs observable in the markets, such as exchange rates or yield curves, using market-based valuation techniques. Fair values measured in this way include those for derivatives and liabilities to customers. Level 3 fair values are measured using valuation techniques incorporating at least one input that is not observable in an active market. Most of the loans to and receivables from cus-

tomers are allocated to Level 3 because their fair value is measured using inputs that are not observable in active markets (see note 54). There was no need for reclassifications during the reporting period.

The following table shows the allocation of financial instruments to this three-level fair value hierarchy by class:

€ million	LEVEL 1		LEVEL 2		LEVEL 3	
	Dec. 31, 2016	Dec. 31, 2015	Dec. 31, 2016	Dec. 31, 2015	Dec. 31, 2016	Dec. 31, 2015
Assets						
Measured at fair value						
Derivative financial instruments	–	–	8	16	–	–
Marketable securities	2,191	2,222	2,264	323	–	12
Miscellaneous financial assets	–	–	–	–	0	0
Measured at amortized cost						
Cash reserve	1,457	1,352	–	–	–	–
Loans to and receivables from banks	1,128	1,041	815	460	–	–
Loans to and receivables from customers[1]	–	–	213	350	46,161	41,031
Other assets	–	–	258	452	–	–
Derivative financial instruments designated as hedges	–	–	213	137	–	–
Total[1]	**4,776**	**4,627**	**3,771**	**1,738**	**46,161**	**41,031**
Liabilities						
Measured at fair value						
Derivative financial instruments	–	–	15	13	–	–
Measured at amortized cost						
Liabilities to banks	–	–	4,835	3,869	–	–
Liabilities to customers	–	–	37,966	30,519	–	–
Notes, commercial paper issued	–	–	4,317	7,618	–	–
Other liabilities	–	–	60	20	–	–
Subordinated capital	–	–	168	238	–	–
Derivative financial instruments designated as hedges	–	–	28	34	–	–
Total	**–**	**–**	**47,390**	**42,311**	**–**	**–**

1 The prior-year figures have been restated in line with the classification used in the reporting period. The previous prior-year figure for the loans to and receivables from customers under Level 3 was €41,029 million. The overall total has been restated accordingly.

54. Fair Value of Financial Instruments in the Classes "Assets and Liabilities Measured at Amortized Cost", "Measured at Fair Value", "Derivative Financial Instruments Designated As Hedges"

The table below shows the fair values of the 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. Where market prices were available, we used these prices without modification for measuring fair value. If no market prices were available, the fair values for loans/receivables and liabilities were calculated by discounting using a maturity-matched discount rate appropriate to the risk. The discount rate was determined by adjusting risk-free yield curves, where appropriate, by relevant risk factors and to take into account capital and administrative costs. For reasons of materiality, the fair values of loans/receivables and liabilities due within one year were deemed to be the same as the carrying amount.

The fair value of irrevocable credit commitments equates to the nominal value of the obligations because of the short maturity and the variable interest rate linked to the market interest rate. There are also no differences between the fair value and the nominal value of the obligation in the case of financial guarantees.

	FAIR VALUE		CARRYING AMOUNT		DIFFERENCE	
€ million	Dec. 31, 2016	Dec. 31, 2015	Dec. 31, 2016	Dec. 31, 2015	Dec. 31, 2016	Dec. 31, 2015
Assets						
Measured at fair value						
Derivative financial instruments	8	16	8	16	–	–
Marketable securities	4,455	2,557	4,455	2,557	–	–
Miscellaneous financial assets	0	0	0	0	–	–
Measured at amortized cost						
Cash reserve	1,457	1,352	1,457	1,352	–	–
Loans to and receivables from banks[1]	1,944	1,501	1,944	1,501	0	–
Loans to and receivables from customers[1]	46,373	41,381	45,667	40,806	706	574
Other assets	258	452	258	452	–	–
Derivative financial instruments designated as hedges	213	137	213	137	–	–
Liabilities						
Measured at fair value						
Derivative financial instruments	15	13	15	13	–	–
Measured at amortized cost						
Liabilities to banks	4,835	3,869	4,930	4,020	–95	–152
Liabilities to customers	37,966	30,519	37,938	30,478	28	41
Notes, commercial paper issued	4,317	7,618	4,311	7,604	5	14
Other liabilities	60	20	60	20	–	–
Subordinated capital	168	238	155	226	13	12
Derivative financial instruments designated as hedges	28	34	28	34	–	–

1 The prior-year figures have been restated in line with the classification used in the reporting period. The previous prior-year figures for the differences were as follows: loans to and receivables from banks, €54 million; loans to and receivables from customers, €520 million.

The fair values of financial instruments were determined on the basis of the following risk-free yield curves:

Percent	EUR	GBP	PLN
Interest rate for six months	–0,251	0,375	1,739
Interest rate for one year	–0,214	0,401	1,762
Interest rate for five years	0,074	0,866	2,340
Interest rate for ten years	0,652	1,233	2,865

55. Offsetting of Financial Assets and Liabilities

The table below contains information about the effects of offsetting in the consolidated balance sheet and the financial effects of offsetting in the case of instruments that are subject to a legally enforceable master netting agreement or a similar arrangement.

Financial assets and financial liabilities are generally reported with their gross values. Offsetting is only then applied if, at the present time, the offsetting of the amounts is legally enforceable by the Volkswagen Bank GmbH Group and there is an intention to settle on a net basis in practice.

The “Financial instruments” column shows the amounts that are subject to a master netting agreement but have not been netted because the relevant criteria have not been satisfied. Most of the amounts involved are positive and negative fair values of derivative financial instruments entered into with the same counterparty.

The “Collateral received/pledged” column shows the amounts of cash and other collateral in the form of financial instruments received in connection with the total sum of assets and liabilities. It includes such collateral relating to assets and liabilities that have not been offset against each other. The collateral amounts primarily consist of pledged cash collateral in connection with ABS transactions and marketable securities pledged as collateral.

€ million	Gross amount of recognized financial assets/liabilities		Gross amount of recognized financial assets/liabilities offset in the balance sheet		Net amount of financial assets/ liabilities reported in the balance sheet		AMOUNTS NOT OFFSET IN THE BALANCE SHEET: Financial instruments		AMOUNTS NOT OFFSET IN THE BALANCE SHEET: Collateral received/pledged		Net amount	
	Dec. 31, 2016	Dec. 31, 2015	Dec. 31, 2016	Dec. 31, 2015	Dec. 31, 2016	Dec. 31, 2015	Dec. 31, 2016	Dec. 31, 2015	Dec. 31, 2016	Dec. 31, 2015	Dec. 31, 2016	Dec. 31, 2015
Assets												
Cash reserve	1,457	1,352	–	–	1,457	1,352	–	–	–	–	1,457	1,352
Loans to and receivables from banks	1,944	1,501	–	–	1,944	1,501	–	–	–	–	1,944	1,501
Loans to and receivables from customers	45,748	40,926	–81	–120	45,667	40,806	–	–	–	–	45,667	40,806
Derivative financial instruments	221	153	–	–	221	153	–19	–30	–175	–123	27	1
Marketable securities	4,455	2,557	–	–	4,455	2,557	–	–	–	–	4,455	2,557
Miscellaneous financial assets	0	0	–	–	0	0	–	–	–	–	0	0
Other assets	272	464	–14	–11	258	452	–	–	–	–	258	452
Total	**54,097**	**46,953**	**–95**	**–132**	**54,002**	**46,822**	**–19**	**–30**	**–175**	**–123**	**53,808**	**46,670**
Liabilities												
Liabilities to banks[1]	4,930	4,020	–	–	4,930	4,020	–	–	–2,657	–1,836	2,273	2,184
Liabilities to customers	38,019	30,598	–81	–120	37,938	30,478	–	–	–	–	37,938	30,478
Notes, commercial paper issued[1]	4,311	7,604	–	–	4,311	7,604	–	–	–188	–319	4,123	7,285
Derivative financial instruments	43	46	–	–	43	46	–19	–30	–24	–12	0	5
Other liabilities	74	32	–14	–11	60	20	–	–	–	–	60	20
Subordinated capital	155	226	–	–	155	226	–	–	–	–	155	226
Total	**47,533**	**42,526**	**–95**	**–132**	**47,438**	**42,394**	**–19**	**–30**	**–2,869**	**–2,167**	**44,551**	**40,198**

1 Modified presentation in the reporting period; prior-year figures have been restated accordingly.

56. Counterparty Default Risk

For qualitative information, please refer to the risk report (Credit Risk section, pages 25 to 27), which forms part of the management report.

The credit and default risk arising from financial assets is essentially the risk that a counterparty will default. The maximum amount of the risk is therefore the amount of the claims against the counterparty concerned arising from recognized carrying amounts and irrevocable credit commitments. The maximum credit and default risk is reduced by collateral and other credit enhancements amounting to €24,489 million (previous year: €22,922 million). The collateral held is in respect of loans to and receivables from customers in the class “Assets measured at amortized cost”. The types of collateral held include vehicles, other assets pledged as collateral, guarantees and charges on real estate. Cash deposits are also used as collateral in connection with derivatives.

The following table shows the credit quality of financial assets:

€ million	GROSS CARRYING AMOUNT		NEITHER PAST DUE NOR IMPAIRED		PAST DUE BUT NOT IMPAIRED		IMPAIRED	
	Dec. 31, 2016	Dec. 31, 2015	Dec. 31, 2016	Dec. 31, 2015	Dec. 31, 2016	Dec. 31, 2015	Dec. 31, 2016	Dec. 31, 2015
Measured at fair value	4,463	2,573	4,463	2,573	–	–	–	–
Measured at amortized cost								
Cash reserve	1,457	1,352	1,457	1,352	–	–	–	–
Loans to and receivables from banks	1,944	1,501	1,944	1,501	–	–	–	–
Loans to and receivables from customers	46,807	41,999	45,236	40,540	330	280	1,241	1,180
Other assets	258	452	258	452	–	0	–	–
Derivative financial instruments designated as hedges	213	137	213	137	–	–	–	–
Total	**55,142**	**48,015**	**53,571**	**46,556**	**330**	**280**	**1,241**	**1,180**

The maximum default risk from irrevocable credit commitments and financial guarantees is €1,544 million (previous year: €1,386 million).

The breakdown of neither past due nor impaired financial assets by risk class is as follows:

€ million	NEITHER PAST DUE NOR IMPAIRED		RISK CLASS 1		RISK CLASS 2	
	Dec. 31, 2016	Dec. 31, 2015	Dec. 31, 2016	Dec. 31, 2015	Dec. 31, 2016	Dec. 31, 2015
Measured at fair value	4,463	2,573	4,463	2,573	–	–
Measured at amortized cost						
Cash reserve	1,457	1,352	1,457	1,352	–	–
Loans to and receivables from banks	1,944	1,501	1,944	1,501	–	–
Loans to and receivables from customers	45,236	40,540	43,283	37,611	1,953	2,929
Other assets[1]	258	452	256	450	1	2
Derivative financial instruments designated as hedges	213	137	213	137	–	–
Total[1]	**53,571**	**46,556**	**51,617**	**43,624**	**1,954**	**2,931**

1 The prior-year figures have been restated in line with the classification used in the reporting period. The previous prior-year figure for the other assets assigned to risk class 1 was €452 million. There was no previous figure for the other assets under risk class 2. The overall total has been restated accordingly.

In the financial services business, the group evaluates the credit quality of the borrower before entering into any lending contract or lease. In the retail business, this evaluation is carried out by using scoring systems, whereas rating systems are used for fleet customers and dealer financing transactions. Lending evaluated as “good” is included in risk class 1. Loans to and receivables from customers whose credit quality has not been classified as “good” but who have not yet defaulted are included under risk class 2.

Age analysis of financial assets past due but not impaired, by class:

€ million	Past due but not impaired		IN THE FOLLOWING AGED PAST DUE CATEGORIES: Up to 1 month		1 to 3 months		More than 3 months	
	Dec. 31, 2016	Dec. 31, 2015	Dec. 31, 2016	Dec. 31, 2015	Dec. 31, 2016	Dec. 31, 2015	Dec. 31, 2016	Dec. 31, 2015
Measured at fair value	–	–	–	–	–	–	–	–
Measured at amortized cost								
Cash reserve	–	–	–	–	–	–	–	–
Loans to and receivables from banks	–	–	–	–	–	–	–	–
Loans to and receivables from customers	330	280	201	172	129	106	–	1
Other assets	–	0	–	–	–	–	–	0
Derivative financial instruments designated as hedges	–	–	–	–	–	–	–	–
Total	**330**	**280**	**201**	**172**	**129**	**106**	**–**	**1**

Volkswagen Bank GmbH intends to recover the following collateral accepted in the reporting period for financial assets:

€ million	Dec. 31, 2016	Dec. 31, 2015
Vehicles	32	29
Real estate	–	–
Other movable assets	–	–
Total	**32**	**29**

The vehicles are remarketed to Volkswagen Group dealers through direct sales and auctions.

57. Liquidity Risk

Please refer to the management report for information on the funding and hedging strategy.

The maturity profile of assets held to manage liquidity risk is as follows:

	ASSETS		REPAYABLE ON DEMAND		UP TO 3 MONTHS		3 MONTHS TO 1 YEAR		1 TO 5 YEARS	
€ million	Dec. 31, 2016	Dec. 31, 2015	Dec. 31, 2016	Dec. 31, 2015	Dec. 31, 2016	Dec. 31, 2015	Dec. 31, 2016	Dec. 31, 2015	Dec. 31, 2016	Dec. 31, 2015
Cash reserve	1,457	1,352	1,457	1,352	–	–	–	–	–	–
Loans to and receivables from banks	1,944	1,501	1,031	926	470	450	121	125	322	–
Marketable securities[1]	2,186	2,222	–	–	2,186	2,222	–	–	–	–
Total[1]	**5,587**	**5,075**	**2,487**	**2,278**	**2,656**	**2,672**	**121**	**125**	**322**	**–**

1 The prior–year figures have been restated in line with the classification used in the reporting period. The previous prior–year figure for marketable securities was €2,557 million. The overall total has been restated accordingly.

The following table shows the maturity profile of undiscounted cash outflows from financial liabilities:

			REMAINING CONTRACTUAL MATURITIES							
	Cash outflows		Up to 3 months		3 months to 1 year		1 to 5 years		More than 5 years	
€ million	Dec. 31, 2016	Dec. 31, 2015	Dec. 31, 2016	Dec. 31, 2015	Dec. 31, 2016	Dec. 31, 2015	Dec. 31, 2016	Dec. 31, 2015	Dec. 31, 2016	Dec. 31, 2015
Liabilities to banks	4,940	4,038	224	323	47	64	4,571	3,589	98	62
Liabilities to customers	38,258	30,741	31,159	26,270	3,831	2,166	2,609	1,800	658	506
Notes, commercial paper issued	4,332	7,665	219	363	1,440	3,077	2,673	4,225	–	–
Derivative financial Instruments[1]	5,465	3,247	2,065	1,920	1,874	1,247	1,527	79	–	–
Other liabilities	60	20	34	18	0	0	26	1	1	1
Subordinated capital	172	244	16	14	39	58	76	128	41	44
Irrevocable credit commitments	1,408	1,290	253	146	1,154	1,144	0	0	–	0
Total[1]	**54,635**	**47,246**	**33,969**	**29,055**	**8,386**	**7,756**	**11,482**	**9,822**	**798**	**614**

1 The prior–year figures have been restated in line with the classification used in the reporting period. The previous prior–year figure for derivative financial instruments was €3,256 million. The residual contractual maturities and the overall total have been restated accordingly.

The maximum possible calls under financial guarantees at any time can be assumed to be €136 million (previous year: €96 million).

58. Market Risk

For qualitative information, please refer to the risk report within the management report.

For quantitative risk measurement, interest rate and currency translation risk are measured using a value-at-risk (VaR) model on the basis of a historical simulation. The value-at-risk calculation indicates the size of the maximum potential loss on the portfolio as a whole within a time horizon of 40 days, measured at a confidence level of 99%. To provide the basis for this calculation, all cash flows from non-derivative and derivative financial instruments are aggregated into an interest rate gap analysis. The historical market data used in determining the value-at-risk covers a period of 1,000 trading days.

This approach has produced the following values:

€ million	2016	2015
Interest-rate risk	21	24
Currency translation risk	1	1
Total market risk[1]	**21**	**23**

1 Due to correlation effects, the total market risk is not equivalent to the sum of individual risks.

59. Foreign Currency Exposures

The following table shows a breakdown of the foreign currency amounts included in the assets and liabilities of the Volkswagen Bank GmbH Group as of December 31, 2016:

€ million	CZK	GBP	NOK	PLN	RUB	TRY	USD	Other
Cash reserve	–	–	–	90	–	–	–	–
Loans to and receivables from banks	0	0	0	0	0	0	0	0
Loans to and receivables from customers	303	3,305	1,366	553	–	689	43	–
Marketable securities	–	1,601	–	102	–	–	–	–
Miscellaneous financial assets	–	–	–	0	–	–	–	–
Intangible Assets	–	–	–	33	–	–	–	–
Property and equipment	–	–	–	2	–	–	–	–
Current tax assets	–	1	–	9	–	–	–	–
Other assets	–	5,862	–	1	–	–	–	–
Assets	**303**	**10,770**	**1,366**	**789**	**0**	**689**	**43**	**0**
Liabilities to banks	–	1	–	60	–	–	–	–
Liabilities to customers	–	108	–	457	–	–	–	–
Notes, commercial paper issued	–	–	–	105	–	–	–	–
Provisions	–	2	–	4	–	–	–	–
Current tax liabilities	–	6	–	5	–	–	–	–
Other liabilities	–	2	–	5	–	–	–	–
Liabilities	**–**	**119**	**–**	**637**	**–**	**–**	**–**	**–**

60. Hedging Policy Disclosures

HEDGING POLICY AND FINANCIAL DERIVATIVES

Given its international financial activities, the Volkswagen Bank GmbH Group is exposed to fluctuations in interest rates on international money and capital markets. The general rules governing the Group-wide currency and interest rate hedging policy are specified in internal Group guidelines and satisfy the Minimum Requirements for Risk Management (MaRisk – Mindestanforderungen an das Risikomanagement) issued by the German Federal Financial Supervisory Authority (BaFin). The partners used by the Group when entering into appropriate financial transactions are national and international banks with strong credit ratings whose credit quality is continuously monitored by leading rating agencies. The Group enters into suitable hedging transactions to limit currency and interest rate risks. Regular derivative financial instruments are used for this purpose.

MARKET RISK

Market risk arises when changes in prices on financial markets (interest rates and exchange rates) have a positive or negative effect on the value of traded products. The fair values listed in the tables were determined using the market information available on the reporting date and represent the present values of the financial derivatives. They were determined on the basis of standardized techniques or quoted prices.

INTEREST RATE RISK

Changes in the level of interest rates in the money and capital markets represent an interest rate risk in the case of any funding that is not maturity-matched. Interest rate risk is managed on the basis of recommendations made by the Asset-Liability Management Committee (ALM Committee). Interest rate risk is quantified using interest rate gap analyses to which various scenarios involving changes in interest rates are applied. The interest rate hedges entered into comprise interest rate swaps and cross-currency swaps.

CURRENCY RISK

Currency risk is avoided by entering into currency hedging contracts, which may be currency forwards, interest rate swaps, or cross-currency swaps. The Group generally hedges all cash flows denominated in foreign currency.

LIQUIDITY RISK, FUNDING RISK

The Volkswagen Bank GmbH Group takes precautions to minimize the risk from any potential liquidity squeeze by holding a confirmed credit line at Volkswagen AG and by using debt issuance programs with multicurrency capability. It also holds marketable securities from public-sector issuers that are readily marketable and are eligible for use as collateral at central banks, and can thus be used to help safeguard liquidity.

DEFAULT RISK

The default risk arising from financial assets is essentially the risk that a counterparty will default. The maximum amount of the risk is therefore the balance due from the counterparty concerned.

Given that only counterparties with strong credit ratings are used for transactions and limits are set for each counterparty as part of the risk management system, the actual default risk is deemed to be low. Furthermore, the default risk in the Group's transactions is also minimized in accordance with regulatory requirements by the use of collateral to be furnished by the counterparty.

Risk concentrations arise in the Volkswagen Bank GmbH Group in a variety of forms. A detailed description can be found in the report on opportunities and risks within the combined management report.

The breakdown of the notional volume of the derivative financial instruments is as follows:

	REMAINING CONTRACTUAL MATURITIES					
	Up to 1 year		1 to 5 years		More than 5 years	
€ million	Dec. 31, 2016	Dec. 31, 2015	Dec. 31, 2016	Dec. 31, 2015	Dec. 31, 2016	Dec. 31, 2015
Cash flow hedges						
Interest rate swaps	–	–	–	–	–	–
Cross-currency interest rate swaps	–	–	–	–	–	–
Currency forward contracts	7	3	–	–	–	–
Currency swaps	–	–	–	–	–	–
Other						
Interest rate swaps	3,374	3,293	3,623	7,027	0	0
Cross-currency interest rate swaps	261	9	585	–	–	–
Currency forward contracts	1,337	266	–	–	–	–
Currency swaps	2,233	2,875	921	62	–	–
Total	**7,213**	**6,446**	**5,128**	**7,089**	**0**	**0**

The timings of the future payments for the hedged items in the cash flow hedges match the maturities of the hedging instruments.

As of the reporting date, none of the recognized cash flow hedges involved a hedged item in which the transaction was no longer expected to occur in the future.

Segment Reporting

61. Breakdown by Geographical Market

The reportable segments in accordance with IFRS 8 and on the basis of the internal reporting structure of the Volkswagen Bank GmbH Group are the reporting segments Germany, Italy, France and Other. The branches in the UK, the Netherlands, Spain, Ireland, Greece, Portugal and Volkswagen Bank Polska S.A. have been allocated to the "Other" segment.

The information made available to management for management purposes is based on the same accounting policies as those used for external financial reporting.

The profit or loss for each individual segment is measured on the basis of the operating profit or loss and profit or loss before tax.

Operating profit or loss includes net income from lending and leasing transactions after provision for credit risks, net fee and commission income, net gain/loss on the measurement of derivative financial instruments and hedged items, general administrative expenses and other operating income and expenses. The interest expenses, net gain/loss on the measurement of derivative financial instruments and hedged items, net gain/loss on marketable securities and miscellaneous financial assets, general administrative expenses and net other operating income/expenses that are not components of operating profit or loss largely comprise net hedge accounting gains or losses, income from investments in affiliated companies, interest expenses from tax audits, interest costs from unwinding the discount on other provisions, interest expenses for pension provisions and the expected return on plan assets for externally funded pension obligations.

Interest income not classified as revenue is interest income that is not attributable to the financial services business. This interest income is not a component of operating profit or loss.

The additional provision for credit risks in relation to loans and receivables of the branches in the countries at the center of the euro crisis is allocated to the Germany segment in accordance with the internal reporting structure.

	FISCAL YEAR 2016					
€ million	Germany	Italy	France	Other	Consolidation	Total
Revenue from lending transactions with third parties	929	107	54	239	–	1,330
Intersegment revenue from lending transactions	88	0	0	0	–88	–
Total segment revenue from lending transactions	1,018	107	54	239	–88	1,330
Revenue from leasing transactions	–	84	529	6	–	618
Fee and commission income	170	72	53	21	–	315
Revenue	**1,187**	**263**	**635**	**266**	**–88**	**2,361**
Cost of sales attributable to lending and leasing transactions	–	–60	–200	–2	–	–262
Reversals of impairment losses on lease assets and investment property	–	–	6	–	–	6
Depreciation of and impairment losses on lease assets and investment property	–	–	–186	–	–	–186
of which impairment losses in accordance with IAS 36	–	–	–15	–	–	–15
Interest expense (component of operating profit or loss)	–192	–19	–27	–58	88	–207
Provision for credit risks from lending and leasing business	29	–23	–51	7	–	–38
Fee and commission expenses	–214	–46	–66	–20	–	–345
Net gain/loss on the measurement of derivative financial instruments and hedged items (component of operating profit or loss)	–11	–	–	–	–	–11
General and administrative expenses (component of operating profit or loss)	–595	–54	–90	–90	1	–827
Net other operating income/expenses (component of operating profit or loss)	210	3	39	9	–1	259
Segment profit or loss (operating profit or loss)	**415**	**64**	**54**	**112**	**–**	**645**
Interest income not classified as revenue	6	–	–	–	–	6
Interest expense (not a component of operating profit or loss)	0	–	–	–	–	0
Net gain/loss on the measurement of derivative financial instruments and hedged items (not a component of operating profit or loss)	3	0	0	–	–	3
Net gain/loss on marketable securities and miscellaneous financial assets	11	–	0	8	–	20
General and administrative expenses (not a component of operating profit or loss)	–1	0	–	0	–	–1
Net other operating income/expenses (not a component of operating profit or loss)	–3	0	–	–	–	–3
Profit before tax	**431**	**64**	**53**	**121**	**–**	**669**
Income tax expense	–129	–18	–16	–23	–	–186
Profit after tax	**302**	**45**	**38**	**98**	**–**	**482**
Share of net income for the year attributable to Volkswagen Financial Services AG	302	45	38	98	–	482
Segment assets	**24,935**	**3,744**	**5,222**	**5,725**	**–**	**39,625**
of which: noncurrent assets	15,182	1,915	1,977	1,277	–	20,350
Segment liabilities	**45,275**	**3,619**	**4,405**	**7,011**	**–14,199**	**46,111**

The segment reporting for the previous year is shown in the following table:

€ million	FISCAL YEAR 2015					
	Germany	Italy	France	Other	Consolidation	Total
Revenue from lending transactions with third parties	918	107	54	217	–	1,296
Intersegment revenue from lending transactions	67	0	0	0	–67	–
Total segment revenue from lending transactions	985	107	54	217	–67	1,296
Revenue from leasing transactions	–	44	405	5	–	454
Fee and commission income	164	62	53	17	–	297
Revenue	**1,150**	**213**	**512**	**240**	**–67**	**2,047**
Cost of sales attributable to lending and leasing transactions	–	–31	–128	–2	–	–162
Reversals of impairment losses on lease assets and investment property	–	–	–	–	–	–
Depreciation of and impairment losses on lease assets and investment property	–	–	–164	–	–	–164
of which impairment losses in accordance with IAS 36	–	–	–26	–	–	–26
Interest expense (component of operating profit or loss)	–181	–16	–24	–40	67	–193
Provision for credit risks from lending and leasing business	0	–24	–46	–1	–	–71
Fee and commission expenses	–158	–31	–58	–12	–	–258
Net gain/loss on the measurement of derivative financial instruments and hedged items (component of operating profit or loss)	–4	–	–	–	–	–4
General and administrative expenses (component of operating profit or loss)	–574	–52	–78	–90	1	–793
Net other operating income/expenses (component of operating profit or loss)	105	0	24	10	–1	138
Segment profit or loss (operating profit or loss)	**337**	**59**	**38**	**105**	**–**	**539**
Interest income not classified as revenue	11	–	–	–	–	11
Interest expense (not a component of operating profit or loss)	–1	–	–	–	–	–1
Net gain/loss on the measurement of derivative financial instruments and hedged items (not a component of operating profit or loss)	13	0	1	–	–	14
Net gain/loss on marketable securities and miscellaneous financial assets	5	–	–	9	–	14
General and administrative expenses (not a component of operating profit or loss)	–1	0	–	0	–	–1
Net other operating income/expenses (not a component of operating profit or loss)	0	–	–	–	–	0
Profit before tax	**363**	**59**	**39**	**144**	**–**	**575**
Income tax expense	–106	–19	–9	–22	–	–157
Profit after tax	**257**	**40**	**29**	**92**	**–**	**418**
Share of net income for the year attributable to Volkswagen Financial Services AG	257	40	29	92	–	418
Segment assets	**23,430**	**3,341**	**4,568**	**5,701**	**–**	**37,040**
of which: noncurrent assets	14,272	1,678	2,465	1,109	–	19,523
Segment liabilities	**39,961**	**3,206**	**3,952**	**5,678**	**–11,591**	**41,205**

Individual line items in the financial statements are aggregated for the purposes of internal reporting. The following table shows the reconciliation of these line items in the financial statements to the segment reporting disclosures.

€ million	Dec. 31, 2016	Dec. 31, 2015
Interest income from lending transactions	1,336	1,307
minus interest income not classified as revenue	6	11
Net income from leasing transactions before provision for credit risks	170	128
minus expenses from insurance business	–262	–162
minus depreciation of and impairment losses on lease assets and investment property	–186	–164
minus reversals of impairment losses on lease assets and investment property	6	–
Fee and commission income	315	297
Consolidated revenue	**2,257**	**2,047**
Net income from leasing transactions before provision for credit risks	170	128
minus income from leasing transactions	618	454
minus depreciation of and impairment losses on lease assets and investment property	–186	–164
Consolidated cost of sales attributable to lending and leasing transactions	**–262**	**–162**
Loans to and receivables from customers attributable to		
Retail financing	24,940	23,312
Dealer financing	10,538	10,302
Leasing business	3,014	2,502
Other loans and receivables	7,175	4,690
of which not included in segment assets	–6,919	–4,476
Lease assets	877	710
Consolidated assets in accordance with segment reporting	**39,625**	**37,040**
Liabilities to banks	4,930	4,020
of which not included in segment liabilities	0	0
Liabilities to customers	37,938	30,478
of which not included in segment liabilities	–1,208	–1,105
Notes, commercial paper issued	4,311	7,604
of which not included in segment liabilities	–16	–17
Subordinated capital	155	226
Consolidated liabilities in accordance with segment reporting	**46,111**	**41,205**

All business transactions between the segments are conducted on an arm's-length basis.

The consolidation in revenue from lending transactions and interest expenses resulted from the provision of intragroup funding between the reporting segments of the Volkswagen Bank GmbH Group.

Information on the main products can be taken directly from the income statement.

The additions to property and equipment, intangible assets, lease assets and investment property were as follows: €3 million (previous year: €3 million) in the Italy segment, €459 million (previous year: €498 million) in the France segment and €2 million (previous year: €3 million) in the other reporting units. As in the previous year, no additions were made to these assets in the Germany segment. The related depreciation, amortization and impairment losses were as follows: €1 million (previous year: €1 million) in the Germany segment, €3 million (previous year: €3 million) in the Italy segment, €188 million (previous year: €166 million) in the France segment and €4 million (previous year: €4 million) in the other reporting units.

Other Disclosures

62. Cash Flow Statement

Volkswagen Bank GmbH's cash flow statement documents changes in cash and cash equivalents attributable to cash flows from operating, investing and financing activities. Cash flows from investing activities comprise purchase payments and disposal proceeds relating to investment property and other assets. Cash flows from financing activities reflect all cash flows arising from transactions involving equity, subordinated capital and other financing activities. All other cash flows are classified as cash flows from operating activities in accordance with standard international practice for financial services companies.

The narrow definition of cash and cash equivalents comprises the cash reserve, which consists of cash-in-hand and central bank balances.

63. Off-Balance-Sheet Liabilities

€ million	Dec. 31, 2016	Dec. 31, 2015
Contingent liabilities under bank and other financial guarantees	136	96
Other contingent liabilities	–	0
Total	**136**	**96**

€ million	DUE 2016	DUE 2017 – 2020	DUE From 2021	TOTAL Dec. 31, 2015
Purchase commitments in respect of				
property and equipment	–	–	–	–
intangible assets	–	–	–	–
investment property	–	–	–	–
Obligations from				
loan commitments to unconsolidated subsidiaries	78	–	–	78
irrevocable credit and leasing commitments to customers	1,290	0	0	1,290
long-term leasing and rental contracts	3	6	6	15
Miscellaneous financial obligations	14	–	–	14

€ million	DUE 2017	DUE 2018 – 2021	DUE From 2022	TOTAL Dec. 31, 2016
Purchase commitments in respect of				
property and equipment	–	–	–	–
intangible assets	–	–	–	–
investment property	–	–	–	–
Obligations from				
loan commitments to unconsolidated subsidiaries	–	–	–	–
irrevocable credit and leasing commitments to customers	1,465	0	–	1,465
long-term leasing and rental contracts	3	5	5	13
Miscellaneous financial obligations	19	2	–	21

Drawdowns on irrevocable credit commitments are possible at any time.

64. Trust Transactions

As in the previous year, there were no trust transactions to be reported as of the reporting date.

65. Average Number of Employees during the Reporting Period

	2016	2015
Salaried employees	1,230	1,167
of which senior managers	24	24
of which part time	69	63
Vocational trainees	15	14

66. Related Party Disclosures

Related parties within the meaning of IAS 24 are deemed to be individuals or entities who can be influenced by Volkswagen Bank GmbH, who can exercise an influence over Volkswagen Bank GmbH, or who are under the influence of another related party of Volkswagen Bank GmbH.

Volkswagen Financial Services AG, Braunschweig, is the sole shareholder of Volkswagen Bank GmbH.

The following disclosures pertain to the relationship with Porsche:

Porsche Automobil Holding SE, Stuttgart, controlled 52.2% of the voting rights in Volkswagen AG as of the reporting date and therefore held a majority. The Extraordinary General Meeting of Volkswagen AG held on December 3, 2009 approved the creation of rights of appointment for the State of Lower Saxony. As a result of these rights, Porsche SE can no longer appoint a majority of the members of Volkswagen AG's Supervisory Board for as long as the State of Lower Saxony holds at least 15% of Volkswagen AG's ordinary shares. However, Porsche SE has the power to participate in the operating policy decisions of the Volkswagen Group and is therefore deemed to be a related party within the meaning of IAS 24. According to a notification submitted on January 5, 2016, the State of Lower Saxony and Hannoversche Beteiligungsgesellschaft mbH, Hanover, held 20.00%

of the voting rights in Volkswagen AG as of December 31, 2016. In addition, as referred to above, the Extraordinary General Meeting of Volkswagen AG held on December 3, 2009 approved a resolution under which the State of Lower Saxony could appoint two members of the Supervisory Board (right of appointment).

The sole shareholder, Volkswagen Financial Services AG, and Volkswagen Bank GmbH have entered into a control and profit-and-loss transfer agreement. All business transactions between the two companies are conducted on an arm's-length basis.

Volkswagen AG and its subsidiaries provide the entities in the Volkswagen Bank GmbH Group with funding on an arm's-length basis. Volkswagen AG and its subsidiaries have also furnished collateral in our favor as part of the operating business.

The production and importer companies in the Volkswagen Group provide the entities in the Volkswagen Bank GmbH Group with financial subsidies to support sales promotion campaigns.

All business transactions with unconsolidated subsidiaries and other related parties in Volkswagen AG's group of consolidated entities are processed at arm's length.

The two tables below show the transactions with related parties. In these tables, the exchange rates used in connection with the figures are the closing rate for asset and liability items, and the average rates for the year for income statement items.

	FISCAL YEAR 2016								
€ million	Supervisory Board/ Audit Committee	Management/ Board of Management	Volkswagen AG	Porsche SE	Volkswagen Financial Services AG	Other related parties in the consolidated entities	Non-consolidated subsidiaries	Joint ventures	Associates
Loans and receivables	0	0	1	–	615	9,020	1	–	–
Valuation allowances on loans and receivables	–	–	–	–	–	–	–	–	–
of which additions in current year	–	–	–	–	–	–	–	–	–
Obligations	3	12	2,627	–	647	1,218	3	–	–
Interest income	0	0	0	–	0	140	1	–	–
Interest expense	0	0	–2	0	–1	–6	0	–	–
Goods and services provided	–	–	0	–	44	293	10	–	–
Goods and services received	–	–	–75	–	–697	–229	0	–	–

€ million	Supervisory Board/ Audit Committee	Manage-ment/ Board of Manage-ment	Volks-wagen AG	Porsche SE	Volks-wagen Financial Services AG	Other related parties in the consoli-dated entities	Non-consoli-dated subsidiaries	Joint ventures	Associates
	FISCAL YEAR 2015								
Loans and receivables	0	0	2	–	110	5,101	30	–	–
Valuation allowances on loans and receivables	–	–	–	–	–	–	–	–	–
of which additions in current year	–	–	–	–	–	–	–	–	–
Obligations	3	7	1,750	100	412	1,715	8	–	–
Interest income	0	0	0	–	0	94	3	–	–
Interest expense	0	0	–1	0	–1	–9	0	–	–
Goods and services provided	–	–	0	–	11	284	3	–	–
Goods and services received	–	–	–66	–	–766	–184	–1	–	–

The goods and services shown in the "Volkswagen Financial Services AG" column include support payments from Volkswagen Financial Services AG.

The "Other related parties in the group of consolidated entities" column includes, in addition to sister entities, joint ventures and associates that are related parties in Volkswagen AG's group of consolidated entities. The relationships with Management, the Board of Management and the Supervisory Board/Audit Committee comprise relationships with the relevant groups of individuals at Volkswagen Bank GmbH, Volkswagen Financial Services AG and the Group parent company Volkswagen AG. As in the prior year, relationships with pension plans and the State of Lower Saxony were of lesser significance.

Members of Management and the Audit Committee of Volkswagen Bank GmbH are members of supervisory boards of other entities in the Volkswagen Group with which we sometimes conduct transactions in the normal course of business. All transactions with these entities are on an arm's-length basis.

All the remuneration for the Management is paid by Volkswagen Financial Services AG.

Provisions of €5 million (previous year: €4 million) have been recognized for pensions and similar obligations in favor of former members of the Management or their surviving dependants. The total payments made to former members of the Management and their surviving dependants amounted to less than €0.5 million, as had also been the case in the previous year.

67. Governing Bodies of the Volkswagen Bank GmbH Group

The members of the Management are as follows:

ANTHONY BANDMANN
Spokesman of the Management
Sales and Marketing
Customer Service, Retail Customers
Human Resources

HARALD HEßKE
Finance/Corporate Management
Back Office/Dealer Recovery/Risk Management

JENS LEGENBAUER
Europe (excluding Germany)

TORSTEN ZIBELL
Direct Bank
Corporate Development

The members of the Audit Committee are as follows:

DR. JÖRG BOCHE
Chairman
Executive Vice President of Volkswagen AG
Head of Group Treasury

WALDEMAR DROSDZIOK
Deputy Chairman
Chairman of the Joint Works Council of Volkswagen Financial Services AG,
Volkswagen Bank GmbH and Euromobil Autovermietung GmbH

DR. ARNO ANTLITZ
Member of the Board of Management Volkswagen Brand
Controlling and Accounting

GABOR POLONYI
Head of Fleet Customer Management, Volkswagen Leasing GmbH

68. Shareholdings

Name and registered office of company	Share of capital and voting rights in percent
I. Subsidiaries	
Volkswagen Bank Polska S.A., Warsaw, Poland	100.00
Volkswagen Serwis Ubezpieczeniowy Sp. z.o.o., Warsaw, Poland	100.00
II. Other long-term equity investments	
Society for Worldwide Interbank Financial Telecommunication SCRL, La Hulpe, Belgium	0.01
paydirekt Beteiligungsgesellschaft privater Banken mbH, Berlin	2.02
III. Shares in affiliated companies	
OOO Volkswagen Bank RUS, Moscow, Russian Federation	1.00

The equity of Volkswagen Bank Polska S.A. amounted to €86 million (PLN 378 million) as of December 31, 2015; Volkswagen Bank Polska S.A. generated a profit of €12 million (PLN 54 million) in 2015. This information is taken from the entity's IFRS financial statements.

MAN Financial Services S.p.A., Italy was merged into Volkswagen Bank GmbH on April 11, 2016, effective retroactively from January 1, 2016.

Each of the special purpose entities included in the consolidated financial statements in accordance with IFRS 10 (Private Driver 2011-3 GmbH i.L., Private Driver 2012-1 GmbH i.L., Private Driver 2012-2 GmbH i.L., Private Driver 2012-3 GmbH, Driver Ten GmbH, Driver Eleven GmbH and Driver Twelve GmbH has its registered office in Frankfurt am Main and has subscribed capital of €25,050. Each of the entities Private Driver 2013-1 UG (haftungsbeschränkt), Private Driver 2013-2 UG (haftungsbeschränkt), Private Driver 2014-1 UG (haftungsbeschränkt), Private Driver 2014-2 UG (haftungsbeschränkt), Private Driver 2014-3 UG (haftungsbeschränkt), Private Driver 2014-4 UG (haftungsbeschränkt), Private Driver 2015-1 UG (haftungsbeschränkt) and Driver Thirteen UG (haftungsbeschränkt) has its registered office in Frankfurt am Main and has subscribed capital of €5,100. The special purpose entity Driver Master S.A., Luxembourg, which was established in fiscal year 2015, has equity of €31,000. Driver France FCT, which has its registered office in Pantin, France, has liable capital of €300. Each of the above-mentioned German special purpose entities generated a profit of less than €0.1 million in 2015. The French special purpose entity generated a profit of €4 million in 2015 (previous year: €1 million).

Information on Volkswagen Serwis Ubezpieczіowy Sp.z.o.o., the equity investments and OOO Volkswagen Bank RUS, Moscow, Russian Federation, is not disclosed because they are of minor significance. For the same reason, no information is provided in accordance with IFRS 7.30.

69. Disclosures Relating to Unconsolidated Structured Entities

A structured entity is designed so that voting rights or similar rights are not the deciding factor in determining control over the entity.

Typical features of a structured entity are as follows:

- limited scope of activities;
- narrowly defined business purpose;
- inadequate equity to finance the business activities;
- financing through a number of instruments that contractually bind investors and that give rise to a concentration of credit risk and other risks.

Volkswagen Bank GmbH maintains business relationships with structured entities. These entities are ABS special purpose entities that securitize assets from lending agreements and leases for vehicle finance as asset-backed securities. Volkswagen Bank GmbH acquired these securities in full or in part or granted subordinated loans to structured entities. Under the principles specified in IFRS 10, these entities are not controlled by Volkswagen Bank GmbH and are therefore not included in the consolidated financial statements.

The purchase of the securities and the granting of subordinated loans give rise to counterparty default risk on the part of the issuers and interest rate risk. The maximum risk exposure of Volkswagen Bank GmbH arising from its involvement with unconsolidated structured entities is limited to the fair value of the acquired bonds reported in the balance sheet and the carrying amount of any subordinated loans granted to the entities concerned. The following table contains disclosures on Volkswagen Bank GmbH's assets reported in the balance sheet that are related to unconsolidated structured entities and the maximum risk exposure of the Volkswagen Bank Group (disregarding collateral). The nominal volume of the securitized assets is also disclosed.

	ABS SPECIAL PURPOSE ENTITIES	
€ million	2016	2015
Reported in the balance sheet as of December 31		
Marketable securities	2,264	323
Loans to and receivables from customers	1,144	1,271
Maximum loss risk	3,408	1,594
Nominal volume of securitized assets	14,842	6,063

Volkswagen Bank did not provide unconsolidated structured entities with any noncontractual support during the reporting period.

70. Events After the Balance Sheet Date

In January 2017, Volkswagen Financial Services AG added €400 million to the capital reserves.

The Standard & Poor's (S&P) senior unsecured ratings for unsecured bonds issued by Volkswagen Financial Services AG and Volkswagen Bank GmbH were downgraded by one notch on February 9, 2017 to BBB (Volkswagen Financial Services AG) and BBB+ (Volkswagen Bank GmbH) because of a regulatory amendment.

Otherwise, in the period up to February 14, 2017, there were no significant events that would have required a substantially different presentation of financial position and financial performance.

71. Responsibility Statement

To the best of our knowledge, and in accordance with the applicable reporting principles, the consolidated financial statements give a true and fair view of the assets, liabilities, financial position and profit or loss of the Group, and the management report of the Group includes a fair review of the development and performance of the business and the position of the Group, together with a description of the material opportunities and risks associated with the expected development of the Group.

Braunschweig, February 14, 2017
The Management

Anthony Bandmann

Harald Heßke

Jens Legenbauer

Torsten Zibell

Auditor's Report

We have audited the consolidated financial statements prepared by Volkswagen Bank Gesellschaft mit beschränkter Haftung, Braunschweig – comprising the balance sheet, the income statement, the statement of comprehensive income, the statement of changes in equity, the cash flow statement and the notes to the consolidated financial statements – together with the group management report, which is combined with the management report of Volkswagen Bank Gesellschaft mit beschränkter Haftung, Braunschweig, for the fiscal year from January 1 to December 31, 2016. The preparation of the consolidated financial statements and the combined management report in accordance with the IFRS, as adopted by the EU, and the additional requirements of German commercial law required to be applied under section 315a(1) of the Handelsgesetzbuch (HGB – German Commercial Code) is the responsibility of the Company's Management. Our responsibility is to express an opinion on the consolidated financial statements and the combined management report based on our audit.

We conducted our audit of the consolidated financial statements in accordance with section 317 HGB and German generally accepted standards for the audit of financial statements promulgated by the Institut der Wirtschaftsprüfer (IDW – Institute of Public Auditors in Germany). Those standards require that we plan and perform the audit such that misstatements materially affecting the presentation of the net assets, financial position and results of operations in the consolidated financial statements in accordance with the applicable financial reporting framework and in the combined management report are detected with reasonable assurance. Knowledge of the business activities and the economic and legal environment of the Group and expectations as to possible misstatements are taken into account in the determination of audit procedures. The effectiveness of the accounting-related internal control system and the evidence supporting the disclosures in the consolidated financial statements and the combined management report are examined primarily on a test basis within the framework of the audit. The audit includes assessing the annual financial statements of those entities included in the consolidated financial statements, the determination of the entities to be included in the consolidation, the accounting and consolidation principles used and significant estimates made by the Company's Management, as well as evaluating the overall presentation of the consolidated financial statements and the combined management report. We believe that our audit provides a reasonable basis for our opinion.

Our audit has not led to any reservations.

In our opinion, based on the findings of our audit, the consolidated financial statements comply with the IFRS, as adopted by the EU, and the additional requirements of German commercial law required to be applied under section 315a(1) HGB and give a true and fair view of the net assets, financial position and results of operations of the Group in accordance with these provisions. The combined management report is consistent with the consolidated financial statements, complies with the statutory requirements, and as a whole provides a suitable view of the Group's position and suitably presents the opportunities and risks of future development.
Hanover, February 14, 2017

PricewaterhouseCoopers
Aktiengesellschaft
Wirtschaftsprüfungsgesellschaft

Burkhard Eckes	Lothar Schreiber
Wirtschaftsprüfer	Wirtschaftsprüfer
(German Public Auditor)	(German Public Auditor)

Report of the Audit Committee

of Volkswagen Bank GmbH

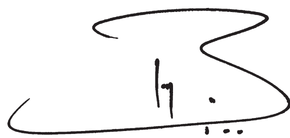
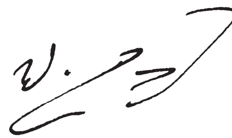
Volkswagen Bank GmbH is a publicly traded corporation within the meaning of section 264d of the HGB. In accordance with the provisions in section 324 of the HGB, the Bank has established an Audit Committee, which concerns itself in particular with the tasks described in section 107(3) sentence 2 of the Aktiengesetz (AktG – German Stock Corporation Act). The Audit Committee has four members. There were no changes in the composition of the Audit Committee compared with the prior year.

The Audit Committee held two regular meetings in the reporting period. There were no extraordinary meetings. During the reporting period, there were no urgent transactions that would have required a decision by circulation of written resolution for approval. All members of the Audit Committee were present at all the meetings.

At the meeting held on February 19, 2016, the Audit Committee reviewed the annual financial statements and the management report, the consolidated financial statements and the group management report of Volkswagen Bank GmbH for the year ended December 31, 2015 together with the proposal for the appropriation of profit. As part of this review, the Audit Committee discussed with the external auditors the reports on the audit of the annual financial statements, management report, consolidated financial statements and group management report of Volkswagen Bank GmbH as well as material transactions and issues related to financial reporting. The Audit Committee reported on its review to the sole shareholder. In addition, the Committee received reports on the diesel issue, the business and risk strategy, the funding and liquidity position, and on the internal and external audit activities and their findings. The Committee also gathered details to establish the extent to which there were relationships of a professional, financial or other nature between the external auditors and the Company and/or its governing bodies with a view to assessing the independence of the external auditors. In this regard, the Audit Committee obtained information on the services that the external auditors had provided for the Company in addition to the auditing activities and on whether there were any grounds for disqualification or partiality. Following a detailed evaluation of the independence of the external auditors, the Audit Committee submitted a recommendation to the sole shareholder regarding the election of the external auditors and drew up the resolution covering the issue of the audit engagement in preparation for the Annual General Meeting.

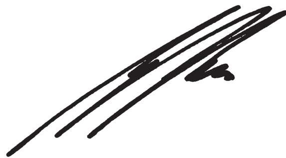
At its meeting on October 27, 2016, the Audit Committee focused in particular on the risk management system at Volkswagen Bank GmbH. The committee also received detailed reports on IT issues of current importance and from the compliance officer. In addition, it held discussions with the external auditor regarding audit planning, key points of the audit and the auditor's information requirements.

Braunschweig, March 1, 2017

Dr. Jörg Boche
Chairman

Waldemar Drosdziok
Deputy Chairman



Dr. Arno Antlitz
Member

Gabor Polonyi
Member

NOTE ON FORWARD-LOOKING STATEMENTS

This report contains forward-looking statements on the future business development of Volkswagen Bank GmbH. These statements are based on assumptions relating to the development of the global economy and of the financial and automotive markets, which Volkswagen Bank GmbH has made on the basis of the information available to it and which it considers to be realistic at the time of going to press. The estimates given entail a degree of risk, and the actual developments may differ from those forecast.

Should actual developments turn out to be different, contrary to expectations and assumptions, or unforeseen events occur that have an impact on the business of Volkswagen Bank GmbH, this will have a corresponding effect on the business development of the Company.

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VOLKSWAGEN BANK GMBH

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