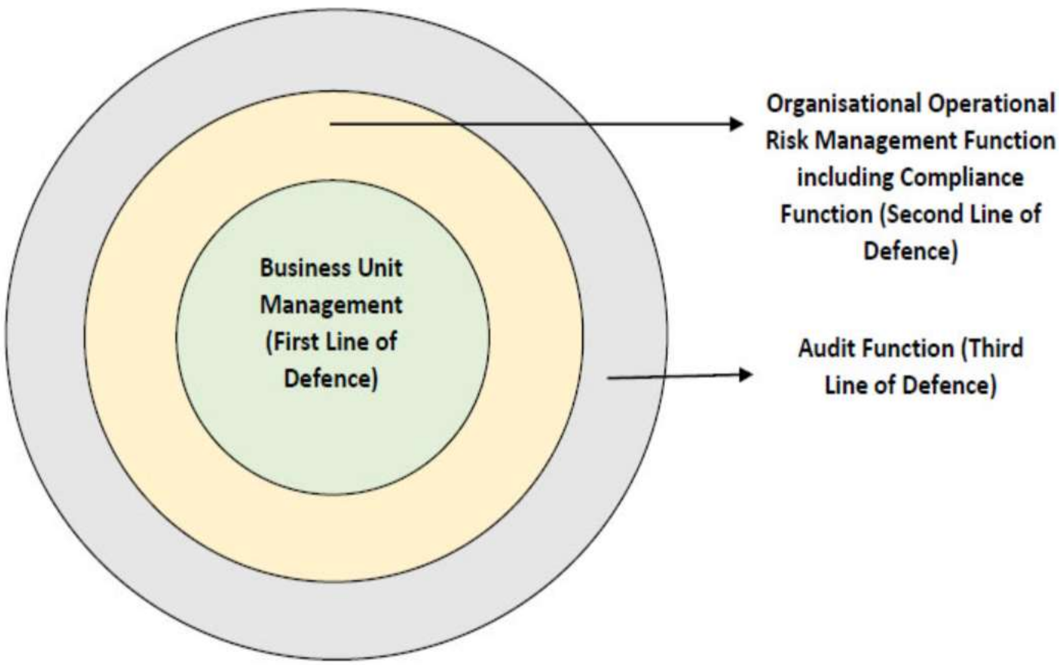
Reserve Bank of India has issued the Guidance Note on Operational Risk Management and Operational Resilience having reference no. RBI/2024-25/31 DOR.ORG.REC.21/14.10.001/2024-25 dated April 30, 2024 where the RBI has mandated the NBFCs to formulate the Operational Risk and Resilience policy. The company has in place the Operational Risk and Resilience policy.

The gist of the same is as mentioned below:

1. Three lines of Defence for management of Operational Risk

Sound internal governance forms the foundation of an effective Operational Risk Management (ORM) . As a part of ORM, SF3-IN shall rely on three lines of defenses:



A. First line of Defence

Business Unit Management typically forms the first line of defence. Sound Operational Risk governance recognises that business unit management is responsible for identifying and managing the risks inherent in the products, services, activities, processes and systems for which it is accountable. The responsibilities of an effective first line of defence in promoting a sound Operational Risk Management culture at SF3-IN include:

- Identifying and assessing the materiality of Operational Risks inherent in their respective business units through the use of Operational Risk Management (ORM) tools;
- Establishing appropriate controls to mitigate inherent Operational Risks, and assessing the design and effectiveness of these controls through the use of the Operational Risk Management tools;
- Reporting whether the business units lack adequate resources, tools, and training to ensure identification and assessment of Operational Risks;

- Monitoring and reporting the business units Risks, and ensuring their adherence to the established Operational Risk appetite and tolerance statement; and
- Reporting Risks, residual Operational Risks not mitigated by controls, including operational loss events, control deficiencies, process inadequacies, and zero tolerance topics.

B. Second line of Defence

Risk Management and Compliance function forms the second line of defence. The responsibilities of an effective second line of defence in promoting a sound Operational Risk Management culture should include:

- Developing an independent view regarding business units' (a) identified material Operational Risks, (b) design and effectiveness of key controls, and (c) risk tolerance;
- Challenging the relevance and consistency of the business unit's implementation of the Operational Risk Management tools, measurement activities and reporting systems, and providing evidence of this effective challenge;
- Developing and maintaining Operational Risk Management and measurement policies, standards and guidelines;
- Reviewing and contributing to the monitoring and reporting of the Operational Risk; and
- Designing and providing Operational Risk training and instilling risk awareness.

C. Third line of Defence

The third line of defence, i.e the audit function provides an independent assurance to the SF3-IN Board regarding the appropriateness of ORM. Internal Audit function's staff should not be involved in the development, implementation and operation of Operational Risk Management processes which has been carried out by the other two lines of defence. The third line of defence reviews are generally carried out by internal and/or external audit but may also involve suitably qualified independent third parties. The scope and frequency of reviews should not only be sufficient to cover all activities at SF3-IN, aligned with the Operational Risks , and identify and prioritize key risk areas that warrant thorough examination but also be responsive to the dynamic nature of the Operational Risk environment. An effective independent review includes two processes:

(i) Validation

Ensuring that the quantification systems used are sufficiently robust as they provide assurance about the integrity of inputs, assumptions, processes and methodologies and results in assessment of Operational Risk.

(ii) Verification

Review of the design and implementation of the Operational Risk Management systems (including compliance and consistency with Board policies) and associated governance processes through the first and second lines of defence (including the independence of the second line of defence):

- Review of validation processes to ensure they are independent and implemented in a manner consistent with established SF3-IN Regulations/policies;
- Ensuring that business units' management promptly, accurately and adequately responds to the issues raised, and regularly reports to the Board of Directors or its relevant Committees on pending and closed issues;
- Identifying gaps, if any, in the Operational Risk Management Framework (ORMF) and reporting to the Board or its relevant Committee; and
- Providing opinion on the overall adequacy and appropriateness of the ORMF and the associated governance processes across the SF3-IN by assessing whether the ORMF meets organisational needs and expectations (such as in respect of the risk appetite and tolerance, and adjustment of the framework to changing circumstances) and complies with statutory and legislative provisions, contractual arrangements, internal rules and ethical conduct.

2. DISCLOSURE REQUIREMENTS

BMW India Financial Services Private limited is a Private Limited Company and a middle layer NBFC and does not have the disclosure requirement as applicable to Listed Companies.
Currently, disclosures in annual financial statements are guided by the following regulations:

1. Companies Act, 2013 read with the rules made thereunder,
2. Master Direction – Reserve Bank of India (Non-Banking Financial Company – Scale Based Regulation) Directions, 2023 dated October 19, 2023, as amended from time to time, and
3. Accounting Standards & Guidelines issued by Institute of Chartered Accountants of India (ICAI) etc.

Further as per Master Direction – Reserve Bank of India (Non-Banking Financial Company – Scale Based Regulation) Directions, 2023 dated October 19, 2023, also gives information by way of Directors' Report and Management Discussion and Analysis Report about the overall performance, its business strategies, its services, products, Risk Management, etc. in its Annual Report every year as a matter of good governance through proper disclosure.

3. RISKS AND CONCERNS

The following risk types have been considered for the current period and have been actively steered:

Credit Risk is the most significant risk type. This is due to the original business model, which offers financing. This risk is consciously taken within a certain risk framework and closely monitored. The Credit risk relevant figures are measured and reported on a monthly basis for both retail and commercial finance businesses.

Interest Rate Risk focuses on potential loss caused by change in market interest rates. Interest Rate risk is included and calculated as a part of the risk inventory by using a value at risk approach. The calculation is based on historical changes of market interest rates. Within BMW Financial

Services there are defined parameters for interest rate risk, which are steered with a benchmark. The benchmark approach is followed.

Liquidity Risk is a risk of not being able to fulfil the Company's payment obligations in due time. The risk arises from both raising as well as lending of funds. This risk is avoided by following defined matched funding principles. The Matched Funding Principles aim to manage maturity mismatches and represent the effect of funding measures. The Matched Funding structure is measured and reported on a monthly basis. Any mismatch between asset and liability maturities is also maintained within the defined range.

Operational Risk is defined as the risk of loss resulting from failure or inadequacy of internal control. Majorly, there are four risk categories under Operational risk: organization processes, people and systems (technology) or from external events. The Company closely monitors the same and reporting is done by operational risk delegates on regular intervals thus ensuring an appropriate steering of operational risk. In addition, a yearly assessment of the quality and efficiency of the Company's risk management set-up is conducted.

Business Risk comprises of risk types that are inseparably linked to the realization of business activities. They take into account both the effects of the economic environment and the impact of fundamental business decisions whose consequences are difficult to predict. Business risk is influenced by numerous factors, including sales volume, per-unit price, input costs, competition, and overall economic climate and government regulations. The Company is in an emerging market, in a developing country, where there is high risk of government regulation. Business risk is steered and measured in terms of key indicators such as market penetration rates and profit margins to ensure that the Company continues to grow even when macro prudential supervision measures apply.

Earnings risk is the risk of potential profitability reductions or increase in expenses which results in reduction in profitability. There are various factors (such as general business risk) which can affect the planned profitability. Therefore, deviations from plan are tracked regularly in line with the monthly reporting and regular forecasting processes.

All the above-mentioned risks are steered, monitored and reported on a regular basis.

Risk Strategy

The Company has developed and implemented a Risk Strategy which provides an insight into the risks faced by the Company. The aim of the Risk Strategy is to continuously and systematically carry out risk management within the organization.

The process of identification, measurement of material risks, steering and influencing the risks identified, constant monitoring is followed under risk strategy.

The Board of Directors through the Risk Management Committee takes responsibility for the overall process of risk management in the organisation. The Risk Management and Risk Controlling processes of the Company are compliant with the BMW Group Financial Services policies and ensure that all risks are identified, assessed, controlled, monitored and communicated. The group

Risk Management system comprises of a decentralised network covering all parts of the business and is steered by a centralised risk management function.

The Board of Directors of BMW Financial Services periodically approves the Risk identified and their mitigation plans devised by the Risk Management Committee.