



ANNUAL REPORT 2017 **OF BANK ZACHODNI WBK**

2017



Bank Zachodni WBK

 **Grupa Santander**

Dear All,

In 2017, Bank Zachodni WBK consistently pursued its development strategy strengthening its position among the top Polish banks. Our performance demonstrates that we have adopted the right strategy.

Once again, we have set new standards for building relationships with customers and creating innovative bank products. We are actively shaping the Polish banking sector by supporting consolidation processes as showcased by the planned integration of the demerged part of the business of Deutsche Bank Polska to the structures of Bank Zachodni WBK. This transaction will strengthen our current position in the domestic banking market and provide new development opportunities for Bank Zachodni WBK in the upcoming years, among others in the private banking and business banking areas.

The economic revival on Polish and European markets has also been a positive stimulus for the Bank's growth.

At the same time, the banking sector faced legal challenges resulting from the actions taken by legislative and regulatory bodies both in the European Union and in Poland forcing financial institutions to promptly adjust their business models to the new requirements.

Macroeconomic environment - we are on the rise

2017 positively surprised us with the pace of economic growth. Already at the beginning of the year, the GDP growth rate exceeded 4% yoy to go beyond 5% yoy at the year-end with the average growth of 4.6% over the year.

Consumption was the driving force behind the economic growth (first fuelled by 500+ programme and then by growing wages and lower households savings) along with exceptionally favourable external environment (in particular sound revival in the Euro zone), which boosted Polish exports. The long-awaited rebound in investment started to materialise in the H2 2017 to gain momentum in the fourth quarter.

Unemployment went down to a record low level and the shortage of labour force has become a serious problem for Polish companies and one of the key obstacles for business growth. Fortunately, the employers were relieved by the labour migration, mainly from Ukraine. The domestic labour market was not significantly disturbed even by the lowering of retirement age introduced in October 2017. However, a salary pressure was observed and it seems quite likely that the remuneration growth will accelerate in 2018 as the imbalance between the labour demand and supply will not decline.

Banking sector ready for new challenges

In 2017, the sector consolidation, observed over the last few years, accelerated with Bank Zachodni as its active participant. We are convinced that thanks to the acquisition of demerged part of Deutsche Bank Polska business, based on experience and skills presented by the teams in those two banks, we will provide customers with a convenient and modern access to services, a branch network covering the entire country and even better, more innovative products and financial solutions.

Banks are also consistently investing in digitisation which is key to sustain profitability in the upcoming years. The Polish banking sector is the most mature in this respect in the Central Europe, both as regards the online and mobile channels.

The issue of mortgage fx loans continues to be a significant challenge for the banking sector. We believe that the adopted solutions will take into account both the interests of the customers and the stability of the banking sector and, in consequence, of the Polish economy.

Bank As You Want It

Our Customers and the relationship with them have always been in the centre of development strategy and business transformation of Bank Zachodni WBK. Therefore, in 2017, we implemented a new strategy based on brand promise "Bank As You Want It". We focus on a progressive growth of customers' satisfaction and ensuring top service standards at each touchpoint with the Bank by offering solutions fully tailored to their individual needs.

The first products designed in line with the new concept of “The Bank As You Want It” is the “Account As I Want It” which comes with a customised card to enable simple and quick personalisation of selected functions. This is an innovative and pioneering solution in the entire Polish banking sector.

The digital transformation is an important element of those changes. Bank Zachodni WBK is one of the leaders in this area. We invest in new technologies enhancing simple, intuitive and integrated access to services and interactive relationship with the customer. We were the first in the Polish banking sector to introduce the video identification service based on biometrics and digital signature in the cloud. The fundamental initiatives encompass also digitalisation and robotisation of processes, design of an optimal model of distribution channels, further growth of CRM, Big Data analysis, and development of Internet and mobile channels, including biometric authentication and authorisation technologies. The digital transformation covered retail, SME and corporate banking.

We have completed work on a distribution strategy defining new roles for digital channels and branches, new branch design and layout, new profile of an advisor and optimal network coverage. We concentrate on leveraging the potential of digital channels while the primary role of branches will be to develop relationships with customers, educate them in using digital channels and sell products to customer preferring personal contacts with advisors.

Through the “Bank As You Want It” strategy we want to be not only the best bank for the customers but also the innovator whose primary goal is to increase loyalty of our customers and business partners.

Business effectiveness

Our financial performance confirms the effectiveness of our development strategy. In 2017, the gross profit of Bank Zachodni WBK totalled PLN 2.5bn, the total income increased substantially and the value of our assets reached almost PLN 133bn.

We enjoy a strong capital position, compliant with regulatory requirements. We have continued strict control over costs whose level has not changed yoy despite investments in the future and development of the Bank.

In 2017, we decided to pay out a dividend of PLN 5.4 per share from retained profit. We successfully conducted a subordinated debt issue worth USD 150m, paid out in EUR, in the form of green bonds. That was the first operation of such kind performed by a Polish bank.

Positive performance is accompanied by growth in our customers’ trust and satisfaction who appreciate the Bank’s digital transformation policy. This is evidenced by a 4.5% growth yoy in the number of active users in digital channels. In 2017, customers made over 23.5m transactions using the mobile banking channel which represents a 10.2m growth yoy (+76%). The number of credit products sold via remote channels (mobile, Internet, contact centre) surged by 36%.

As for the SME segment, we consistently strive to become first choice bank for Polish entrepreneurs. The number of customers is growing in response to simplified access to financial solutions and business support.

The Business and Corporate Banking Division persistently increased its market share in 2017, and the lending activity and new sales were growing steadily. This is the result of a new strategy introduced at the beginning of 2017 with the emphasis on customers acquisition and activation by ensuring flexible approach to their needs. We continued the Export Development Programme and initiated, leveraging the Santander Group potential, the International Businesses Corridors Programme to facilitate customers’ access to new business partners on international markets. We also gradually developed the sectoral approach which is a unique offer on the Polish market, giving us a better understanding with a view to tailoring our products to business needs.

2017 was also successful for the **Global Corporate Banking Division**. We played a leading role in numerous transactions for the main sectors of the Polish economy, such as the biggest private placement transaction in the history of Warsaw Stock Exchange for a top telecommunication company. We also actively supported our domestic and international customers by financing their development and acquisition deals, hedging fx and interest rate risk, and providing advisory services in capital and M&A transactions.

In 2017, changes took place in the composition of the Bank's Management Board. Dorota Strojowska, in charge of the Business Partnership Division, Arkadiusz Przybył, in charge of the Retail Banking Division and Maciej Reluga, the head of Financial Management Division joined the Board. Eamonn Crowley resigned from his post.

Corporate social responsibility

Responsibility is one of the foundations of Bank Zachodni WBK. This is why we initiate and actively participate in CSR projects. In 2017, similarly as in the previous years, we focused on activities that are important for large communities and that make a lasting change in the society. By this, I mean investments in science and education, supporting local communities, promoting equal opportunities and social inclusion and popularizing road safety standards. The scale of these activities is constantly growing, reflecting our belief in the synergy of business and investments that stimulate development of a civic society.

In 2017, Bank Zachodni WBK engaged, amongst others, in the following social projects: Jak Jeźdźsisz (How's Your Driving), Santander Orchestra, Santander Universidades, Obsługa bez barier (Barrier-Free Banking). Bank Zachodni WBK Foundation and volunteering campaigns our employees got involved in also made a lasting difference.

Our commitment to the Customers

It was our Customers' trust in our strategy of being the best bank for them that enabled Bank Zachodni WBK to generate satisfactory results in 2017. It was also, and I cannot stress it enough, a reflection of skills, experience and engagement of all Bank's employees that is visible in their work, each and every single day. Thanks to all this, Bank Zachodni WBK won the "Best Bank in Poland" award for third time in a row in a prestigious competition "Euromoney Awards for Excellence". Bank Zachodni WBK was also awarded for its outstanding financial results, business efficiency and successful implementation of innovations and new technologies to foster customer satisfaction and add value. **The Bank also received the "Best Bank in Poland for SME" award as the best bank in Poland for SMEs.** Once again, we were ranked first in "Financing Provider of the Year" category and we received Eurobuild Awards title for the best real estate bank in CEE.

We perceive all the awards as a valuable feedback but also a commitment to continue our hard work on improving the quality of our services and customer satisfaction.

Michał Gajewski

President of Bank Zachodni WBK S.A. Management Board

FINANCIAL HIGHLIGHTS		PLN k		EUR k		
		for reporting period ended:		31.12.2017	31.12.2016	31.12.2017
Stand alone financial statement						
I	Net interest income		3 785 549	3 480 440	891 830	795 402
II	Net fee and commission income		1 726 648	1 604 735	406 777	366 738
III	Operating profit		2 903 317	3 005 326	683 986	686 822
IV	Profit before tax		2 515 330	2 649 248	592 581	605 446
V	Profit for the period		1 916 156	2 081 720	451 423	475 746
VI	Total net cash flows		(4 048 528)	(175 348)	(953 784)	(40 073)
VII	Total assets		132 863 268	131 417 988	31 854 820	29 705 693
VIII	Deposits from banks		1 414 448	1 212 765	339 123	274 133
IX	Deposits from customers		102 155 522	103 381 249	24 492 441	23 368 275
X	Total liabilities		112 024 431	112 388 468	26 858 575	25 404 265
XI	Total equity		20 838 837	19 029 520	4 996 245	4 301 429
XII	Number of shares		99 333 481	99 234 534		
XIII	Net book value per share in PLN/EUR		209.79	191.76	50.30	43.35
XIV	Capital ratio		18.95%	16.52%		
XV	Profit per share in PLN/EUR		19.30	20.98	4.55	4.79
XVI	Diluted earnings per share in PLN/EUR		19.27	20.94	4.54	4.79
XVII	Declared or paid dividend per share in PLN/EUR*		5.40	-	1.27	-

*As of the date of publication of this report, the Management Board of Bank Zachodni WBK has not finalised its analysis in respect of recommendation on dividend payout for 2017. On 17.05.2017 Annual General Meeting of Bank Zachodni WBK S.A. adopted a resolution on dividend payment. It was decided to allocate PLN 535,866k from the Bank's undivided net profit for 2014 and 2015 to dividend for shareholders. Dividend per share was PLN 5.40.

The following rates were applied to determine the key EUR amounts for selected financials:

- for balance sheet items – average NBP exchange rate as at 29.12.2017 EUR 1 = 4,1709 PLN and as at 30.12.2016: EUR 1 = PLN 4.4240
- for profit and loss items – as at 31.12.2017 - the rate is calculated as the average of NBP exchange rates prevailing as at the last day of each month in 2017: EUR 1 = 4,2447; as at 31.12.2016 - the rate is calculated as the average of NBP exchange rates prevailing as at the last day of each month in 2016: EUR 1 = PLN 4.3757

As at 31.12.2017, FX denominated balance sheet positions were converted into PLN in line with the NBP FX table no. 251/A/NBP/2017 dd. 29.12.2017.



**FINANCIAL STATEMENT
OF BANK ZACHODNI WBK
FOR 2017**

2017



Bank Zachodni WBK

 Grupa Santander

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in thousands of PLN

Income statement of Bank Zachodni WBK

	for reporting period:	01.01.2017- 31.12.2017	01.01.2016- 31.12.2016
Interest income		4 703 187	4 469 917
Interest expenses		(917 638)	(989 477)
Net interest income	Note 5	3 785 549	3 480 440
Fee and commission income		2 048 486	1 904 106
Fee and commission expenses		(321 838)	(299 371)
Net fee and commission income	Note 6	1 726 648	1 604 735
Dividend income	Note 7	299 518	439 288
Net gains/(losses) on subordinated entities		(288)	-
Net trading income and revaluation	Note 8	183 229	266 371
Gains (losses) from other financial securities	Note 9	44 614	401 189
Other operating income	Note 10	83 763	119 465
Impairment losses on loans and advances	Note 11	(540 375)	(583 479)
Operating expenses incl.:		(2 679 341)	(2 722 683)
<i>Bank's staff, operating expenses and management costs</i>	<i>Notes 12,13</i>	<i>(2 323 197)</i>	<i>(2 360 209)</i>
<i>Depreciation/amortisation</i>		<i>(274 954)</i>	<i>(234 117)</i>
<i>Other operating expenses</i>	Note 14	<i>(81 190)</i>	<i>(128 357)</i>
Operating profit		2 903 317	3 005 326
Tax on financial institutions		(387 987)	(356 078)
Profit before tax		2 515 330	2 649 248
Corporate income tax	Note 15	(599 174)	(567 528)
Profit for the period		1 916 156	2 081 720
Net earnings per share (PLN/share)	Note 16		
Basic earnings per share		19,30	20,98
Diluted earnings per share		19,27	20,94

Statement of comprehensive income of Bank Zachodni WBK

	for reporting period:	01.01.2017- 31.12.2017	01.01.2016- 31.12.2016
Profit for the period		1 916 156	2 081 720
Other comprehensive income which can be transferred to the profit and loss account:		438 053	(492 701)
Available-for sale financial assets valuation, gross		515 926	(713 041)
Deferred tax		(98 026)	135 478
Cash flow hedges valuation, gross		24 880	104 768
Deferred tax		(4 727)	(19 906)
Other comprehensive income which can't be transferred to the profit and loss account		(7 504)	5 208
Provision for retirement allowances – actuarial gains/losses, gross		(9 264)	6 430
Deferred tax		1 760	(1 222)
Other comprehensive income for the period, net of income tax		430 549	(487 493)
TOTAL COMPREHENSIVE INCOME FOR THE PERIOD		2 346 705	1 594 227

Notes presented on pages 8 - 99 constitute an integral part of this Financial Statement.

in thousands of PLN

Statement of financial position of Bank Zachodni WBK

	as at:	31.12.2017	31.12.2016
ASSETS			
Cash and balances with central banks	Note 17	4 114 801	4 696 634
Loans and advances to banks	Note 18	2 012 118	3 308 802
Financial assets held for trading	Note 19	3 421 547	3 198 187
Hedging derivatives	Note 20	146 724	66 787
Loans and advances to customers	Note 21	90 537 003	87 102 390
Financial assets available for sale	Note 22	25 784 029	26 322 361
Investments in subsidiaries and associates	Note 23	2 377 037	2 377 325
Intangible assets	Note 24	459 976	464 308
Goodwill	Note 25	1 688 516	1 688 516
Property, plant and equipment	Note 26	821 532	779 866
Net deferred tax assets	Note 27	709 867	950 307
Assets classified as held for sale	Note 28	8	608
Other assets	Note 29	790 110	461 897
Total assets		132 863 268	131 417 988
LIABILITIES AND EQUITY			
Deposits from banks	Note 30	1 414 448	1 212 765
Hedging derivatives	Note 20	578 798	1 961 828
Financial liabilities held for trading	Note 19	1 263 859	1 809 969
Deposits from customers	Note 31	102 155 522	103 381 249
Sell-buy-back transactions	Note 40	1 479 667	-
Subordinated liabilities	Note 32	1 488 602	440 457
Debt securities in issue	Note 33	1 240 244	1 783 303
Current income tax liabilities		61 143	12 999
Provisions	Note 34	82 600	66 345
Other liabilities	Note 35	2 259 548	1 719 553
Total liabilities		112 024 431	112 388 468
Equity			
Share capital	Note 36	993 335	992 345
Other reserve capital	Note 37	16 176 183	15 132 993
Revaluation reserve	Note 38	712 303	281 754
Retained earnings		1 040 860	540 708
Profit for the current period		1 916 156	2 081 720
Total equity		20 838 837	19 029 520
Total liabilities and equity		132 863 268	131 417 988

Notes presented on pages 8 - 99 constitute an integral part of this Financial Statement.

in thousands of PLN

Statement of changes in equity

Statement of changes in equity	Share capital	Other reserve capital	Revaluation reserve	Retained earnings and profit for the period	Total
Note	36	37	38		
Opening balance as at 31.12.2016	992 345	15 132 993	281 754	2 622 428	19 029 520
Total comprehensive income	-	-	430 549	1 916 156	2 346 705
Profit for the period	-	-	-	1 916 156	1 916 156
Other comprehensive income	-	-	430 549	-	430 549
Issue of shares	990	-	-	-	990
Distribution of profits and losses	-	1 045 702	-	(1 045 702)	-
Dividends	-	-	-	(535 866)	(535 866)
Share scheme charge	-	(2 512)	-	-	(2 512)
As at 31.12.2017	993 335	16 176 183	712 303	2 957 016	20 838 837

The revaluation reserve of PLN 712,303 k comprises valuation of debt securities of PLN 237,275 k, equity shares of PLN 566,134 k, cash flow hedges of PLN (91,429)k and the provision for retirement allowances with cumulative actuarial gains of PLN 323 k.

Statement of changes in equity	Share capital	Other reserve capital	Revaluation reserve	Retained earnings and profit for the period	Total
Note	36	37	38		
Opening balance as at 31.12.2015	992 345	14 238 675	769 247	2 708 862	18 709 129
Total comprehensive income	-	-	(487 493)	2 081 720	1 594 227
Profit for the period	-	-	-	2 081 720	2 081 720
Other comprehensive income	-	-	(487 493)	-	(487 493)
Distribution of profits and losses	-	878 105	-	(878 105)	-
Dividends	-	-	-	(1 290 049)	(1 290 049)
Share scheme charge	-	16 213	-	-	16 213
As at 31.12.2016	992 345	15 132 993	281 754	2 622 428	19 029 520

The revaluation reserve of PLN 281,754 k comprises valuation of debt securities of PLN (143,435)k, equity shares of PLN 528,944k, cash flow hedges of PLN (111,581)k and the provision for retirement allowances with cumulative actuarial gains of PLN 7,826 k.

Notes presented on pages 8 - 99 constitute an integral part of this Financial Statement.

in thousands of PLN

Statement of cash flows of Bank Zachodni WBK

	for reporting period:	01.01.2017- 31.12.2017	01.01.2016- 31.12.2016
Profit before tax		2 515 330	2 649 248
Total adjustments:			
Depreciation/amortisation		274 954	234 117
Profit from investing activities		(58 698)	(407 305)
Impairment losses		8 342	13 767
		2 739 928	2 489 827
Changes in:			
Provisions		16 255	(16 304)
Trading portfolio financial instruments		(1 469 353)	950 591
Hedging derivatives		(1 462 967)	33 852
Loans and advances to banks		(273)	1 005 145
Loans and advances to customers		(3 434 613)	(5 977 040)
Deposits from banks		201 824	225 942
Deposits from customers		(636 987)	9 079 395
Buy-sell/ Sell-buy-back transactions		1 479 667	(3 990 565)
Other assets and liabilities		278 379	460 547
		(5 028 068)	1 771 563
Interest accrued excluded from operating activities		(522 528)	(508 586)
Dividend		(298 972)	(438 757)
Paid income tax		(411 583)	(713 260)
Net cash flows from operating activities		(3 521 223)	2 600 787
Inflows		3 934 371	6 237 656
Sale/maturity of financial assets available for sale		3 012 773	5 179 272
Sale of intangible assets and property, plant and equipment		22 226	19 534
Dividend received		298 972	438 609
Interest received		600 400	600 241
Outflows		(3 818 079)	(8 451 780)
Purchase of financial assets available for sale		(3 491 908)	(8 155 389)
Purchase of intangible assets and property, plant and equipment		(326 171)	(296 391)
Net cash flows from investing activities		116 292	(2 214 124)
Inflows		2 031 978	2 454 500
Debt securities in issue		1 988 788	1 065 880
Proceeds from issuing/shares		990	-
Drawing of loans		42 200	1 388 620
Outflows		(2 675 575)	(3 016 511)
Debt securities buy out		(1 430 000)	(980 000)
Repayment of loans		(630 728)	(670 906)
Dividends and other payments to shareholders		(535 866)	(1 290 049)
Interest paid		(78 981)	(75 556)
Net cash flows from financing activities		(643 597)	(562 011)
Total net cash flows		(4 048 528)	(175 348)
Cash and cash equivalents at the beginning of the accounting period		11 554 555	11 729 903
Cash and cash equivalents at the end of the accounting period		7 506 027	11 554 555

Cash components are presented in Note 45.

Information regarding liabilities arising from financial activities in loans received, subordinated liabilities and the issue of debt securities were presented respectively in notes 30-33.

Notes presented on pages 8 - 99 constitute an integral part of this Financial Statement.

in thousands of PLN

Additional notes to financial statement of Bank Zachodni WBK

1. General information about issuer

Bank Zachodni WBK S.A. is a bank seated in Poland, 50-950 Wrocław, Rynek 9/11, TIN 896-000-56-73, National Official Business Register number (REGON) 930041341, registered in the District Court for Wrocław-Fabryczna, VI Economic Unit of the National Court Registry under 0000008723 number.

The immediate and ultimate parent entity of Bank Zachodni WBK S.A. is Banco Santander S.A., having its registered office in Santander, Spain.

Bank Zachodni WBK S.A. offers a wide range of banking services for individual and business customers and operates in domestic and interbank foreign markets. Additionally, it offers also the following services:

- intermediation in trading securities,
- leasing,
- factoring,
- asset/ fund management,
- insurance services,
- trading in stock and shares of commercial companies,
- brokerage activity.

2. Basis of preparation of financial statement

2.1 Statement of compliance

This unconsolidated annual financial statement of Bank Zachodni WBK S.A. was prepared in accordance with the International Financial Reporting Standards (IFRS) adopted by the European Union, which are applied on a consistent basis, as at 31.12.2017 and, in the case of matters not governed by the above Standards, in accordance with the provisions of the Accounting Act of 29.09.1994 (consolidated text: Journal of Law of 22 November 2017, item 2342, as amended) and related implementing acts as well as the requirements imposed on issuers whose securities are admitted to trading on regulated markets or issuers who have applied to have securities admitted to trading on regulated markets outlined in Act dated 29 July 2005 on Public Offering, on Conditions for the Introduction of Financial Instruments to the Organized Trading System and on Public Companies.

These unconsolidated financial statements have been approved for publication by Bank Zachodni WBK S.A. Management Board on 12 February 2018.

Unconsolidated financial statement of Bank Zachodni WBK S.A. is published on the same date as the consolidated report of the BZ WBK Group.

in thousands of PLN

2.2. New standards and interpretations or changes to existing standards or interpretations which can be applicable to the Bank Zachodni WBK S.A. and are not yet effective or have neither been implemented earlier

IFRS	Nature of changes	Effective from	Influence on Bank Zachodni WBK S.A.
IFRIC 22 Foreign Currency Transactions and Advance Consideration *	IFRIC Interpretation 22 clarify the date of the transaction for the purpose of determining the exchange rate to use on initial recognition of the related asset, expense or income when an entity has received or paid advance consideration in a foreign currency. The Interpretation relates to the situation when the transaction is in foreign currency and the entity pays or receives consideration in advance in a foreign currency before the recognition of the related asset, expense or income.	1 January 2018	The amendment will not have a significant impact on financial statements.
IFRS 9 Financial Instruments	<p>The changes refer to the following areas:</p> <ul style="list-style-type: none"> • Classification and measurement – introduction of three classification categories for debt instruments, i.e. measured at: amortised cost, fair value through other comprehensive income and fair value through profit or loss. Changes were made in the measurement of equity instruments by limiting the possibility of measurement at historical cost; • Expected credit losses – introduction of a new model for recognition of impairment (ECL): impairment charge is required to be measured as lifetime expected credit losses rather than 12-month expected credit losses; • Hedge effectiveness testing and eligibility for hedge accounting – replacement of the precise effectiveness range (80-125%) with a requirement that there is an economic relationship between the hedged item and the hedging instrument and that the hedge ratio is the same as the one used for risk management purposes. Ineffective hedges continue to be taken to a profit and loss account; • Hedged items – new requirements allow appointment of new hedged items in relation to certain economically viable hedging strategies, which, to date, were not eligible under IAS 39; • Hedging instruments – relaxation of requirements pertaining to certain hedging instruments listed in IAS 39. The standard allow recognition of the time value of options purchased and implementing non-derivative financial instruments as hedging instruments; • Recognition of change in the fair value of financial liability arising from changes in the liability's credit risk in other comprehensive income (in principle). 	1 January 2018	IFRS 9 implementation is described below.
Amendment to IFRS 9 Financial Instruments Prepayment right with negative compensation*	Amendment to IFRS 9 is effective for annual periods starting from 1 January 2019 or later with a possibility of earlier application. As a result of amendment to IFRS 9, companies will be able to measure pre-payable financial assets with negative compensation at amortised cost or at fair value through other comprehensive income if a specified condition is met, instead of at fair value a valuation at fair value through profit or loss.	1 January 2019	Bank Zachodni WBK S.A. is currently in the process of analysing the amendment of the Standard and the assessment of impact of the amendment
IFRS 15 - Revenue from Contracts with Customers	<p>Changes relate to the following areas:</p> <ul style="list-style-type: none"> • Transfer of control – recognition of revenue only when the customer gains control over a good or service. The amendment makes the definition of the transfer of control more precise. Introducing regulations allowing to define the legitimacy of recognising the revenue over time or at a point in time; • Variable consideration - the amendment takes into account variable consideration in prices of goods or services arising, for example, as a result of penalties or performance bonus; • Allocation of the transaction price on the basis of an adequate sales price per unit - introduction of the requirement to allocate the payment for goods or services in the case of sale under a single contract; • Licences - introduction of the requirement for entities to define the time for which a licence is transferred and specifying more precisely the revenue calculation in the case of transferring a licence at a point in time or over time; • Time value of money – the transaction price is adjusted for the time value of money. The entity may choose not to account for the time value of money when the interval between transfer of the promised goods or services and payment by the customer is expected to be less than 12 months; • Costs of obtaining a contract - introducing the conditions which determine if the given costs of obtaining a contract are subject to capitalization and can be amortised parallel to revenue recognition; • Disclosures - introduction of a requirement to disclose qualitative and quantitative information relating to judgements and changes in the judgements related with revenue recognition. 	1 January 2018	IFRS 15 implementation is described below.
Commentary on IFRS 15 Revenue from Contracts with Customers	<p>The commentary is a source of additional information and guidance re: the key assumptions of IFRS 15, including the identification of unit-specific commitments, the establishment of the unit's role (agent vs. principal) and the mode of recording revenue generated under the licence.</p> <p>Apart from additional guidance, there are exemptions and simplified rules for first time adopters.</p>	1 January 2018	IFRS 15 implementation is described below.

in thousands of PLN

IFRS 16 Leases	<p>The new standard establishes principles for the recognition, measurement, presentation and disclosure of leases. All lease transactions results in the lessee's right to use the assets and the obligation to make a payment. Accordingly, the classification of leases into operating lease and finance lease as per IAS 17 no longer applies under IFRS 16, as the new standard introduces a single model for accounting for leases by the lessee. The lessee will be required to present the following: (a) assets and liabilities in respect of all leases executed for more than 12 months, except where an asset is of low quality; and (b) depreciation charge for the leased asset separately from the interest expense on the lease liability in the statement of profit or loss and other comprehensive income.</p> <p>The principles of accounting for leases by the lessee established in IFRS 16 are largely the same as in IAS 17. As a consequence, the lessee continues to use the classification into operating lease and finance lease and accounts for them accordingly.</p>	1 January 2019	IFRS 16 implementation progress is described below.
Annual Improvements to IFRS 2014-2016 *	<p>In December 2016, the International Accounting Standards Board published 'Annual Improvements to IFRS Standards 2014-2016 Cycle' which amended 3 standards, i.e. IFRS 12 'Disclosure of Interests in Other Entities', IFRS 1 'First-time Adoption of International Financial Reporting Standards' and IAS 28 'Investments in Associates'.</p> <p>The improvements feature guidelines and amendments re: the scope of applicability, recognition and valuation as well as terminology and editing changes.</p>	1 January 2018 for improvements to IFRS 1 and IAS 28	The amendment will not have a significant impact on financial statements.
Amendments to IAS 28 Long-term Interests in Associates and Joint Ventures *	<p>The amendment is effective for annual periods starting from 1 January 2019 or later with a possibility of earlier application. The amendments to IAS 28 Investments in Associates and Joint Ventures clarify that companies accounting for long-term interests in an associate or joint venture where the equity method is not applied, have to use IFRS 9. The IASB has also published an example that illustrates how companies apply the requirements in IFRS 9 and IAS 28 to long-term interests in an associate or joint venture.</p>	1 January 2019	Bank Zachodni WBK S.A. is currently in the process of analysing the amendment of the Standard and the assessment of impact of the amendment
Improvements to IAS 40 'Investment Property' *	<p>Improvements to IAS 40 specify the requirements for transfers to or from investment property classification. According to the amended standard, a change in management intention to use the property is not evidence of change in the use of the property. The amendment applies to all changes in use that are introduced after the effective date of the amendment and to all investment properties held at that date.</p>	1 January 2018	The amendment will not have a significant impact on financial statements.
Amendments to IFRS 2: Classification and measurement share-based payment transactions *	<p>Changes relate to the following areas:</p> <ul style="list-style-type: none"> • Guideliness on fair value measurement of liability due to cash-settled share-based payment transaction; • Guideliness on classification modification from cash-based to equity-settled payment transactions and also • Guideliness on employees tax liabilities recognition relating to share-based payment transactions. 	1 January 2018	The amendment will not have a significant impact on financial statements.
Improvements to IFRS 4: Applying IFRS 9 'Financial Instruments' with IFRS 4 'Insurance Contracts'	<p>Improvements to IFRS 4 'Insurance Contracts' address the issue of adopting a new standard, i.e. IFRS 9 'Financial Instruments'. Improvements to IFRS 4 supplement the existing options and are aimed to prevent temporary fluctuations in the insurance industry results arising from the implementation of IFRS 9.</p>	1 January 2018	The amendment will not have a significant impact on financial statements.
Improvements to IFRS 10 and IAS 28 *	<p>Improvements to IFRS 10 and IAS 28 cover sales or contributions of assets between an investor and its associate/joint venture. The improvements eliminate the inconsistencies between IFRS 10 and IAS 28. The accounting treatment hinges on whether the non-monetary assets sold or contributed to an associate/joint venture constitute a business. Should the assets constitute a business, the investor shall recognize the profit or loss in full. Should the assets not constitute a business, the profit or loss shall be recognised only to the extent of unrelated investors' interests in the associate or joint venture. The improvements were published on 11 September 2014.</p>	The International Accounting Standards Board has not established the validity date of the amended regulations.	The amendment will not have a significant impact on financial statements.
IFRS 17 Insurance Contracts *	<p>IFRS 17 replaces IFRS 4, which was brought in as an interim Standard in 2004. IFRS 4 has given companies dispensation to carry on accounting for insurance contracts using national accounting standards, resulting in a multitude of different approaches. As a consequence, it is difficult for investors to compare and contrast the financial performance of otherwise similar companies. IFRS 17 solves the comparison problems created by IFRS 4 by requiring all insurance contracts to be accounted for in a consistent manner, benefiting both investors and insurance companies. Insurance obligations will be accounted for using fair value – instead of historical cost.</p>	1 January 2021	The standard will not have a significant impact on financial statements.
IFRIC 23 Uncertainty over Income Tax Treatments *	<p>Interpretation clarifies how the recognition and measurement requirements of IAS 12 "Income taxes" are applied where there is uncertainty over income tax treatments. An uncertain tax treatment is any tax treatment applied where there is uncertainty over whether that treatment will be accepted by the tax authority. The impact of the uncertainty should be measured using the method that best predicts the resolution of the uncertainty - either the most likely amount method or the expected value method when measuring an uncertainty.</p>	1 January 2019	The amendment will not have a significant impact on financial statements.

*New standards and amendments to the existing standards issued by the IASB, but not yet authorized for use in the EU.

in thousands of PLN

IFRS 9 Financial Instruments

IFRS 9 Financial Instruments was published by the International Accounting Standards Board on 24 July 2014 and approved by virtue of the Commission Regulation (EU) 2016/2067 of 22 November 2016 for application in the EU member states. The standard applies to financial statements for annual reporting periods beginning on or after 1 January 2018, except for insurers which may apply the standard starting from 1 January 2021. IFRS 9 supersedes IAS 39 Financial Instruments: Recognition and Measurement. However, it allows reporting entities an option to continue to use the hedge accounting provisions stipulated in IAS 39.

IFRS 9 introduces changes that affect the following areas of financial instruments accounting:

- classification and measurement of financial instruments
- recognition and calculation of impairment and
- hedge accounting.

In mid 2016, Bank Zachodni WBK S.A. launched a project aimed at the implementation of IFRS 9. The project is delivered in liaison with an external consultant and involves Bank Zachodni WBK S.A. departments responsible for accounting policy, reporting, management information, taxes, impairment charges for financial instruments, IT systems and operations related to loan sanction and monitoring. The first stage of the project was completed in early 2017. The differences between IAS 39 and IFRS 9 were identified and an action plan was defined to ensure the compliance with the new standard. The second stage was launched in February 2017 and is aimed at implementing changes arising from IFRS 9. In particular, Bank Zachodni WBK S.A.'s objective was :

- development and implementation of models aimed to calculate impairment charges based on the expected credit loss (ECL) method. A particular focus was placed on defining a significant credit risk increase, rules for classifying financial instruments into stages and the impact of macroeconomic scenarios considered in individual risk parameters.
- development and implementation of models for determining fair value of financial instruments unquoted on the active market in the form of loans and debt financial instruments that must, due to the contractual cash flow test failure, be mandatory valued at fair value through profit or loss,
- to design and implement new processes related to the test of contractual cash flows, assessment of business model and modification of contractual cash flows,
- to develop and implement IT solutions,
- to modify the existing internal regulations (policies, terms of references, processes etc.).

Classification and measurement

The categories of financial instruments introduced by IAS 39, specifically held-to-maturity and available-for-sale financial instruments, no longer apply under IFRS 9. Pursuant to the new standard, the classification of financial assets depends on the business model of financial assets management and the nature of contractual cash flows. In accordance with the standard, financial instruments can be classified, on the basis of assessment of business models and the test of contractual cash flows, to the following groups only:

- financial assets measured at fair value through profit or loss,
- financial assets measured at fair value through other comprehensive income or
- financial assets measured at amortised cost.

Business models

The business model refers to how Bank Zachodni WBK S.A. manages its financial assets in order to generate cash flows. That is, the business model determines whether cash flows will result from collecting contractual cash flows, selling financial assets or both.

The business model assessment involves the analysis of qualitative and quantitative criteria.

Qualitative criteria are assessed by the key management personnel of Bank Zachodni WBK S.A. The following aspects are taken into account during the assessment:

- a) how the performance of the business model and the financial assets held within that business model are evaluated and reported to the key management personnel for the management accounting purposes.
- b) the risks that affect the performance of the business model (and the financial assets held within that business model) and, in particular, the way in which those risks are managed.
- c) the method of remunerating the persons who manage the financial instruments portfolio.

The purpose of the analysis of quantitative criteria of business model assessment is to determine if the sale of financial assets during the analysed period exceeds the pre-determined threshold values (in percentage terms) defined in internal regulations.

in thousands of PLN

In the analysis of the quantitative criteria of the business model assessment, Bank Zachodni WBK S.A. determines that a business model whose objective is to hold assets in order to collect contractual cash flows enables the sale of those assets, without affecting the current business model, in the following cases:

- if the sale is due to the increase in credit risk related to the assets
- if the sale is infrequent (even if its value is significant)
- if the value of the sale is insignificant (even if the sale is frequent)
- if the assets are sold to improve liquidity in a stress case scenario
- if the sale is required by third parties (it applies to the assets which have to be sold owing to e.g. the requirements of supervisory authorities, but were originally held to collect contractual cash flows)
- If the sale results from exceeding the concentration limits specified in internal procedures and is a part of the credit risk management policy
- if the sale is made close to the maturity date of the financial assets and the proceeds from the sale are an approximation of the contractual cash flows that the Bank Zachodni WBK S.A. would have collected if it had held the assets until their maturity date.

Other forms of the sale of assets as part of the business model whose objective is to hold assets in order to collect contractual cash flows (e.g. frequent sales of significant value) result in the need to change the business model, and reclassify the financial assets which were originally allocated to that model.

Bank Zachodni WBK S.A. has assessed the business models, and on the basis of the analysis determined the business model whose objective is to hold assets in order to collect contractual cash flows as the prevailing financial assets management model. This is with the exception of:

- Available-for-sale debt instruments which Bank Zachodni WBK S.A. holds for liquidity management purposes in a portfolio for which the business model whose objective is achieved by both collecting contractual cash flows and selling financial assets was determined as the appropriate business model;
- Held-for-trading instruments for which another (residual) business model was determined as the appropriate business model which reflects the method of their management.

Contractual cash flows test

In accordance with IFRS 9, only the contracts whose contractual cash flows include:

- the contractual principal (principal amount) and
- contractual interest

meet the requirements of the contractual cash flows test, and may be measured at:

- amortised cost, in the case of the assets classified to the business model whose purpose is to hold assets to collect contractual cash flows, or
- fair value through other comprehensive income with regard to the assets classified to the business model whose purpose is both to collect contractual cash flows and sell financial assets.

The assets which do not meet the contractual cash flows test must be measured at fair value through profit or loss regardless of the adopted business model.

Contractual principal is the fair value of the financial asset at initial recognition. However, that principal amount may change over the life of the financial asset (for example, if there are repayments of principal). In turn, interest includes a payment for:

- the time value of money;
- credit risk associated with the principal amount outstanding during a particular period of time;
- other basic lending risks and costs;
- as well as a profit margin.

For the purpose of this disclosure Bank Zachodni WBK S.A. takes into account the portfolio of financial assets, whose interest construction is based on a multiplier greater than one, at amortized cost.

Given the pending discussions regarding the classification and measurement of financial instruments whose interest rate structure is based on a multiplier higher than 1, the above approach may change and portfolio of credit cards offered to retail banking customers may have to be measured at fair value through profit or loss.

As part of analyses of the cash flows to which Bank Zachodni WBK S.A. is entitled under an agreement with the customer, a particular note was taken of the prepayment option and the impact of that option on the result of the contractual cash flows test.

in thousands of PLN

According to Bank Zachodni WBK S.A., the assessment of whether the prepayment option is in line with the contractual cash flows test criteria depends both on the nature of the circumstances which give one of the parties the right to make a prepayment, and on the prepayment amount. As a rule, these two factors are taken into account when assessing whether contractual cash flows include only repayment of principal and interest on the outstanding principal, which may also include reasonable additional compensation for the early termination of the contract.

A contractual term that permits the issuer (i.e. the debtor) to prepay a debt instrument or permits the holder (i.e. Bank Zachodni WBK S.A.) to put a debt instrument back to the issuer before maturity and the prepayment amount substantially represents unpaid amounts of principal and interest on the principal amount outstanding, which may include reasonable additional compensation for the early termination of the contract, is contractual cash flows which are only repayment of the principal amount and interest on the outstanding principal amount, and as such meet the SPPI test criteria.

Identified changes in classification and measurement

In order to ensure correct classification and measurement of the financial assets held as at 31 December 2017, Bank Zachodni WBK S.A. analysed its assets portfolios whereby it:

- determined and allocated financial assets to the business models which reflect the asset management method through how the portfolio results are reported to the key management personnel, an analysis of the risk types affecting the profitability and effectiveness of portfolios, the method of managing the risk related to the given portfolio and the method of remunerating portfolio managers;
- analysed the value, frequency and reasons for selling the assets in the years prior to implementation of IFRS 9;
- determined the expectations and plans of the key management personnel as to the method of managing the assets portfolio, including the value and frequency of financial asset sales;
- analysed the contractual terms relating to financial assets to determine if the contractual cash flows to which Bank Zachodni WBK S.A. is entitled represent payment of principal and interest.

Based on the results of the analyses performed by Bank Zachodni WBK S.A., supported by the outcome of tests of contractual cash flows and assessment of the business model, additional changes in the classification and measurement of financial assets concern the following:

– profit sharing agreements identified in certain tranches of debt instruments that have additional cash flows, other than solely payments of principal and interest, representing a contractually determined share in the customer's profit or loss. The adjustment to the fair-value measurement has been set at PLN -64.726 k, without the deferred tax effect.

– financial instruments whose contractual cash flows are not payments of principal and interest, which applies to debt instruments classified as "Loans and advances" whose interest is accrued on the subscription price and capitalised over the life of the product (until maturity) whereas interest payments to Bank Zachodni WBK S.A. will be calculated on the nominal price so these cash flows do not represent interest payments as defined in IFRS 9. The adjustment to the fair-value measurement has been set at PLN -15.897 k and unsettled provision amounted PLN -106 k without the deferred tax effect,

– a different recognition method for interest income from assets held, depending on the level of credit risk. Until the end of 2017, the interest income from exposures measured at amortised cost, for which IBNR impairment charge was calculated, was recognised at the net carrying amount, whereas from 1 January 2018 at the gross carrying amount of the exposure. IFRS 9 provides for two exceptions from this rule:

- a) POCI (Purchased or Originated Credit Impaired) assets. The interest income from these exposures is calculated on the net carrying amount based on the credit risk-adjusted effective interest rate.
- b) financial assets impaired after the initial recognition (stage 3) The interest income from these exposures is calculated based on the effective interest rate and the net carrying amount.

Considering the differences in the recognition of interest income from financial assets classified into stages 1 and 2, for which until end of 2017 the IBNR provision charge was calculated, on the effective date of IFRS 9, Bank Zachodni WBK S.A. recognised an interest income adjustment of PLN -28.305 k without deferred tax effect.

– non-listed equity instruments classified as available for sale, due to a significant limitation of the ability to measure such assets at historical cost less impairment charges, if any. By default, equity instruments are measured at fair value through profit or loss unless an irrevocable election is made at initial recognition to measure subsequent fair value changes at fair value through other comprehensive income.

Using the option permitted by IFRS 9, Bank Zachodni WBK S.A. took an irrevocable decision to designate strategic equity investments from the portfolio of financial assets other than those held for trading as instruments measured at fair value through other comprehensive income. The equity investments for which Bank Zachodni WBK S.A. chose the option of fair value measurement through other comprehensive income were acquired to be maintained in the investment portfolio for a long term and strategically, without the intention to make a profit on selling them in the short or medium term. If the equity instrument designated to

in thousands of PLN

be measured at fair value through other comprehensive income is sold, the gain (loss) on the transaction is not recycled to profit or loss at the time of the sale. The adjustment to the fair-value measurement of equity instruments has been set at PLN -17.702 k and amount of reversed impairment charges at PLN 1.984 k, without the deferred tax effect.

As at 31 December 2017, Bank Zachodni WBK S.A. has not identified any financial assets which it would intend to designate, as of 1 January 2018, to be measured at fair value through profit or loss to reduce the accounting mismatch, which would otherwise emerge as a result of measuring financial assets at amortised cost or at fair value through other comprehensive income.

Financial liabilities will continue to be measured in accordance with the existing rules laid down in IAS 39, i.e. at amortised cost or at fair value through profit or loss. Bank Zachodni WBK S.A. has not chosen the option of measuring financial liabilities at fair value. Should this option be chosen, changes in the fair value arising from changes in Bank Zachodni WBK S.A. credit risk will be taken to other comprehensive income, and once a financial liability is derecognised, the value previously recognised in other comprehensive income will not be recycled to profit or loss.

Comparative data

The use of IFRS 9 requires a change in presentation and the scope of disclosure, including in the first year after adoption, when a wide range of information is needed to allow financial statement users to understand the impact that the IFRS 9 might have in terms of classification, measurement and impairment of financial instruments on the financial position and the financial results of Bank Zachodni WBK S.A.

Bank Zachodni WBK S.A. elected to use the IFRS 9 provisions which provide for exemption of the obligation to restate comparative information for prior periods in relation to the changes arising from classification, measurement and impairment. Differences in the carrying amount of financial assets and liabilities resulting from the application of IFRS 9 are reported in retained earnings in equity as at 1 January 2018.

Hedge accounting

The standard expands the list of eligible hedged items and allows entities to designate as hedging instruments financial assets or liabilities measured at fair value through profit or loss. The retrospective effectiveness test and the 80-125% bright line are removed, and the prerequisite for applying hedge accounting is the existence of an economic relationship between the hedged item and the hedging instrument. Furthermore, the standard expands the scope of disclosures concerning risk management strategies, cash flows arising from hedging transactions and impact of hedge accounting on financial statements.

Pursuant to paragraph 7.2.21 of IFRS 9, Bank Zachodni WBK S.A. chose to continue to apply the hedge accounting requirements and hedging relationships arising from IAS 39.

For this reason, implementation of IFRS 9 will have no impact on the financial position of Bank Zachodni WBK S.A. with regard to hedge accounting.

Impairment of credit exposures

IFRS 9 introduced a new approach to estimating losses related to credit exposures measured at amortised cost. The new approach is based on expected credit loss instead of the incurred loss model that is currently used under IAS 39. In accordance with IFRS 9, the recognition of expected credit losses depends on changes in risk after recognition of the exposure.

IFRS 9 makes the method of recognizing expected losses dependent on the change in the level of risk that occurred since the exposure was recognized. The standard introduced three main stages for recognising expected credit losses:

- stage 1 – exposures with no significant increase in risk since initial recognition, i.e. the likelihood of the exposure being downgraded to the impaired portfolio (Stage 3 exposures) has not increased. For such exposures, 12-month expected credit losses is recognised.
- stage 2 – exposures with a significant increase in risk since initial recognition, but with no objective evidence of default. For such exposures, lifetime expected credit losses is recognised.
- stage 3 – exposures for which the risk of default has materialised. For such exposures, lifetime expected credit losses is recognised.

In addition, for exposures classified as POCI (purchased or originated credit impaired), expected losses are recognized over the remaining life time horizon.

One of the key aspects of implementation of IFRS 9 was to work out a definition of a significant increase in credit risk that determines the classification of an exposure into Stage 2. Bank Zachodni WBK S.A. developed the definition of detailed criteria for a significant increase in risk. Bank Zachodni WBK S.A. developed detailed criteria for the definition of a significant increase in the level of risk based on the following main assumptions:

in thousands of PLN

- qualitative:
 - customer coverage with dedicated monitoring strategies as a consequence of identifying early warning signals indicating a significant increase in credit risk,
 - restructuring measures related to providing clients with facilities forced by their difficult financial situation,
- quantitative:
 - the risk buffer method based on a comparison of the probability of insolvency curves in the horizon of the current remaining lifetime of exposures according to the risk level assessment at the moment of the exposure recognition and the reporting date,
 - delay in payment in accordance with the criteria of the standard, ie 30 days of delay in payment combined with materiality threshold consistent with the classification to stage 3.

Another key feature introduced by IFRS 9 is the approach to the estimation of risk parameters. For the purpose of estimating impairment losses, Bank Zachodni WBK S.A. continues using own estimates of risk parameters that are based on internal models, however with the necessary modifications in the context of IFRS 9 requirements (such as estimating the parameters over the life of the exposure or taking into account future macroeconomic conditions). Bank Zachodni WBK S.A. has defined a methodology for parameters modelling and has developed models compliant with IFRS 9.

Expected credit losses are the product of the individual for each exposure of estimated values of PD, LGD and EAD parameters, and the final value of expected losses is the sum of expected losses in individual periods (depending on the basket over a 12 month horizon or lifetime) discounted by the effective interest rate. The estimated parameters in accordance with the assumptions of IFRS 9 are subject to adjustment for macroeconomic scenarios. Bank Zachodni WBK S.A. uses internally developed scenarios.

The models and parameters created for the needs of IFRS 9 are subject to the process of model management and regular calibration and validation.

Bank Zachodni WBK S.A. has developed IT solutions for the purpose of implementation of a new method for calculation of impairment in the systems. The changes were implemented in production systems in January 2018.

The implementation of IFRS 9 requirements caused increase in impairment losses in Bank Zachodni WBK S.A.

The total value of additional impairment charges recognised in retained earnings for previous years is PLN 162.660 k, without the deferred tax effect, of which PLN 199.978 k relates to balance sheet items, PLN 24.489 k the increase in provisions for off-balance sheet liabilities presented in the line "Provisions" and the reclassifications of financial instruments from the category of assets measured at amortized cost to measured at fair value through profit or loss triggered impairment charge reversal in the amount of PLN 61.807 k.

In addition, Bank Zachodni WBK S.A. expects higher volatility of impairment charges due to changes in the classification of exposures between stage 1 and 2 and material changes in the coverage of the exposure resulting in write-offs due to different horizons for recognizing expected losses.

An important element affecting the volatility of estimates is also the use of macroeconomic forecasts in the calculation expected credit losses.

Impact of IFRS 9 on financial position

The table below presents the impact of IFRS 9 implementation on financial assets as at 1 January 2018:

Item	Measurement category – IAS 39	Measurement category – IFRS 9	Carrying amount – IAS 39	IFRS 9 implementation impact * Classification and measurement impact	IFRS 9 implementation Impairment impact	Carrying amount – IFRS 9
ASSETS						
Loans and advances to customers	Amortised cost	Amortised cost	90 412 680	(28 305)	(199 978)	90 184 397
Loans and advances to customers	Amortised cost	Fair value through profit or loss	124 323	(80 729)	61 807	105 401
Financial assets available for sale	Historic cost/purchase price less impairment charges	Fair value through OCI	48 146	(17 702)	1 984	32 428
Total assets			90 585 149	(126 736)	(136 187)	90 322 226

* without deferred tax effect

The value of other financial assets presented in the statement of financial position did not change significantly as a result of implementation of IFRS 9.

in thousands of PLN

The table below presents the impact of IFRS 9 implementation on liabilities as at 1 January 2018:

Item	Measurement category	Measurement category	Carrying amount	IFRS 9 implementation impact * Classification and measurement impact	IFRS 9 implementation Impairment impact	Carrying amount – IFRS 9
LIABILITIES						
Provisions	IAS 37	IFRS 9	25 384	-	24 489	49 873
Total liabilities			25 384	-	24 489	49 873

* without deferred tax effect

The value of other liabilities presented in the statement of financial position did not change as a result of implementation of IFRS 9.

As at 1 January 2018, the total value of the impact of IFRS 9 implementation PLN -287,412 k, and the deferred tax effect in the form of deferred net tax asset increase PLN 54,608 k decreased the balance of retained earnings and revaluation reserve by the amount of PLN -232,804 k.

However, as indicated in the section on classification and measurement of financial instruments, the impact of changes in the classification and measurement rules is presented for information only. As at the date of this report, there are different opinions as to the potential impact of a multiplier higher than 1 on the classification and measurement of financial assets other than held-for-trading instruments. For financial asset portfolios which include such a multiplier, the total impact might differ from the impact presented above.

Impact of IFRS 9 on capital adequacy

On 12 December 2017, the European Parliament and the Council adopted Regulation No 2017/2395 amending Regulation (EU) No 575/2013 as regards transitional arrangements for mitigating the impact of the introduction of IFRS 9 on own funds and for the large exposures treatment of certain public sector exposures denominated in the domestic currency of any Member State. This Regulation entered into force on the next day following its publication in the Official Journal of the European Union and has been applicable since 1 January 2018. The European Parliament and the Council concluded that the application of IFRS 9 may lead to a sudden significant increase in expected credit loss provisions and consequently to a sudden decrease in institutions' Common Equity Tier 1 capital.

The regulation regarding the mitigation of impact of IFRS 9 on Tier 1 capital provides for the following:

- Where an opening balance sheet on the day of first IFRS 9 application reflects a decrease in Common Equity Tier 1 capital as a result of increased expected credit loss provisions, including the loss allowance for lifetime expected credit losses for financial assets that are credit-impaired, compared to the closing balance sheet on the previous day, Bank Zachodni WBK S.A. should be allowed to include in its Common Equity Tier 1 capital a portion of the increased expected credit loss provisions for a transitional period. That transitional period should have a maximum duration of 5 years and should start in 2018. The portion of expected credit loss provisions that can be included in Common Equity Tier 1 capital should decrease over time down to zero to ensure the full implementation of IFRS 9 on the day immediately after the end of the transitional period.
- The multipliers that can be applied in consecutive years of the transitional period are as follows: 95%, 85%, 70%, 50%, 25%.
- If Bank Zachodni WBK S.A. decides to apply the IFRS 9 transitional arrangements, it should publicly disclose its own funds, capital ratios and leverage ratio both with and without the application of those arrangements in order to enable the recipients of financial statements to determine the impact of those arrangements.
- Bank Zachodni WBK S.A. should decide whether to apply those transitional arrangements and inform the KNF accordingly.
- During the transitional period, Bank Zachodni WBK S.A. may reverse once its initial decision, subject to the prior permission of the KNF, which should ensure that such decision is not motivated by considerations of regulatory arbitrage.
- Institutions that decide to apply transitional arrangements should be required to adjust the calculation of regulatory items which are directly affected by expected credit loss provisions to ensure that they do not receive inappropriate capital relief. For example, the specific credit risk adjustments by which the exposure value is reduced under the standardised approach for credit risk should be reduced by a factor which has the effect of increasing the exposure value. This would ensure that an institution would not benefit from both an increase in its Common Equity Tier 1 capital due to transitional arrangements as well as a reduced exposure value.

Having analysed Regulation No. 2017/2395, Bank Zachodni WBK S.A. has decided to apply the transitional arrangements provided for therein, which means that the full impact of the introduction of IFRS 9 will not be taken into account for the purpose of capital adequacy assessment of Bank Zachodni WBK S.A.

As a result of the adjustment of the regulatory capital requirements calculation, which include transitional arrangements for mitigating the impact of the introduction of IFRS 9 referred in the Regulation (EU) 2017/2395 of the European Parliament and of the Council of 12 December 2017, the Tier 1 capital ratio and total capital ratio on Bank Zachodni WBK S.A. level decreased by 2 bps. In the case

in thousands of PLN

of non-application of the transitional arrangements related to IFRS 9 specified in this regulation and taking into account the full impact of the implementation of IFRS 9, the above-mentioned ratios would decrease by 24 bps.

As presented above, as a result of IFRS 9 implementation, Tier 1 capital ratio and total capital ratio of Bank Zachodni WBK S.A. decreased mainly due to the introduction of a new impairment model based on expected credit loss of Stage 2 exposures.

Due to the decision to apply the transitional provisions as of February 1, 2018, Bank Zachodni WBK S.A. will disclose own funds, capital ratios, as well as the leverage ratio, both with and without the application of transitional solutions resulting from article 473a of Regulation (EU) No 575/2013 from the first quarter of 2018.

IFRS 15 Revenue from Contracts with Customers

Description of changes

IFRS 15 Revenue from Contracts with Customers was published on 28.05.2014 by the International Accounting Standards Board and applies to annual reporting periods beginning on or after 01.01.2018.

IFRS 15 introduced a new, 5-step model to be applied to revenue-generating contracts with customers, excluding the contracts which are covered by a separate standard. The standard was introduced to harmonise the rules used by enterprises and to eliminate inconsistencies with previous standards.

- As of 01.01.2018, IFRS 15 replaces the following standards and interpretations:
- IAS 18 Revenue
- IAS 11 Construction contracts
- SIC-31 Revenue - Barter Transactions Involving Advertising Services
- IFRIC 13 Customer Loyalty Programmes
- IFRIC 15 Agreements for the Construction of Real Estate
- IFRIC 18 Transfers of Assets from Customers.

The new standard is applied to almost all contracts with customers. The main exceptions include leases (IAS 17), financial instruments and other contractual rights or obligations (IFRS 9, IFRS 10, IFRS 11, IAS 27 and IAS 28), insurance contracts (IFRS 4) and guarantees covered by other standards.

The previous standards (IAS 11/IAS 18) distinguished three separate models for revenue recognition, depending on the type of the sale transaction:

- construction contract
- sale of goods
- sale of services.

IFRS 15, introduced a single, five-step revenue recognition model, replacing the previous three separate models of revenue recognition. The new model applies to all transactions, enterprises and industries. The model will be used in two versions, depending on how the entity satisfies a performance obligation:

- over time or
- at a point in time.

The core principle of IFRS 15 is that an entity will recognise revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which Bank Zachodni WBK S.A. expects to be entitled in exchange for those goods or services.

The key criterion for the recognition of revenue is no longer the moment of transferring the "risks and rewards", which was considered as key under IAS 18, but the moment of satisfaction of a performance obligation, which takes place as control is passed. This determines the recognition of a revenue under IFRS 15. However, the expectation is that the moment will more often than not coincide with the moment of transfer of risks and rewards within the meaning of IAS 18.

Furthermore, in line with IFRS 15, costs incurred to obtain and secure a contract with a customer should be capitalised and amortised over time for as long as the benefits from the contract are consumed.

Each of those five steps of the revenue recognition model are described below:

Step 1: Identify the contract with the customer The first step is to identify the contract with the customer. IFRS 15 defines a contract as an agreement between two or more parties that creates enforceable rights and obligations. However, not all contracts are covered by IFRS 15. Bank Zachodni WBK S.A. recognises a contract with a customer within the scope of IFRS 15 if all the following conditions are met:

- the contract has been approved in writing, orally, or in accordance with other customary business practices and the parties are committed to perform their obligations in the contract,
- Bank Zachodni WBK S.A. can identify each party's rights regarding the assets to be transferred,

in thousands of PLN

- Bank Zachodni WBK S.A. can identify payment terms for the assets to be transferred,
- the contract has commercial substance (i.e. the risk, timing or amount of the vendor's future cash flows to Bank Zachodni WBK S.A. are expected to change as a result of the contract),
- it is probable that Bank Zachodni WBK S.A. will collect the consideration to which it will be entitled in exchange for the assets that will be transferred to the customer. In evaluating whether collectability of an amount of consideration is probable, Bank Zachodni WBK S.A. shall consider only the customer's ability and intention to pay that amount of consideration when it is due.

In the identification process, Bank Zachodni WBK S.A. takes into account both combination and modification of contracts as this may affect the method of recognising revenue from contracts with customers.

Bank Zachodni WBK S.A. combines two or more contracts entered into at or near the same time with the same customer (or related parties of the customer), and accounts for the contracts as a single contract if one or more of the following criteria are met:

- the contracts are negotiated as a package with a single commercial objective;
- the amount of consideration to be paid in one contract depends on the price or performance of the other contract or
- the assets promised in the contracts (or some assets promised in each of the contracts) are a single performance obligation.

Pursuant to the new accounting policy of Bank Zachodni WBK S.A., a contract modification is a change in the scope or price (or both) of a contract that is approved by the parties to the contract. A contract modification exists when the parties to a contract approve a modification that either creates new or changes existing enforceable rights and obligations of the parties to the contract. A contract modification could be approved in writing, by oral agreement or implied by customary business practices. If the parties to the contract have not approved a contract modification, Bank Zachodni WBK S.A. continues to apply IFRS 15 to the existing contract until the contract modification is approved.

A contract modification may exist even though the parties to the contract have a dispute about the scope or price (or both) of the modification or the parties have approved a change in the scope of the contract but have not yet determined the corresponding change in price. In determining whether the rights and obligations that are created or changed by a modification are enforceable, Bank Zachodni WBK S.A. considers all relevant facts and circumstances including the terms of the contract and other evidence. If the parties to a contract have approved a change in the scope of the contract but have not yet determined the corresponding change in price, Bank Zachodni WBK S.A. estimates the change to the transaction price arising from the modification in relation to the estimation of variable consideration and constraining estimates of variable consideration.

Step 2: Identify the performance obligations in the contract. The next step in the process of recognising revenue is to identify performance obligations (assets) under the contract which are distinct. An asset is distinct if the customer can benefit from the asset either on its own or together with other resources that are readily available to the customer, and at the same time an asset is separately identifiable from other promises in the contract. In such a case, Bank Zachodni WBK S.A. is dealing with separate performance obligations.

Factors that indicate that Bank Zachodni WBK S.A. promise to transfer an asset to a customer is separately identifiable include, but are not limited to, the following:

- Bank Zachodni WBK S.A. does not provide a significant service of integrating the asset with other assets promised in the contract into a bundle of assets that represent the combined output for which the customer has contracted.
- the asset does not significantly modify or customise another assets promised in the contract,
- the asset is not highly dependent on, or highly interrelated with, other assets promised in the contract.

If a promised asset is not distinct, Bank Zachodni WBK S.A. combines that asset with other promised assets until it identifies a bundle of assets that is distinct. In some cases, that would result in Bank Zachodni WBK S.A. accounting for all the assets promised in a contract as a single performance obligation.

Step 3: Determine the transaction price. In accordance with IFRS 15, the transaction price is the amount of consideration that Bank Zachodni WBK S.A. expects to be entitled to in exchange for assets promised. It represents the amount of the revenue that will be recognised as a result of performance of the contract. In addition to the amount of consideration, the transaction price should also reflect any highly probably variable consideration (including bonuses or penalties), a discounting factor, amounts paid to customers or non-cash consideration. As the transaction price may be based to a large degree on estimates, Bank Zachodni WBK S.A. reviews it as at each balance sheet date.

If the consideration promised in a contract includes a variable amount, Bank Zachodni WBK S.A. estimates the amount of consideration to which it will be entitled in exchange for transferring the promised assets to a customer. An amount of consideration can vary because of discounts, rebates, refunds, credits, price concessions, incentives, performance bonuses, penalties or other similar items.

in thousands of PLN

Step 4: Allocate the transaction price to the performance obligations. As individual performance obligations may be recognised at different times and in different ways (at a point in time or over time), in the case of multiple performance obligations in a contract, the transaction price needs to be allocated to identified performance obligations. The allocation should be based on the stand-alone selling price, which is the price at which a vendor would sell an asset separately in similar circumstances and to similar customers. If the transaction price changes during the contract, the re-allocation is based on the original stand-alone selling prices.

Step 5: Recognise revenue when each performance obligation is satisfied. Revenue is recognised when assets are transferred to a customer and the customer acquires control over the subject matter of the contract. IFRS 15 specifies the conditions under which a control is said to be transferred to the customer. Control may be transferred at a point in time or over time, which is determined on the basis of the criteria set out in the standard. Control is the ability to direct the use of, and obtain substantially all of the remaining benefits from an asset. This is a wider concept than the previously used moment of transfer of significant risks and rewards. Indicators that control has passed include that the customer has, for example: physical possession of the asset, legal title of the asset, or has accepted the effect of the performance obligation.

According to Bank Zachodni WBK S.A., the indicators of the transfer of control include the following:

- Bank Zachodni WBK S.A. has a present right to payment for the asset – if a customer is presently obliged to pay for an asset, then that may indicate that the customer has obtained the ability to direct the use of, and obtain substantially all of the remaining benefits from, the asset in exchange.
- The customer has legal title to the asset – legal title may indicate which party to a contract has the ability to direct the use of, and obtain substantially all of the remaining benefits from, an asset or to restrict the access of other entities to those benefits. Therefore, the transfer of legal title of an asset may indicate that the customer has obtained control of the asset. If Bank Zachodni WBK S.A. retains legal title solely as protection against the customer's failure to pay, those rights of Bank Zachodni WBK S.A. do not preclude the customer from obtaining control of an asset.
- Bank Zachodni WBK S.A. has transferred physical possession of the asset – the customer's physical possession of an asset may indicate that the customer has the ability to direct the use of, and obtain substantially all of the remaining benefits from, the asset or to restrict the access of other entities to those benefits. However, physical possession may not coincide with control of an asset. For example, in some repurchase agreements a customer may have physical possession of an asset that Bank Zachodni WBK S.A. controls.
- The customer has the significant risks and rewards of ownership of the asset – the transfer of the significant risks and rewards of ownership of an asset to the customer may indicate that the customer has obtained the ability to direct the use of, and obtain substantially all of the remaining benefits from, the asset. However, when evaluating the risks and rewards of ownership of a promised asset, Bank Zachodni WBK S.A. excludes any risks that give rise to a separate performance obligation in addition to the performance obligation to transfer the asset.
- The customer has accepted the asset – the customer's acceptance of an asset may indicate that it has obtained the ability to direct the use of, and obtain substantially all of the remaining benefits from, the asset.

Control may be transferred at a point in time or over time. The following criteria are used to determine when control is transferred and how income should be recognised:

- The customer receives the benefits as the contract is performed; if the service was discontinued, another service provider would not need to re-perform the work that the entity has completed to date if that other entity were to fulfil the remaining performance obligation to the customer already done;
- Bank Zachodni WBK S.A. creates or enhances an asset that the customer controls as it is created or enhanced;
- Bank Zachodni WBK S.A. does not create an asset with an alternative use and has a right to payment for performance completed to date.

If any of the above criteria is satisfied, income should be recognised over time. In other cases, income should be recognised when control is transferred.

Bank Zachodni WBK S.A. applies IFRS 15 starting from 1.01.2018.

Status

In Q2 2017, Bank Zachodni WBK S.A. launched a project aimed at analysing the impact of implementing a five-step model of revenue recognition. As a result of the analysis, a report was prepared by Bank Zachodni WBK S.A. experts, indicating the types of revenue which, in principle, should be accounted for in accordance with IFRS 15:

- revenue from advisory services
- revenue from the sale of fixed assets used for operational activities or repossessed, which together with the cost of assets sold are presented as the result on sale in line "Other operating income",
- loyalty programmes,
- success fee - i.e. contracts which do not guarantee the remuneration for Bank Zachodni WBK S.A. or provide for the minimum level of remuneration during the term of the contract until a certain condition is met (e.g. a transaction is finalised), entitling Bank Zachodni WBK S.A. to receive significant remuneration to compensate for the effort made by Bank Zachodni WBK S.A. in a long term.

in thousands of PLN

- revenue from asset management
- revenue from the sale of insurance products which show indications of a connection with financial instruments to an extent not covered by separate standards, and
- costs of contracts with customers.

In order to analyse the impact of the introduction of IFRS 15, Bank Zachodni WBK S.A. applied the portfolio practical expedient for the purpose of analysis of contracts with customers, as described in paragraph (4) of IFRS 15. Bank Zachodni WBK S.A. reasonably expects that the effects on the financial statements of applying this standard to the portfolio would not differ materially from applying this standard to the individual contracts (or performance obligations) within that portfolio. Bank Zachodni WBK S.A. applied the portfolio approach to the majority of income categories indicated above.

Bank Zachodni WBK S.A. , in cooperation with an independent external advisor, did not identify any significant categories of revenue and costs whose recognition would need to be changed due to the implementation of IFRS 15.

Impact of IFRS 15 on the financial standing and own funds

Impact of IFRS 15 implementation is not significant because revenue derived from financial instruments offered by Bank Zachodni WBK S.A. such as loans or leases is recognised using an effective interest rate and the recognition and accounting method for revenue that is in the scope of IFRS 15 and corresponding costs, due to the applicable contractual provisions, will not be modified.

IFRS 16 Leases

Description of changes

IFRS 16 Leases was published by the International Accounting Standards Board on 13 January 2016 and approved by virtue of the Commission Regulation (EU) 2017/1986 of 31 October 2017 for application in the EU member states. The standard applies to financial statements for annual reporting periods beginning on or after 1 January 2019.

As of 1 January 2019, IFRS 16 replaces the following standards and interpretations:

- IAS 17 Leases
- IFRIC 4 Determining whether an Arrangement Contains a Lease
- SIC-15 Operating Leases - Incentives
- SIC-27 Evaluating the Substance of Transactions Involving the Legal Form of a Lease.

The new standard applies to all leases, including leases of right-of use assets in a sublease, except for leases which are subject of other standards:

- Leases to explore for or use minerals, oil, natural gas and similar non-regenerative resources;
- Arrangements within the scope of IFRIC 12 Service Concession Arrangements;
- For lessors: licences of intellectual property granted by a lessor within the scope of IFRS 15 Revenue from Contracts with Customers; and
- For lessees: leases of biological assets within the scope of IAS 41 Agriculture and rights held under licensing agreements within the scope of IAS 38 Intangible Assets for such items as motion picture films, video recordings, plays, manuscripts, patents and copyrights.

The new standard presents the overall model for identification and accounting for leases in financial statements of lessors and lessees. Significant changes have been introduced to lessee accounting, e.g. the distinction between operating and finance lease is no longer applied.

For the purpose of identification of leases, IFRS 16 introduces a control model which differentiates between leases and service agreements depending on the existence of an asset controlled by the lessee.

In accordance with IFRS 16, a contract is, or contains, a lease if it conveys the right to control the use of an identified asset, and to obtain economic benefits from that use, for a period of time in exchange for consideration.

Under IFRS 16, a contract may be considered a lease if it meets the following criteria:

- fulfilment of the lease conditions relates to a specified asset which is identified by being explicitly or implicitly specified in a contract, and the lessor may not have a substantive right of substitution;
- the contract conveys the right to control the use of the asset in exchange for consideration. It means that the lessee has the right to direct the use of the asset and to obtain substantially all the economic benefits from that use, taking into account the scope of such use.

A specified asset may be identified either directly or indirectly. A portion of an asset which can be physically separated meets the identification criterion, and a portion of an asset that cannot be physically separated may not be treated as a specified asset and may not be the subject of a lease under IFRS 16.

in thousands of PLN

The contracts which give the lessor the substantive right to substitute the asset which is the subject of the lease may not be treated as leases as fulfilment of the contract conditions does not depend on the use of a specified asset. A lessor's right to substitute an asset is substantive only if the lessor has the practical ability to substitute alternative assets, the lessor would benefit economically from the exercise of its right to substitute the asset, and the substitution may take place without the lessee's consent. The contracts which give lessees the substantive right to substitute the asset do not meet the criteria of IFRS 16 and will continue to be recognised in accordance with IFRS 15.

The right to control the use of a specified asset is conveyed if the lessee has the ability both to direct the use of the asset and obtain benefits from its use. The contracts whereby the lessee obtains substantially all of the economic benefits from use of the asset, but does not have the ability to direct its use, are not treated as leases. A lessee has the right to direct the use of the asset if they can take decisions about how and for what purpose the asset is used, and the decisions materially affect the economic benefits to be derived from use.

The overall rule at inception of a lease the lessee will recognise a lease liability (obligation to make lease payments) and the asset which is the right to use the leased asset throughout the term of the lease (period of use) for all leases. At the same time, reporting entities have the right to use two simplifications for short-term leases and leases for which the underlying asset is of low value described below:

- IFRS 16 allows lessee to use the existing methods of accounting for operating leases to account for short-term leases. A short-term lease has a lease term of 12 months or less, including a renewal option. Whether or not a lease is a short-term lease is determined solely on the basis of the maximum lease term, which is the term in which exercisable rights and obligations arise. The above simplification is not available to the lessee in the case of short-term lease with an option to purchase the leased asset regardless of the lessor's intentions or expectations regarding the subject of the lease.
- To determine whether the leased asset is of low value, the Bank Zachodni WBK S.A. assesses the value of the asset when it is new, regardless of the actual age or wear and tear of the asset being leased. Even though the amount to be considered low was not indicated in the text of the standard, lessees may rely on the amount of USD 5,000 specified in the justification to the standard.

The lease liability is valued on the basis of the present value of lease payment during the term of the lease. The payments reflected in the valuation of lease liabilities include:

- fixed payments less any incentives paid or payable to the lessee;
- any other variable payments that depend on an index or a rate;
- amounts expected to be payable by the lessee under residual value guarantees;
- the price of exercising the payment option, if it is reasonably certain that the lessee will use that option;
- payments of penalties for terminating the lease, if the lease term reflects the lessee exercising an option to terminate the lease.

In turn, the right-to-use asset should reflect:

- the amount of the initial measurement of the lease liability;
- any lease payments made at or before the commencement date, less any lease incentives received;
- any initial direct costs incurred by the lessee; and
- an estimate of costs to be incurred by the lessee in dismantling and removing the underlying asset, restoring the site on which it is located or restoring the underlying asset to the condition required by the terms and conditions of the lease.

The discount rate should be set separately for each lease. For a lessee, the discount rate for the lease is the interest rate implicit in the lease and, if that rate is not known, its incremental borrowing rate.

IFRS 16 approach to lessor accounting is not substantially changed. Lessors continue to classify leases as operating or finance and recognise them as two different types of lease.

Status

Bank Zachodni WBK S.A. launched the work on the implementation of the new standard in the second half of 2017. The process is actively supported by the units specialised in reporting, taxes, accounting policy, IT as well as operational units which enter into lease or rental agreements.

First, Bank Zachodni WBK S.A. focused on identification of all leases and agreements with a lease component as well as assets used by the Bank under such arrangements. So far, agreements have been identified that provide for the lease of the following assets:

- buildings and commercial units
- land and perpetual usufruct of land
- vehicles and
- technical equipment.

Bank Zachodni WBK S.A. plans to apply two exemptions regarding:

in thousands of PLN

- short-term leases (whose term is 12 months or less and which do not contain purchase option) and
- low-value assets (assets with the initial value of PLN 17,000 or less) by taking them directly to costs, usually on a straight-line basis, over the lease term.

For the purpose of first-time adoption of the standard, Bank Zachodni WBK S.A. plans to use a modified retrospective approach and measure a right-of-use asset at the amount of the lease liability adjusted for any prepayments or accrued lease payments relating to that lease only, recognised in the statement of financial position directly before the first-time adoption, and avoid the obligation to restate comparative data.

In addition, at the date of first adoption of the standard, Bank Zachodni WBK S.A. plans to use additional simplifications available for first-time adopters, specifically:

- grandfather assessments regarding whether a contract existing at the date of initial application contains a lease;
- classify as short-term contracts the leases whose term ends 12 months after the first adoption;
- exclude any initial direct costs from measurement of the right-of-use asset;
- apply a single discount rate to the portfolio of leases with substantially similar characteristics (such as leases with a similar remaining lease term for a similar class of the underlying asset in a similar economic environment);
- adopt the requirements of the standard to the portfolio of leases with similar characteristics if Bank Zachodni WBK S.A. reasonably expects that the impact on the financial statements resulting from application of the standard to the portfolio will not be substantially different from the impact of application of the standard to individual leases as part of that portfolio. When measuring the portfolio, Bank Zachodni WBK S.A. uses the estimates and assumptions which reflect the value and composition of the portfolio;
- determining the provisions for onerous leases as an alternative to performing an impairment review. The use of this expedient will entail an adjustment of the right-of-use asset at the date of initial application by the amount of any provision for onerous leases recognised in the statement of financial position immediately before the date of initial application.

Estimated impact of IFRS 16 on Bank Zachodni WBK S.A.

Bank Zachodni WBK S.A. expects that the application of the new standard will affect the recognition, presentation, measurement and disclosure of assets under operating lease and their corresponding liabilities in financial statements of Bank Zachodni WBK S.A. as a lessee. The implementation of the new standard is not expected to have significant impact on recognition of finance lease in financial statements.

The value of lease payments by their maturity dates as at 31 December 2017 is presented in Note 44.

2.3. Standards and interpretations or changes to existing standards or interpretations which were applied for the first time in 2017

IFRS	Nature of changes	Effective from	Influence on Bank Zachodni WBK S.A.
Amendments to IAS 7 Statement of Cash Flows	Amendments to IAS 7 introduce the requirements to disclose changes in liabilities arising from financing activities in statement of cash flows, including both changes arising from cash flows and non-cash changes. To fulfill the requirement the standard requires a reconciliation between the opening and closing balances in the statement of financial position for liabilities arising from financing activities in cash flow statement.	1 January 2017	Reconciliation of changes in liabilities arising from financing activities are presented in notes 30-33.
Amendment to IAS 12 Income Taxes	Amendments to IAS 12 clarify the requirements on recognition of deferred tax assets for unrealized losses on debt instruments measured at fair value. The amendments introduce the guidance on the identification of deductible temporary differences. Especially the standard confirms that decreases below cost in the carrying amount of a fixed-rate debt instrument measured at fair value for which the tax base remains at cost give rise to a deductible temporary difference. This applies irrespective of whether the debt instrument's holder expects to use it or sale it.	1 January 2017	The amendments does not have any material impact on the financial statements.
Annual Improvements to IFRS 2014-2016 *	In December 2016, the International Accounting Standards Board published 'Annual Improvements to IFRS Standards 2014-2016 Cycle' which amended 3 standards, i.e. IFRS 12 'Disclosure of Interests in Other Entities', IFRS 1 'First-time Adoption of International Financial Reporting Standards' and IAS 28 'Investments in Associates'. The improvements feature guidelines and amendments re: the scope of applicability, recognition and valuation as well as terminology and editing changes.	1 January 2017 for improvements to IFRS 12	The amendment did not have a significant impact on financial statements.

*New standards and amendments to the existing standards issued by the IASB, but not yet authorized for use in the EU.

2.4. Basis of preparation

The financial statements are presented in PLN, rounded to the nearest thousand.

in thousands of PLN

The financial statement of Bank Zachodni WBK S.A. has been prepared in accordance with the International Financial Reporting Standards (IFRS) adopted in the European Union, on a historical cost basis, taking into account measurement basis used for available-for-sale financial assets, financial assets and liabilities at fair value through profit and loss and all derivative contracts and liabilities for cash-settled share-based payment transactions, which are measured at fair value. Fixed assets available for sale and disposal groups of fixed assets designated as available for sale are recognised at the lower of their carrying amount and their fair value less costs of disposal.

2.5. Use of estimates and judgments

The preparation of financial statements in conformity with IFRSs requires the management to make judgments, estimates and assumptions that affect the application of accounting policies and reported amounts of assets and liabilities, income and expenses.

The estimates and assumptions are based on historical experience and various other factors that are believed to be reasonable under the given circumstances, the results of which form the basis of making the judgments about carrying values of assets and liabilities that are not readily apparent from other sources.

The estimates and assumptions are reviewed on an ongoing basis. Changes to estimates are recognised in the period in which the estimate is changed if the change affects only that period, or in the period of the change and future periods if the change affects both current and future periods.

2.6. Main estimates and judgments made by Bank Zachodni WBK S.A.

Loan impairment

The estimation of potential loan impairment charges is inherently uncertain and depends upon many factors in respect of credit risk, including loans' impairment charges trends, portfolio grade profiles, economic climates, conditions in various industries to which Bank Zachodni WBK S.A. is exposed and other external factors such as legal and regulatory requirements. Impairment charges are posted for loans with indications of impairment if in the management's opinion the estimated recovery from the debtor, including value of the existing collateral, may be lower than the outstanding exposure.

For all the impaired credit exposures, Bank Zachodni WBK S.A. calculates an impairment charge as a difference between the credit exposure's book value and the present value of the estimated future cash flows, discounted using the effective interest rate as at the date of recognition of impairment

The identification of exposures that require impairment charges to be posted is based on several independent review levels. Credit quality and loan impairment charges are independently monitored by head office personnel on a regular basis. Bank Zachodni WBK S.A. uses a consistent system for grading advances according to agreed credit criteria with an important objective being the timely identification of vulnerable loans so that remedial action can be taken at the earliest opportunity. The credit grading system plays a key role in the calculation of impairment charges in Bank Zachodni WBK S.A.; this is the starting point of a process that ends in an impairment charge being posted against the individual exposures that are at the risk of default.

The analysis of impairment is carried out:

- with reference to individual credit exposures representing significant reporting items, for which indications of impairment have been identified for customers classified to Global Corporate Banking segment, customers with a commercial grading, property customers and local authorities, and for significant retail exposures (individual analysis);
- with reference to the portfolio of individually insignificant credit exposures (collective analysis) or individually significant exposures, but with no identified indications of impairment.

Bank Zachodni WBK S.A. regularly reviews the methodologies and assumptions underpinning estimation of cash flows and periods of time in which they occur; in particular Bank Zachodni WBK S.A. compares estimated and actual cash flows to arrive at the best estimate of the recoverable amount.

Net impairment losses on loans and advances are presented in Note 11.

For other receivables impairment charge is recognised considering the expected recoverable amounts, and for long term other receivables discounting is applied.

Impairment loss on non-financial assets

The valuation of fixed assets is reviewed at the end of the reporting period to specify whether there are indicators for write-down due to impairment. If there are such indicators, the recoverable value of assets should be determined.

Impairment charge is recognised if the book value of an asset exceeds its recoverable value and is presented in the income statement.

Fixed assets available for sale and disposals groups of fixed assets designated as available for sale are recognised at the lower of their carrying amount and their fair value less costs of disposal.

in thousands of PLN

The value of impairment losses on individual tangible and intangible fixed assets is presented in Notes 24 and 26.

Fair value of financial instruments

Some financial instruments are carried at fair value, including all derivatives, other financial assets measured at fair value through profit and loss and financial instruments classified as available for sale. Financial instruments are either marked-to-market or priced by using a valuation model. Where the fair value is calculated using financial-markets pricing models, the methodology is to calculate the expected cash flows under the terms of each specific contract and then discount these values back to a present value. These models use as their basis independently sourced market parameters including, for example, interest rate yield curves, securities and commodities prices, option volatilities and currency rates. Most market parameters are either directly observable or are implied from instrument prices.

In justified cases, for financial instruments whose carrying amount is based on current prices or valuation models, Bank Zachodni WBK S.A. takes into account the need to identify additional adjustments to the fair value of the counterparty credit risk.

A summary of the carrying amounts and fair values of the individual groups of assets and liabilities is presented in Note 41.

Revenues arising from insurance mediation

Bank Zachodni WBK S.A. periodically performs the link assessment between financial instruments and insurance products distributed with them, using a questionnaire prepared in accordance with KNF Recommendation U.

Bank Zachodni WBK S.A. performs the link assessment:

- in relation to new insurance products,
- at each change of terms of the existing insurance products and
- at least once a year, in the third quarter, taking into account the updated data about the product portfolio and the market data.

In 2017, Bank Zachodni WBK S.A. has changed estimation of the parameters of the relative-fair-value model which is applied by Bank Zachodni WBK S.A. to allocate the amount of intermediation remuneration services arising from insurance sale offered in conjunction with a financial instrument. Based on the parameters review, the following elements have been changed: a portion of remuneration arising from the offered financial instrument, remuneration for insurance mediation services and remuneration for additional activities carried out during the term of the insurance contract.

The change in relative-fair-value parameters were applied prospectively.

Classification of leases

Bank Zachodni WBK S.A. uses judgement to classify leases as finance or operating leases, on the basis of an analysis of the economic substance of the transaction based on an assessment of whether or not all the risks and rewards of ownership of the leased asset have been transferred.

A lease is classified as a finance lease if it transfers substantially all the risks and rewards of ownership of the leased asset. A lease is classified as an operating lease if it does not transfer substantially all the risks and rewards of ownership of the leased asset.

Note 44 presents gross receivables in respect of finance leases by maturity dates, present value of due minimum lease payments by maturity dates, reconciliation of differences between finance lease receivables and the present value of due minimum lease payments, and operating lease payments by maturity dates.

Economic life of intangible and tangible fixed assets

At initial recognition of an intangible or tangible fixed asset, Bank Zachodni WBK S.A. determines their estimated economic life.

For the purpose of this process, Bank Zachodni WBK S.A. takes into account in particular:

- objective criteria – beyond the control of Bank Zachodni WBK S.A., and arising from the very characteristics of the asset or from other conditions, mainly external ones, which are key to its potential economic life;
- criteria connected with the specific nature of activities of Bank Zachodni WBK S.A., which may cause extension or reduction of the economic life of an asset (e.g. intensity of use, including the number of changes being processed, capacity measured by the number of working hours, operating conditions, frequency and economic rationale for repairs).

Economic life of fixed assets is periodically reviewed by Bank Zachodni WBK S.A.

in thousands of PLN

Other accounting estimates and judgments

Provisions for employee benefits paid on termination of employment, i.e. post-employment benefits, are estimated on the basis of an actuarial valuation. The actuarial valuation of those accruals is updated at least on an annual basis.

See Note 48 for details about provisions for staff benefits.

The fair value of awards granted under an incentive scheme is determined using the share based payments pricing models, which take into account the exercise price of the award, the share price at date of grant, discount rate - the risk free rate, the expected volatility of the share price over the life of the award and other relevant factors influencing fair value. Bank Zachodni WBK S.A. assesses probability of the programme vesting which affects the programme value in the costs of the reporting period. Description of the share-based incentive scheme is contained in Note 49.

Provisions for legal claims have been estimated considering the expected loss arising on individual cases. Provisions for cases disputed in court are presented in Note 34.

Changes in judgments and estimates

In 2017, the scope of data covered by estimates did not change in comparison with the unconsolidated financial statements of Bank Zachodni WBK S.A. for 2016 with the exception of those listed above.

2.7. Accounting policies

The accounting policies set out below have been applied consistently to all periods presented in the financial statements.

Changes in accounting policies

Except the new standards, changes to existing standards and the interpretations described in Section 2.3, Bank Zachodni WBK S.A. has applied the same accounting principles as to the consolidated financial statements for 2016.

Comparability with results of previous periods

No major changes were introduced in respect of presentation of financial data for comparative periods of time.

Foreign currency

Foreign currency transactions

The functional and presentation currency of Bank Zachodni WBK S.A. are the Polish zloty (PLN).

Transactions in foreign currencies are translated at the foreign exchange rate applicable at the date of the transaction. Resulting from these transactions monetary assets and liabilities denominated in foreign currencies, are translated at the foreign exchange rate applicable at the end of the reporting period. Non-monetary assets and liabilities denominated in foreign currencies, which are stated at historical cost, are translated at the foreign exchange rate applicable at the date of the transaction. Non-monetary assets and liabilities denominated in foreign currencies that are stated at fair value are translated to the reporting currency at the foreign exchange rates ruling at the dates that the fair values were determined. Foreign exchange differences arising on translation are recognised in profit or loss except for differences arising on retranslation of available for sale equity instruments of other entities, which are recognised in other comprehensive income.

Financial assets and financial liabilities

Classification

Bank Zachodni WBK S.A. classifies its financial instruments into the following categories:

- financial assets or financial liabilities measured at fair value through profit or loss;
- held-to-maturity investments;
- loans and receivables;
- available-for-sale financial assets;
- other financial liabilities.

Financial asset or financial liability measured at fair value through profit and loss

This is a financial asset or liability that meets either of the following conditions.

- a) Classified as held for trading.

A financial asset or financial liability is classified as held for trading if:

in thousands of PLN

- i. it is acquired or incurred principally for the purpose of selling or repurchasing in the near term;
 - ii. it is part of a portfolio of identified financial instruments that are managed together and for which there is evidence of a recent actual pattern of short-term profit taking;
 - iii. derivatives are held for trading unless the derivative is a designated and effective hedging instrument.
- b) Upon initial recognition it is designated by Bank Zachodni WBK S.A. at fair value through profit and loss. As at the current balance sheet date and in previous financial year Bank Zachodni WBK S.A. did not hold this category of financial instrument.

Held-to-maturity investments

These are non-derivative financial assets with fixed or determinable payments and fixed maturity that Bank's Zachodni WBK S.A. management has the positive intention and ability to hold to maturity. If Bank Zachodni WBK S.A. were to sell or reclassify more than an insignificant amount of held to maturity investments before maturity, the entire category would be reclassified as available for sale and for a two year period Bank Zachodni WBK S.A. would not classify financial assets as held to maturity. As at the current balance sheet date and in previous financial year Bank Zachodni WBK S.A. did not hold this category of financial instrument.

Loans and receivables

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market, other than:

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

Loans and receivables comprise loans and advances to banks and customers including purchased receivables and investments in debt instruments provided that they are not quoted in an active market and receivables due to reverse repo transactions.

Available-for-sale financial assets

Available-for-sale financial assets are those non-derivative financial assets that are designated as available for sale or are not classified as:

- a) loans and receivables;
- b) held-to-maturity investments;
- c) financial assets measured at fair value through profit and loss.

Other financial liabilities

Financial liabilities include financial liabilities not classified as those measured at fair value through income statement. Those liabilities are valued at amortised cost and comprise: deposits from banks, deposits from customers, liabilities due to reverse repo transactions, received credits and loans, debt securities in issue and subordinated liabilities.

Subordinated liabilities are recognised as liabilities which in the event of resolution of Bank Zachodni WBK S.A. are repaid after satisfaction of claims of other Bank Zachodni WBK S.A. creditors. Financial liabilities are classified as subordinated liabilities by the decision of the Polish Financial Supervision Authority issued at the request of Bank Zachodni WBK S.A.

Recognition

Bank Zachodni WBK S.A. recognises a financial asset or a financial liability in its statement of financial position when, and only when, the entity becomes a party to the contractual provision of the instrument.

A regular way purchase of a financial asset is recognised in the statement of financial position as at the transaction settlement date. For assets that are carried at fair value, changes in fair value between the trade date and the settlement date are recognised in profit or loss or in revaluation reserve. This method is applied consistently for all purchases and sales of financial assets. Loans are recognised in the statement of financial position when cash is advanced to the borrowers. At the time of signing the loan agreement, the loans are recognised as contingent commitments.

Derecognition

Financial assets are derecognised from the statement of financial position when the contractual rights to the cash flows from the financial assets expire or when Bank Zachodni WBK S.A. transfers the contractual rights to receive the cash flows in a transaction in which substantially all risk and rewards of ownership of the financial asset are transferred.

in thousands of PLN

A regular way purchase of a financial asset is derecognised from the statement of financial position as at the transaction settlement date. This method is applied consistently for all purchases and sales of financial assets.

Bank Zachodni WBK S.A. removes a financial liability (or a part of a financial liability) from its statement of financial position when, and only when, it is extinguished — i.e. when the obligation specified in the contract is discharged or cancelled or expires.

Measurement

When a financial asset or financial liability is recognised initially, it is measured at fair value including (in the case of a financial asset or financial liability not classified at fair value through profit or loss) transaction costs that are directly attributable to the acquisition or issue of the financial asset or financial liability. The best evidence of the fair value of a financial instrument at initial recognition is the transaction price (i.e. the fair value of the consideration given or received) unless the fair value of that instrument is evidenced by comparison with other observable current market transactions in the same instrument (i.e. without modification) or based on a valuation technique whose variables include only data from observable markets.

After initial recognition, Bank Zachodni WBK S.A. measures financial assets, including derivatives that are assets, at their fair values, without any deduction for transaction costs it may incur on sale or other disposal, except for:

- (a) loans and receivables which shall be measured at amortised cost using the effective interest rate method;
- (b) held-to-maturity investments, which are measured at amortised cost using the effective interest rate;
- (c) investments in equity instruments that do not have a quoted market price in an active market and whose fair value cannot be reliably measured.

The fair values of quoted financial instruments in active markets are based on current bid prices. If the market for a financial asset is not active (and for unlisted securities) Bank Zachodni WBK S.A. establishes fair value by using valuation techniques which include recent arm's length market transactions, discounted cash flow analysis, option pricing models and other valuation techniques commonly used by market participants.

Where a fair value cannot be reliably estimated, unquoted instruments that do not have a quoted market price in an active market are measured at cost and periodically reviewed for impairment.

After initial recognition, financial liabilities are measured at amortised cost using the effective interest rate method, except for:

- (a) financial liabilities at fair value through profit and loss. Such liabilities, including derivatives that are liabilities, are measured at fair value;
- (b) financial liabilities resulting from transferring a financial asset that is not to be derecognised.

Financial assets and financial liabilities that are designated as hedged items are subject to measurement under hedge accounting requirements.

Gains and losses on subsequent measurement

A gain or loss arising from a change in the fair value of a financial asset or financial liability that is not part of a hedging relationship is recognised as follows:

- a gain or loss on a financial asset or financial liability classified at fair value through profit and loss is recognised in profit or loss presented in line "Net trading income and revaluation";
- a gain or loss on an available-for-sale financial asset, except for impairment losses, is recognised in other comprehensive income, until the financial asset is derecognised, at which time the cumulative gain or loss previously recognised in other comprehensive income is recognised in profit or loss. However, interest calculated using the effective interest rate method is recognised in profit or loss. Dividends on an available-for-sale equity instruments are recognised in income statement when the entity's right to receive payment is established.

Offsetting financial instruments

Financial assets and financial liabilities are offset and the net amount presented in the statement of financial position when, and only when there is:

- (a) a legally enforceable right to set off the recognised amounts;
- (b) and when there is an intention either to settle on a net basis, or to realise the asset and settle the liability simultaneously.

Subsidiaries, associates and joint ventures

An investment in subsidiaries, associates and joint ventures is recognised at cost less impairment. Impairment is recognised in the income statement. A release of an impairment provision is recognised in a statement of comprehensive income if estimates used to calculate return on investment have changed.

in thousands of PLN

Repurchase and reverse repurchase transactions

Bank Zachodni WBK S.A. also generates/invests funds by selling/purchasing financial instruments under repurchase/reverse repurchase agreements whereby the instruments must be repurchased/resold at the previously agreed price.

Securities sold subject to repurchase agreements ("repo and sell-buy-back transactions") are not derecognised from the statement of financial position at the end of the reporting period. The difference between sale and repurchase price is treated as interest cost and accrued over the life of the agreement.

Securities purchased subject to resale agreements ("reverse repo and buy-sell-back transactions") are not recognised in the statement of financial position at the end of the reporting period. The difference between purchase and resale price is treated as interest income and accrued over the life of the agreement.

Derivative financial instruments

Derivative financial instruments are initially recognised at fair value. After their initial recognition, derivatives are subsequently measured at their fair values without any deduction for transactions costs to be incurred on sale or disposal. The best evidence of the fair value of a financial instrument at initial recognition is the transaction price (i.e. the fair value of the consideration given or received).

Certain derivatives embedded in other financial instruments shall be separated from the host contract and accounted for as a derivative if the economic characteristics and risks of the embedded derivative are not closely related to the economic characteristics and risks of the host contract and the host contract is not carried at fair value through profit or loss. Embedded derivatives are measured at fair value with changes recognised through the income statement.

Bank Zachodni WBK S.A. uses derivative financial instruments to hedge its exposure to foreign exchange and interest rate risks arising from Bank's Zachodni WBK S.A. activities. Derivatives that do not qualify for hedge accounting are accounted for as trading instruments and recognised at fair value.

Hedge accounting

Hedge accounting recognises the offsetting effects on the statement of comprehensive income of changes in the fair values of the hedging instrument and the hedged item.

At the inception of the hedge there is formal designation and documentation of the hedging relationship and Bank's Zachodni WBK S.A. risk management objective and strategy for undertaking the hedge. The documentation includes identification of the hedging instrument, the hedged item or transaction and the nature of the risk being hedged. Bank Zachodni WBK S.A. also documents, at inception and on ongoing basis, an assessment of the hedging instrument's effectiveness in offsetting the exposure to changes in the fair value of the hedged item.

Bank Zachodni WBK S.A. uses derivative financial instruments among others to hedge its exposure to interest rate risks arising from operational, financing and investment activities.

Bank Zachodni WBK S.A. discontinues hedge accounting when:

- (a) it is determined that a derivative is not, or has ceased to be, highly effective as a hedge,
- (b) the derivative expires, or is sold, terminated, or exercised,
- (c) the hedged item matures or is sold or repaid,
- (d) the hedging relationship ceases.

Fair value hedge

This is a hedge of the exposure to changes in fair value of a recognised asset or liability or an unrecognised firm commitment, or an identified portion of such an asset, liability or firm commitment, that is attributable to a particular risk and could affect the income statement.

A fair value hedge is accounted for as follows: the gain or loss from remeasuring the hedging instrument at fair value (for a derivative hedging instrument) shall be recognised in profit or loss; and the gain or loss on the hedged item attributable to the hedged risk shall adjust the carrying amount of the hedged item and be recognised in profit or loss. This applies also to the hedged item, which otherwise would be measured at amortised cost or presented as available-for-sale financial asset.

Cash flow hedge

This is a hedge of the exposure to variability in cash flows that:

- (a) is attributable to a particular risk associated with a recognised asset or liability (such as all or some future interest payments on variable rate debt) or a highly probable forecast transaction and

in thousands of PLN

- (b) could affect the profit and losses.

A cash flow hedge is accounted for as follows: the portion of the gain or loss on the hedging instrument that is determined to be an effective hedge shall be recognised directly in other comprehensive income and the ineffective portion of the gain or loss on the hedging instrument shall be recognised in income statement.

Interest income and expenses from hedged and hedging are recognised as net interest income.

Amounts recognised in 'Other comprehensive income' are reclassified to profit or loss during the period of time in which the hedged item affects the income statement.

If the hedging instrument expires or is sold or the hedge accounting relationship is terminated, Bank Zachodni WBK S.A. discontinues hedge accounting. All profits or losses on the hedging instrument pertaining to the effective hedge recognised in other comprehensive income remains an element of equity until the forecast transaction occurs, when it is recognised in profit or loss.

If the transaction is no longer expected to occur, the cumulative gain or loss relating to the hedging instrument recognised in comprehensive total income is reclassified to profit or loss.

Impairment of financial assets

Assets carried at amortised cost – loans and receivables

Bank Zachodni WBK S.A. assesses at the end of each reporting period whether there is any objective evidence that a financial asset or group of financial assets are impaired. A financial asset or a group of financial assets are impaired and impairment charges are incurred if, and only if, there is objective evidence of impairment as a result of one or more events that occurred after the initial recognition of the asset (a "impairment event") and that impairment event (or events) has an impact on the estimated future cash flows of the financial asset or group of financial assets that can be reliably estimated. It may not be possible to identify a single, discrete event that caused the impairment. Rather the combined effect of several events may have caused the impairment. Losses expected as a result of future events, no matter how likely, are not recognised. Objective evidence that a financial asset or group of assets is impaired includes observable data:

- (a) significant financial difficulty of the issuer or obligor;
- (b) a breach of contract, such as a default or delinquency in interest or principal payments;
- (c) Bank Zachodni WBK S.A., for economic or legal reasons relating to the borrower's financial difficulty, granting to the borrower a concession that Bank Zachodni WBK S.A. would not otherwise consider;
- (d) it becoming probable that the borrower will enter bankruptcy, recovery, arrangement or other financial reorganisation;
- (e) the disappearance of an active market for that financial asset because of financial difficulties; or
- (f) observable data indicating that there is a measurable decrease in the estimated future cash flows from a group of financial assets since the initial recognition of those assets, although the decrease cannot yet be identified with the individual financial assets in Bank Zachodni WBK S.A., including:
 - (i) adverse changes in the payment status of borrowers in Bank Zachodni WBK S.A., or
 - (ii) national or local economic conditions that correlate with defaults on the assets in Bank Zachodni WBK S.A.

If there is objective evidence that an impairment charge on loans and receivables has been incurred, the amount of the impairment charge is measured as the difference between the asset's carrying amount and the present value of estimated future cash flows discounted at the financial asset's original effective interest rate (i.e. the effective interest rate computed at initial recognition). If a loan or receivable has a variable interest rate, the discount rate for measuring any impairment loss is the current effective interest rate determined under the contract. If a floating rate financial asset or floating rate financial liability is recognised initially at an amount equal to the principal receivable or payable on maturity, re-estimating the future interest payments normally has no significant effect on the carrying amount of the asset or liability. The carrying amount of the asset shall be reduced through identification of a impairment charge. The amount of the impairment charge shall be recognised in profit or loss.

The calculation of the present value of the estimated future cash flows of a collateralised financial asset reflects the cash flows that may result from foreclosure less costs in obtaining and selling the collateral.

Bank Zachodni WBK S.A. periodically reviews its loan portfolio to check whether there is any objective evidence that a financial asset or group of financial assets are impaired.

With regard to impairment, the review of individual loan exposures is carried out once a quarter or more often, if needed. Impairment for the portfolio (collective approach), which is assessed jointly, is verified monthly. Bank Zachodni WBK S.A. carries out validation (so called "back tests") of parameters which are used to calculate provisions under collective approach, on the basis of historical observations, at least twice a year.

in thousands of PLN

Impairment of individual loan exposures is based on the amount of prospective receivables (defined as the current value of expected cash flows discounted by the effective interest rate) using the scenario-based approach to the individually significant exposures. As part of the scenario analysis, the relationship manager selects the strategy that reflects the current recovery method. Within each strategy, consideration is given to other possible scenarios. The selected strategy affects the limitations of other parameters' value that can be used in the model. In the individual approach, the impairment charge is determined based on the calculation of the total likelihood-weighted impairment charges estimated for all the possible recovery scenarios, depending on the recovery strategy currently employed vis-à-vis the customer.

In the scenario analysis, the key strategies / scenarios used are as follows:

- Recovery from the operating cash flows / refinancing / capital support;
- Recovery through the voluntary liquidation of collateral;
- Recovery through debt enforcement;
- Recovery through an arrangement / turnaround / bankruptcy;
- Recovery by take-over of the debt / assets / sale of receivables.

Under the collective approach, credit exposures are grouped into portfolios reflecting specific features of the client or product (property, commercial customers, SMEs, mortgages, overdrafts, cash loans, etc.). Each portfolio contains systematic pools based on similar characteristics of the credit risk, i.e.:

- Internal grade;
- Timeliness of debt service;
- Time that has elapsed from the moment of default, i.e. from identification of an indication of impairment;
- Time that has elapsed since an indication of impairment ceased to exist;
- Time from the commencement of debt enforcement;
- Implementation of restructuring measures;
- Parameters specific to certain products (e.g. currency, distribution channel).

If Bank Zachodni WBK S.A. determines that no objective evidence of impairment exists for an individually assessed financial asset, whether significant or not, it includes the asset in a group of financial assets with similar credit risk characteristics and collectively assesses them for impairment. Assets that are individually assessed for impairment and for which an impairment loss is or continues to be recognised by Bank Zachodni WBK S.A. are not included in a collective assessment of impairment.

For the purpose of the collective evaluation of impairment, financial assets are grouped on the basis of similar credit risk characteristics that are indicative of the debtors' ability to pay all amounts due according to the contractual terms (for example, on the basis of Bank's Zachodni WBK S.A. credit risk evaluation or the bank's grading process that considers asset type, industry, geographical location, collateral type, past-due status and other relevant factors). The characteristics chosen are relevant to the estimation of future cash flows for groups of such assets by being indicative of the debtors' ability to pay all amounts due according to the contractual terms of the assets being evaluated.

The rating systems have been internally developed and are continually being enhanced, e.g. externally benchmarked to help underpin the aforementioned factors which determine the estimates of impairment charges.

Future cash flows for a group of financial assets that are collectively evaluated for impairment are estimated on the basis of historical impairment charges experience for assets with credit risk characteristics similar to those in the group. Historical impairment charges experience is adjusted on the basis of current observable data to reflect the effects of current conditions that did not affect the period on which the historical impairment charges experience is based and to remove the effects of conditions in the historical period that do not exist currently.

Estimates of changes in future cash flows reflect and are directionally consistent with changes in related observable data from period to period (such as changes in unemployment rates, property prices, commodity prices, payment status or other factors that are indicative of impairment charges in the group and their magnitude). Bank Zachodni WBK S.A. reviews regularly the methodology and assumptions used for estimating future cash flows in order to reduce any differences between estimates and actual impairment charges experience.

IBNR (Incurred But Not Reported) impairment charges are also maintained to cover loans, which are impaired at the end of the reporting period and, while not separately identified, are known from experience to be present in any portfolio of loans.

IBNR impairment charges are maintained at levels that are deemed appropriate by management having considered: credit grading profiles and grading movements, historic loan impairment charges rates, changes in credit management, procedures, processes and policies, economic climates, portfolio sector profiles/industry conditions and current estimates of loss in the portfolio.

Estimates of incurred but not reported losses (IBNR) take into account the following key factors:

- EP - Emergence Period i.e. estimated time between the occurrence of event of default and its identification by Bank Zachodni WBK S.A.;

in thousands of PLN

- PD - Probability of Default, based on historical observations together with EP is considered to be best indicator of incurred but not reported losses;
- LGD - Loss Given Default i.e. the fraction of the exposure amount that will be lost in the event of default;
- EAD - Exposure at Default;
- CCF - Credit Conversion Factor determining level to which liability to pay out cash will be realized (conversion of off-balance sheet items into on-balance sheet exposure).

These parameters are estimated based on historical experience of impairment charges on loans with a similar credit profile on account of the adopted granularity of the estimated risk parameters.

If, in a subsequent period, the amount of the impairment charge decreases and the decrease is related objectively to an event occurring after the impairment was recognised, the previously recognised impairment charge is reversed by adjusting the impairment charge. The reversal shall not result in a carrying amount of the financial asset that exceeds what the amortised cost would have been had the impairment not been recognised at the date the impairment is reversed.

The amount of the impairment charge reversal is recognised in income statement.

When a loan has been subject to a specific provision and the prospects of recovery do not improve, eventually it may be concluded that there is no real prospect of recovery. When this point is reached, the amount of the loan which is considered to be non-recoverable is written off against the related provision for loan impairment. Subsequent recoveries of amounts previously written off decrease the amount of the provision for loan impairment in the income statement.

Available-for-sale financial assets

For financial assets classified as available-for-sale for which there is objective evidence that the asset is impaired, the cumulative impairment charge that had been recognised directly in other comprehensive income shall be removed and recognised in income statement. The amount of the cumulative impairment charge that is removed from other comprehensive income and recognised in income statement shall be the difference between the acquisition cost (net of any principal repayments and amortisation) and current fair value. If, in a subsequent period, the fair value of a debt instrument classified as available for sale increases and the increase can be objectively related to an event occurring after the impairment charge was recognised, the impairment charge shall be reversed, with the amount of the reversal recognised in income statement.

If there is objective evidence that an impairment loss has been incurred on an unquoted equity instrument that is not carried at fair value because its fair value cannot be reliably measured, the amount of the impairment loss is measured as the difference between the carrying amount of the financial asset and the present value of estimated future cash flows discounted at the current market rate of return for a similar financial asset. Calculated in this way impairment charges are not reversed through income statement.

Contingent liabilities

Bank Zachodni WBK S.A. creates provisions for impairment of risk-bearing irrevocable conditional liabilities (irrevocable credit lines, financial guarantees, letters of credit, etc.). The value of the provision is determined as the difference between the estimated amount of available conditional exposure estimated with the use of Credit Conversion Factor (CCF) and the current value of expected future cash flows under this exposure.

Property, plant and equipment

Owned fixed assets

Property, plant and equipment are stated at cost or deemed cost less accumulated depreciation and impairment losses.

Leased assets

Leases for which Bank Zachodni WBK S.A. assumes substantially all the risks and rewards of ownership are classified as finance leases. Owner-occupied property acquired through finance lease is stated at an amount equal to the lower of its fair value and the present value of the minimum lease payments at inception of the lease, less accumulated depreciation and impairment losses.

Subsequent expenditure

Bank Zachodni WBK S.A. recognises in the carrying amount of property, plant and equipment the cost of replacing part of such an asset when that cost is incurred if it is probable that the future economic benefits embodied with the item will flow to Bank Zachodni WBK S.A. and the cost of the item can be measured reliably. All other costs are recognised in the income statement as an expense as incurred.

in thousands of PLN

Depreciation

Depreciation is charged to the income statement on a straight-line basis over the estimated economic useful lives of each asset. The estimated economic useful lives are as follows:

- | | |
|------------------------|-------------|
| • buildings | 22-40 years |
| • IT equipment | 3 years |
| • transportation means | 4 years |
| • other fixed assets | 14 years |

Depreciation rates are verified annually. On the basis of this verification, depreciation periods might be changed.

Fixed assets held for sale

On initial date of classification of non-current assets as assets held-for-sale, Bank Zachodni WBK S.A. measures them at the lower of carrying amount and fair value less cost to sell.

Any initial or subsequent write-down of assets held-for-sale to fair value less cost to sell is recognised in the income statement.

Goodwill and Intangible assets

Goodwill

Goodwill as of the acquisition date measured as the excess of the consideration transferred over the net of the acquisition-date amounts of the identifiable assets acquired and the liabilities, less impairment. Goodwill value is tested for impairment annually.

Licences, patents, licences and similar assets

Acquired computer software licences are recognized on the basis of the costs incurred to acquire and bring to use the specific software.

Expenditures that are directly associated with the production of identifiable and unique software products controlled by Bank Zachodni WBK S.A., and that will probably generate economic benefits exceeding expenditures beyond one year, are recognised as intangible assets.

Other intangible assets

Other intangible assets that are acquired by Bank Zachodni WBK S.A. are stated at cost less accumulated amortisation and impairment losses.

Expenditure on intangible assets

Subsequent expenditure on capitalised intangible assets is capitalised only when it increases the future economic benefits embodied in the specific asset to which it relates. All other expenditure is expensed as incurred.

Amortisation

Amortisation is charged to the income statement on a straight-line basis over the estimated economic useful lives of intangible assets, which for the majority of intangibles equals to three years.

Amortisation rates are verified annually. On the basis of this verification, amortisation periods might be changed.

Other items of statement of financial position

Other trade and other receivables

Trade receivables and other receivables payable within 12 months from the origination are measured at the initial recognition at par due to the immaterial effect of discounting. Trade receivables and other receivables payable within 12 months are at the balance sheet day recognised in the amount of the required payment less impairment loss.

Other liabilities

Other liabilities payable within 12 months from the initial recognition are measured at par due to the immaterial effect of discounting. Like other liabilities payable within 12 months, trade payables are recognised at the balance sheet day in the amount of the payment due.

in thousands of PLN

Equity

Equity comprises capital and funds created in accordance with applicable law, acts and the Articles of Association. Equity also includes retained earnings and prior year losses carried forward.

Share capital is stated at its nominal value in accordance with the Articles of Association and the entry in the court register.

Supplementary capital is created from profit allocations and share issue premiums.

Reserve capital is created from profit allocations and is earmarked for covering balance sheet losses.

The result of valuation of management incentive program is included in reserve capital (IFRS 2.53).

The supplementary, reserve, general banking risk fund and share premium are presented jointly under category "Other reserve funds".

Revaluation reserve is comprised of adjustments relating to the valuation of available-for-sale financial assets and adjustments relating to the valuation of effective cash flow hedges taking into account deferred tax and actuarial gains from estimating provision for retirement. The revaluation reserve is not distributable.

On derecognition of all or part of financial assets available for sale the total effects of periodical change in the fair value reflected in the revaluation reserve are reversed. Total or part of the previous revaluation charge increases or decreases the value of the given financial asset available for sale. The effects of the fair value changes are removed from the revaluation reserve with a corresponding change in the income statement.

The net financial result for the accounting year is the profit disclosed in the income statement of the current year adjusted by the corporate income tax charge.

Custody services

Income from custody services is an element of the fee and commission income. The corresponding customer assets do not form part of the Bank's Zachodni WBK S.A. assets and as such are not disclosed in the consolidated statement of financial position.

Capital payments (Dividends)

Dividends for a particular year, which have been approved by the General Meeting of Shareholders but not paid at the end of the reporting period are recognised as dividend liabilities in "other liabilities" item.

Employee benefits

Short-term employee benefits

Bank's Zachodni WBK S.A. short-term employment benefits which include wages, bonuses, holiday pay and social insurance payments are recognised as an expense as incurred.

Long-term employee benefits

Bank's Zachodni WBK S.A. net obligation in respect of long-term employee benefits is the amount of future benefit that employees have earned in return for their service in the current and prior periods. The accrual for retirement bonus is estimated using actuarial valuation methods. The valuation of those accruals is updated at least once a year.

Equity-settled share-based payment transactions

For equity-settled share-based payment transactions, Bank Zachodni WBK S.A. measures the goods or services received, and the corresponding increase in equity, directly, at the fair value of the goods or services received, unless that fair value cannot be estimated reliably. If Bank Zachodni WBK S.A. cannot estimate reliably the fair value of the goods or services received, Bank Zachodni WBK S.A. measures their value, and the corresponding increase in equity, indirectly, by reference to the fair value of the equity instruments granted.

Vesting conditions included in the terms of the grant are not taken into account in estimating fair value except where those terms are dependent on market conditions. Non-market vesting conditions are taken into account by adjusting the number of awards included in the measurement of the cost of employee services so that ultimately, the amount recognised in the income statement reflects the number of vested awards.

The expense related to share based payments is credited to shareholder's equity. Where the share based payment arrangements give rise to the issue of new shares, the proceeds of issue of the shares are credited to share capital (nominal amount) and share premium (if any) when awards are exercised.

in thousands of PLN

Cash-settled share-based payment transactions

For cash-settled share-based payment transactions, Bank Zachodni WBK S.A. measures the goods or services acquired and the liability incurred at the fair value of the liability. Until the liability is settled, Bank Zachodni WBK S.A. remeasures the fair value of the liability at each reporting date and at the date of settlement, with any changes in fair value recognised in profit or loss for the period. Bank Zachodni WBK S.A. recognises the services received, and a liability to pay for those services, as the employees render the service. The liability is measured, initially and at each reporting date until settled, at the fair value of the share appreciation rights, by applying an option pricing model, taking into account the terms and conditions on which the share appreciation rights were granted, and the extent to which the employees have rendered the service to that date.

Provisions

A provision is recognised in the balance sheet when Bank Zachodni WBK S.A. has a present legal or constructive obligation as a result of a past event, and it is probable that an outflow of economic benefits will be required to settle the obligation. If the amount is material, provisions are determined by discounting the expected future cash flows at a pre-tax rate that reflects current market assessments of the time value of money and, where appropriate, the risks specific to the liability.

Provisions for contingent liabilities such as guarantees, letters of credit, and unutilised irrevocable credit facilities are recognised in accordance with this policy.

Net interest income

Interest income from a financial asset is recognised when it is probable that the economic benefits will flow to Bank Zachodni WBK S.A. and the amount of income can be measured reliably.

Interest income and expenses for all financial instruments is recognised in the income statement at amortised cost using the effective interest rate method.

The effective interest rate is the rate that exactly discounts estimated future cash payments or receipts through the expected life of the financial instrument or, when appropriate, a shorter period to the net carrying amount of the financial asset or financial liability.

When calculating the effective interest rate, Bank Zachodni WBK S.A. shall estimate cash flows considering all contractual terms of the financial instrument (for example, prepayment, call and similar options) but does not consider future credit losses.

The calculation includes all fees (e.g. arrangement, drawdown, renewal, restructure fees and fees for annexes which modify payments) and amounts paid or received between parties to the contract, transaction costs, and all other premiums or discounts.

Costs that can be directly related to the sales of loan products are partly amortised according to the effective interest method, if there is a possibility of direct allocation to the specific loan agreement, and partly recognised in the fee income, at the moment of realisation, if there is no possibility of direct allocation to the specific loan agreement.

For the selected loan products, where linkage to the insurance product has been identified, Bank Zachodni WBK S.A. splits realised income into a portion recognised as interest income according to effective interest rate method and a portion recognised as fee income. Bank Zachodni WBK S.A. qualifies distributed insurance products as linked to loans in particular if the insurance product influences contractual provisions of a loan.

In case impairment charge is recognised for a financial asset, interest income is accrued based on the carrying amount of receivable (i.e. the value reduced by revaluation charge) using the interest rate according to which future cash flows were discounted for impairment charge valuation.

Net commission income

Fees and commissions settled under effective interest rate are described under section "Net interest income".

Fees on overdrafts, revolving loans, credit cards and off balance sheet liabilities are recognised on a straight-line basis in the income statement. Other fees and charges, which are not settled according to effective interest rate, are included in income statement in accordance with accrual method.

Net fee and commission income includes the outcome from FX transactions.

Net income on bancassurance

For the selected loan products, where linkage to the insurance product has been identified, Bank Zachodni WBK S.A. splits realised income into a portion recognised as interest income according to effective interest rate method and a portion recognised as fee income. Bank Zachodni WBK S.A. qualifies distributed insurance products as linked to loans in particular if the insurance product influences contractual provisions of a loan.

in thousands of PLN

To determine what part of income is an integral part of the credit agreement recognised as interest income using effective interest rate, Bank Zachodni WBK S.A. separates the fair value of the financial instrument offered and the fair value of the intermediation service of insurance product sold together with such instrument. The portion that represents an element of the amortised cost of the financial instrument and the portion that represents remuneration for the agency services are split in proportion to the fair value of the financial instrument and the fair value of the agency service cost, respectively, relative to the sum of the two values.

The portion of income that is considered an agency fee for sales of an insurance product linked to a loan agreement is recognised by Bank Zachodni WBK S.A. as fee income when the fee is charged for sales of an insurance product.

Bank Zachodni WBK S.A. verifies the accuracy of the assumed allocation of different types of income at least annually.

Net trading income and revaluation

Net trading income and revaluation include profits and losses resulting from changes in fair value of financial assets and liabilities classified as held for trading that are measured at fair value through profit and loss. Interest cost and income related to the debt instruments are also reflected in the net interest income.

Dividend income

Dividends are taken to the income statement at the moment of acquiring rights to them by shareholders provided that it is probable that the economic benefits will flow to Bank Zachodni WBK S.A. and the amount of income can be measured reliably.

Profit on disposal of subsidiaries, associates and joint ventures

Profit on the sale of interests in subsidiaries is the difference between the net asset value and their sale price.

Profit on the sale of interests in associates and joint ventures is the difference between the carrying amount and their sale price.

Gains on other financial instruments

Gains on other financial instruments include:

- gains and losses on disposal of equity instruments and debt instruments from the available-for-sale portfolio;
- and changes in the fair value of hedged and hedging instruments, including ineffective portion of cash flow hedges.

Bank Zachodni WBK S.A. uses fair value hedge accounting and cash flow hedge accounting. Details are presented in Note 39 "Hedge accounting".

Other operating income and other operating costs

Other operating income and other operating costs include operating expenses and revenues, which are not related directly to the statutory activity of Bank Zachodni WBK S.A. These are primarily revenues and costs from the sale and liquidation of fixed assets, income from sale of other services, paid and received damages, penalties and fines.

Impairment losses on loans and advances

The line item "Net impairment losses on loans and advances" presents impairment losses on balance sheet and off-balance sheet exposures and the gains/losses on the sale of credit receivables.

The result on loan receivables' sale is computed at the assets' derecognition date in the difference between balance sheet amount and remuneration received.

Staff and general and administrative expenses of the bank

The "Staff expenses" line item presents the following costs:

- remuneration and social insurance (including pension benefit contributions);
- provisions for unused leaves;
- pension provisions;
- bonus provisions;
- the programme for variable components of remuneration paid to individuals holding managerial positions, a part of which is recognised as an obligation on account of share-based payment in cash, in accordance with IFRS 2 Share-Based Payment; and
- employee training and other salary and non-salary benefits for employees.

in thousands of PLN

The line item “General and administrative expenses” presents the following costs:

- maintenance and lease of fixed assets;
- IT and ICT services;
- administrative activity;
- promotion and advertising;
- property protection;
- rental and operating lease;
- charges paid to the Bank Guarantee Fund, the Financial Supervision Authority, the National Depository of Securities;
- taxes and fees (property tax, payments to the National Fund for the Rehabilitation of the Disabled, municipal and administrative fees, perpetual usufruct fees);
- insurance;
- repairs not classified as fixed asset improvements.

Operating lease payments

Operating lease payments are taken to cost in income statement on a straight-line basis over the lease term.

Finance lease payments

Minimum lease payments are apportioned between the finance charge and the reduction of the outstanding liability. Finance charge is allocated over lease term so as to produce a constant periodic rate of interest on the remaining balance of the liability.

Tax on financial institutions

Introduced by an act implemented on 1 February 2016, the tax on financial institutions is calculated on the excess of the entity’s total assets over the PLN 4 billion level; in the case of banks the excess results from the statement of turnover and balances at the end of each month. Banks are permitted to reduce the tax base by e.g. the value of own funds and the value of treasury securities. In addition, banks reduce the tax base by the value of assets purchased from the National Bank of Poland held as collateral for a refinancing credit facility granted by the latter. The tax rate for all taxpayers is 0.0366% per month, and the tax is paid monthly by the 25th day of the month following the month it relates to.

Bank Zachodni WBK S.A. reports the tax charge under “Tax on financial institutions”, separately from the income tax charge.

Corporate income tax

Corporate income tax comprises current and deferred tax. Income tax is recognised in income statement except to the extent that it relates to items recognised in other comprehensive income.

Current tax is the tax payable on the taxable income for the year using tax rates enacted or substantively enacted at the end of the reporting period and any adjustment to tax payable in respect of previous years.

Deferred tax assets and liabilities are provided, using the balance sheet method, on temporary differences between the tax bases of assets and liabilities and their values arising from the statement of financial position. Deferred income tax is determined using tax rates based on legislation enacted or substantively enacted at the end of the reporting period and expected to apply when the deferred tax asset is realised or the deferred tax liability is settled. Deferred tax assets are recognised at realizable amount – it is to the extent that is probable that Bank Zachodni WBK S.A. generates taxable profit allowing partial or wholly realisation of deferred tax assets. The carrying value of deferred tax assets is verified at the end of each reporting period. Bank Zachodni WBK S.A. reduces the carrying amount of the deferred tax asset to the realizable value - that is, to the extent that it is probable that taxable income will be sufficient to partially or fully realize the deferred tax asset.

Deferred and current tax assets and liabilities are only offset when they arise in the same tax reporting group and where there is both the legal right and the intention to settle on a net basis or to realise the asset and settle the liability simultaneously.

in thousands of PLN

3. Risk management

Bank Zachodni WBK is exposed to a variety of risks in its ordinary business activities. The role of risk management is to ensure that the Bank continues to take risk in a controlled way in order to enhance shareholder value. Risk is a possibility that some events would materialise, which would impact the achievement of the Bank's strategic goals.

Risk management policies are designed to identify and measure those risks, define the most profitable return within the accepted risk level (risk-reward), and to continually set and review appropriate risk limits, which restrict the risk exposure.

Bank Zachodni WBK continues to modify and enhance its risk management practices to reflect changes in the Bank's risk profile, economic environment, regulatory requirements and evolving best practice.

In Bank Zachodni WBK, the Management Board and Supervisory Board set the business direction and actively support the risk management strategies. This is achieved by approving the key risk management policies, participation of the Management Board Members in the risk management committees, reviewing and signing off on the key risks and risk reports.

The Supervisory Board continuously oversees the risk management system. The Supervisory Board approves the strategy, key risk management policies, the acceptable risk level and monitors the utilisation of the internal limits in relation to the current business strategy and macroeconomic environment. It conducts the reviews of the key risk areas, the identification of threats and the process of defining and monitoring of remedial actions. The Supervisory Board assesses if the Management Board control activities are effective and aligned with the Supervisory Board policy, including the assessment of the risk management system.

Audit and Compliance Committee of the Supervisory Board supports the Supervisory Board in its supervisory activities. The Committee annually reviews the internal controls in financial reporting, accepts the reports from the independent internal audit unit and compliance units. The Committee receives the regular quarterly reports on the status of the implementation of audit recommendations as the basis of the assessment of the quality of management actions. The Audit Committee assesses the efficiency of the internal control system and the risk management system. In addition, the Committee also monitors financial audit activities, particularly the reviews carried out by the audit firm, checks and monitors independence of the statutory auditor, informs the Supervisory Board of the audit results and evaluates the independence of the statutory auditor and the audit firm. Furthermore, the Committee is responsible for developing an auditor selection policy and procedure, and recommending to the Supervisory Board appointment, reappointment and removal of the external auditor, and the external auditor's fees.

Risk Oversight Committee supports the Supervisory Board in assessment of the effectiveness of the internal control system and risk management system and the resources, which were accepted and planned in order to provide the efficient management of the material risks of the Bank.

In addition, the Supervisory Board is also supported by the **Remuneration Committee** and the **Nomination Committee**, however outside the risk management area.

Management Board is responsible for the effectiveness of the risk management. In particular, the Management Board introduces the organisational structure aligned with the level and profile of the risk being undertaken, split of the responsibilities providing the separation of the risk measurement and control function from the operational activity, is responsible for implementation and updating of the written risk management strategies, and transparency of the activities. The Management Board reviews the financial results of the Bank. The Management Board established a number of committees directly responsible for the development of the risk management methodology and monitoring of risks in particular areas.

The Management Board fulfils its risk management role through the following three committees: Risk Management Committee, Risk Management Sub-Committee and Risk Control Committee.

Risk Management Committee, which is an executive committee responsible for developing a risk management strategy across the Group, including the identification of material risk types, setting the risk appetite and defining the methods of risk measurement, control, monitoring and reporting. **Risk Management Sub-Committee** constitutes part of the Risk Management Committee which approves the key decisions taken by the lower-level risk committees (above established limits).

Risk Control Committee set up to monitor the risk level across different areas of the bank's operations and supervise the activities of lower-level risk management committees set up by the Management Board. Those Committees, acting within the established by the Board competences, are directly responsible for developing risk management methods and for on-going monitoring of risk levels.

The Risk Control Committee has an oversight over the following risk committees:

Risk Management Forum, a body authorised to approve and supervise the risk measurement policy and methodology and to monitor the credit risk, market risk in the banking book, market risk in the trading book, structural balance sheet risk and liquidity risk. The Forum operates through 4 panels:

- **Credit Risk Panel;**
- **Market Risk Panel;**
- **Models and Methodology Panel;**

in thousands of PLN

- **Equity Investment and Underwriting Panel.**

Credit Committee takes credit decisions in accordance with the applicable credit discretion levels.

Provisions Committee decides on the amount of impairment losses, both in individual and portfolio approach to credit exposures, as well as for other financial instruments assets and the legal provisions. The Committee formulates the methodology, reviews and verifies the adequacy of the parameters used for the calculation of impairment on a portfolio and individual level for the Bank.

Information Management Committee is responsible for the quality and organisation of data related to risk management and other areas of the bank's operations.

Cyber Risk Committee as a forum for direct cooperation and communication among all organisational units involved in the processes related to cyber security, to ensure effective supervision of the cyber security strategy.

Operational Risk Management Committee (ORMCo) sets the strategic activities within the operational risk management in the Bank, including business continuity management, information security and fraud prevention.

Assets and Liabilities Committee (ALCO) exercises oversight over the banking portfolio activity and takes decisions on liquidity management and the management of the interest rate risk on the banking book. It is responsible for the funding and balance sheet management, including for the pricing policy.

Capital Committee is responsible for capital management, in particular the ICAAP process.

Disclosures Committee verifies the Bank's financial information in terms of its compliance with legal and regulatory requirements.

Deposit Working Group has a responsibility for ensuring a balanced growth of the savings and investment products portfolio.

Product Marketing and Monitoring Committee approves new products and services to be implemented in the market, taking into account the reputation risk analysis.

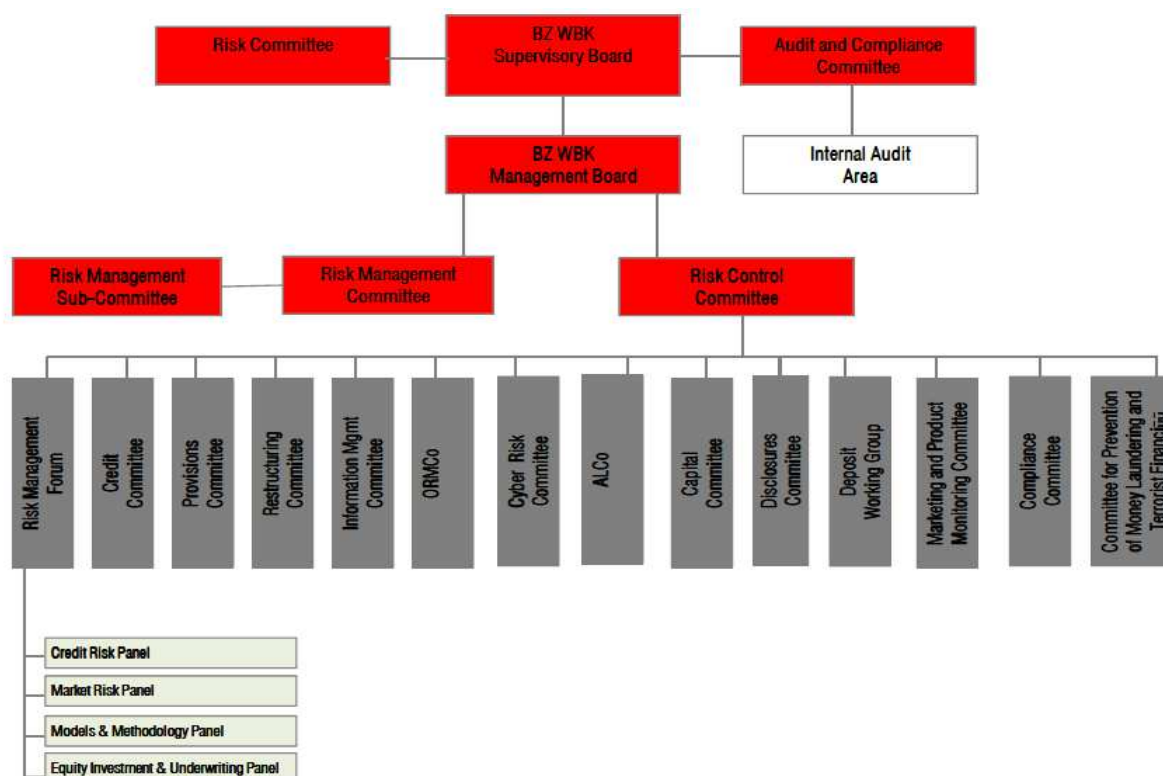
Compliance Committee is responsible for setting standards with respect to the management of compliance risk and the codes of conducts adopted by the Bank.

Anti-Money Laundering and Terrorism Financing Committee approves the Bank's policy on prevention of money laundering and the financing of terrorism. It approves and monitors the Bank's activities in this area.

Restructuring Committee takes decisions as to the relationship management strategy for borrowers in distress as well as the cancellation and sale of loan receivables under the lending discretions.

in thousands of PLN

The picture below presents the corporate governance in relation to the risk governance process.



Risk management is consistent with risk profile resulting from agreed general risk appetite approved by the Risk Management Committee.

Risk appetite is expressed as quantitative limits and captured in the "Risk Appetite Statement" approved by the Management Board and the Supervisory Board. With global limits in place, watch limits are set and risk management policies are drafted.

Bank Zachodni WBK is exposed to a variety of risks affecting its strategic goals. The Bank continuously analyses the risks, identifies their sources, creates the relevant risk management mechanisms including among others the measurement, control, mitigation and reporting. The risks the Bank is exposed to include:

- credit risk;
- concentration risk;
- market risk in the banking and trading books;
- liquidity risk;
- operational risk;
- compliance risk.

Detailed principles, roles and responsibilities of the Bank's units have been described in the relevant internal policies on the management of the particular risks.

Credit risk

The credit delivery activities of Bank Zachodni WBK focus on growing a high quality and profitable loan-book and ensuring customer satisfaction.

Credit risk is defined as the possibility of suffering a loss if the borrower fails to meet their credit obligation, including payment of interest and fees. Credit risk arises also from the impairment of credit assets and contingent liabilities as a consequence of the borrower's worsening credit quality. Credit risk measurement is based on the estimation of credit risk weighted assets, with the relevant risk weights representing both the probability of default and the potential loss given default of the borrower.

in thousands of PLN

The Bank's credit risk arises mainly from lending activities on the retail, corporate and inter-bank markets. This risk is managed as part of the policy approved by the Management Board on the basis of the adopted credit procedures as well as on the basis of discretionary limits allocated to individual credit officers based on their knowledge and experience. The Bank's internal system of credit grading and monitoring allows for an early identification of likely defaults that might impair the loan-book. Additionally the Bank uses a large set of credit risk mitigation tools, both collaterals (financial and non-financial) and specific credit provisions and clauses (covenants).

The Bank continues to develop and implement risk based methods of grading loans, allocating capital and measuring returns. Risk valuation models are used for all credit portfolios.

The Bank is closely looking at the macroeconomic environment and analysing its credit exposure to particular customer segments and economic sectors to respond with an adequate and prompt action and adjust its credit policy parameters accordingly. The year 2017 in this respect was fairly stable and the introduced changes only modified Bank's policy.

One of the Bank's priorities in 2017 was close monitoring of foreign currency housing loan portfolio. In response to the numerous legislative proposals Bank conducted multivariate analyzes and actively participated in the consultation processes. The Bank pays particular attention to credit risk on these portfolios.

The Bank continues to develop and implement processes and procedures of managing and monitoring of credit portfolio' risk adjusting them to the revised regulatory requirements, especially to Recommendations of KNF.

Risk Management Forum

The credit risk oversight in Bank Zachodni WBK is performed by Credit Policy Panel (CPP) operating within the Risk Management Forum. Its key responsibilities include development and approval of the best sectoral practice, industry analyses, credit policies as well as implementation of grading and assessment systems aimed at ensuring sustainable growth of the credit portfolio. To align the Bank's management processes with the current strategic goals, three sub-committees were established within the CPP with a responsibility for the key customer segments: retail segment, SME segment and the business/corporate segment. The oversight over the credit risk models is the responsibility of the Models and Methodology Panel.

Risk Management Division

The Risk Management Division is responsible for a consolidated credit risk management process, including management and supervision of credit delivery, defining credit policies, providing decision-making tools and credit risk measurement tools, quality assurance of the credit portfolio and provision of reliable management information on the credit portfolio.

Credit Policies

Credit policies refer to particular business segments, loan portfolios and banking products. They contain guidelines for the identification of the areas where specific types of risks manifest themselves, specifying the methods of their measurement and mitigation to the level acceptable to the Bank (e.g. "Loan-to-Value" ratios, FX risk in the case of foreign currency loans).

The Bank reviews and updates its credit policies on a regular basis, aiming to bring them in line with the Bank's strategy, current macroeconomic situation, legal developments and changes in regulatory requirements.

Credit Decision Making Process

The credit decision-making process as a part of the risk management policy is based upon Individual Credit Discretions vested in credit officers, commensurate with their knowledge and experience within the business segments. Credit exposures in excess of PLN 25 m are referred to the Credit Committee composed of senior management and top executives. Transactions above PLN 187.5m are additionally ratified by Risk Management Sub-Committee.

The Bank continually strives to ensure best quality credit service while satisfying the borrowers' expectations and ensuring security of the credit portfolio. To this end, the credit risk approval function has been segregated from the sales function.

Credit Grading

Intensive work has been undertaken to further develop credit risk assessment tools to conform to the recommendations of the Polish Financial Supervision Authority, the International Accounting Standards/International Financial Reporting Standards and the best practice in the market.

The Bank uses credit risk grading models for its key credit portfolios, including corporate customers, SMEs, home loans, property loan, cash loans, credit cards and personal overdrafts.

The Bank regularly monitors its credit grading using the rules specified in its Lending Manuals. Additionally, for selected models, automated process of credit grade verification is carried out based on the number of overdue days or an analysis of the customer's behavioural data. Credit grade is also verified at subsequent credit assessments.

in thousands of PLN

Credit Reviews

The Bank performs regular reviews to determine the actual quality of the credit portfolio, confirm that adequate credit grading and provisioning processes are in place, verify compliance with the procedures and credit decisions and to objectively assess professionalism in credit management. The reviews are performed by the two specialised units: Credit Review Department and the Control & Quality Assessment Department, which are independent of the risk-taking units.

Collateral

In the Bank's security model, the Collateral and Credit Agreements Department is the central unit responsible for creation and maintenance of collateral. The Security Manual as a procedure describing legal standards for the application of collateral security is managed by the Legal and Compliance Division. The Collateral and Credit Agreements Department is the owner of the security contract templates.

The role of the department is to ensure that security covers are duly established and held effective in line with the lending policy for all business segments. The unit is also responsible for developing standardised internal procedures with respect to perfecting and maintaining validity of collateral as well as ensuring that establishment, monitoring and release of security covers is duly effected.

Furthermore, the Collateral and Credit Agreements Department provides assistance to credit units in credit decision making and development of credit policies with respect to collateral. The unit gathers data on collateral and ensures appropriate management information.

The tables below show types of collateral that can be used to secure loans and advances to customers from non-banking sector.

Retail customers

Type of loan	Type of collateral
Cash loan	bills, guarantees, credit insurance
Credit on liquid assets	guaranty deposit, amounts frozen on account, investment funds
Student loan	sureties
Housing loan	mortgage, credit insurance, transfer of claim
Leasing	bills, guarantees, transfer of rights to bank's account; court registered pledge on movables; transfer of ownership, open mortgage, obligation of the leased asset supplier to buy the asset back (buy-back guarantee)

Business customers

Type of loan	Type of collateral
Commercial credit	guaranty deposit, registered pledge, bills
Revolving credit	assignment of credit, bills, guarantees, registered pledge
Building credit	mortgage
Investment credit	mortgage, sureties, warranty
Granted and with supplements	guarantees, warranty
Leasing	bills, guarantees, transfer of rights to bank's account; court registered pledge on movables; transfer of ownership, open mortgage, obligation of the leased asset supplier to buy the asset back (buy-back guarantee)

Collateral management process

Before a credit decision is approved, in the situations provided for in internal regulations, the Collateral and Credit Agreements Department assesses the collateral quality, a process that includes:

- verification of the valuation reports prepared by external valuers, and – assessment of the security value;
- assessment of the legal status of the security;
- assessment of the investment process for the properties;
- seeking legal advice on the securities offered.

The Collateral and Credit Agreements Department actively participates in the individual stages of the credit process, focusing on:

- drafting credit documentation in the SME and corporate segments;
- verification and assessment of the signed credit documentation and checking compliance with formal and legal conditions for loan disbursement in the corporate segment;
- verification of data in the IT systems;
- collateral monitoring and reporting;
- releasing the collateral.

in thousands of PLN

The Bank's process of managing its exposures also includes liquidation of collateral. The choice of the scope and method of collateral liquidation to satisfy the Bank's claims depends on the type of collateral (personal or tangible). As a rule, the Bank aims to liquidate the collateral voluntarily through negotiation. If the collateral provider is uncooperative the Bank follows the debt collection course prescribed by law and the Bank's internal regulations.

Financial effect of the collateral

The financial effect of the collateral accepted was calculated as a change in the credit loss allowance as a result of exclusion of the cash flow from collateral (non-performing exposures are assessed on a case-by-case basis). For other portfolios (mortgage, SME and corporate loans), this effect was calculated by adjusting the LGD parameter to the level observed for particular clients on unsecured products.

The table below present financial effect of collateral of Bank Zachodni WBK as at 31.12.2017:

Financial effect of collateral	Gross Amount	Financial effect of collateral
Loans and advances to customers		
housing loans	33 723 865	(175 822)
business	49 011 673	(560 443)
Total balance sheet	93 569 128	(736 265)
Total off-balance sheet	21 409 105	(8 634)

Credit risk stress testing

Stress testing is one of the components of the credit risk management process aimed at assessing how the Bank might be affected by specific changes in its environment, changes in financial and macroeconomic indicators or in the risk profile. The analysis also looks at the potential credit quality changes in the wake of adverse developments. The process also provides management information about adequacy of agreed limits and internal capital allocation.

Calculation of impairment

Bank Zachodni WBK posts impairment losses on credit exposures in accordance with the International Accounting Standard (IAS 39). Impairment losses reflect deterioration in the value of credit assets. An impairment loss is recognised if the Bank has objective evidence that the debt cannot be recovered in line with the signed loan agreement. Objective indications of impairment were defined in accordance with recommendations of the Basel Committee, the International Accounting Standards (IAS 39) and Recommendation R.

Impairment is calculated on the basis of the estimated recoverable amount. Impairment analysis is performed using both the individual (for individually significant exposures with objectively evidenced impairment) and collective approach (individually insignificant exposures with objectively evidenced impairment, and incurred but not reported losses).

Twice a year, the Bank compares the assumptions and parameters used for impairment calculations with the actual situation, taking into account changes of economic conditions, amendments to the Bank's credit policies and recovery processes. The responsibility for ensuring adequacy of the impairment charges rests with the Provisions Committee.

The tables below present the Bank's maximum exposure to credit risk, for presentation purposes grouped by classes, defined by provisions cover.

in thousands of PLN

31.12.2017	Provision cover/ number of days	Loans and advances to customers			Total
		individuals	housing loans	business	
Individually impaired portfolio					
Gross amount		-	-	2 245 995	2 245 995
Impairment		-	-	(1 144 503)	(1 144 503)
Net amount		-	-	1 101 492	1 101 492
Collectively impaired					
Gross amount		696 554	700 511	1 080 562	2 477 627
Impairment		(441 603)	(353 001)	(735 652)	(1 530 256)
Net amount		254 951	347 510	344 910	947 371
IBNR portfolio- non-past due					
	up to 0,10%	1 264 709	29 710 103	29 037 501	60 012 313
	0,10% - 0,30%	2 273 990	1 325 621	9 811 835	13 411 446
	0,30% - 0,65%	5 223 108	52 328	1 869 423	7 144 859
	over 0,65%	385 823	589 556	4 256 648	5 232 027
IBNR portfolio- past due					
	1-30 days	575 927	1 054 952	802 316	2 433 195
	31-60 days	112 848	208 307	84 201	405 356
	61-90 days	61 160	82 284	36 662	180 106
	> 90 days	4 777	205	13 918	18 900
Gross amount-IBNR portfolio					88 838 202
Impairment					(357 366)
Net amount					88 480 836
Gross amount -total		10 598 896	33 723 867	49 239 061	93 561 824
					(3 032 125)
Other receivables*					7 304
Total net amount					90 537 003

in thousands of PLN

31.12.2016	Provision cover/ number of days	Loans and advances to customers			
		individuals	housing loans	business	Total
Individually impaired portfolio					
Gross amount		-	-	2 501 378	2 501 378
Impairment		-	-	(1 196 414)	(1 196 414)
Net amount				1 304 964	1 304 964
Collectively impaired					
Gross amount		818 602	676 207	1 388 789	2 883 598
Impairment		(606 669)	(334 101)	(603 677)	(1 544 447)
Net amount		211 933	342 106	785 112	1 339 151
IBNR portfolio- non-past due					
	up to 0,10%	949 293	24 715 796	28 823 102	51 312 758
	0,10% - 0,30%	1 513 383	5 319 953	7 789 841	15 178 908
	0,30% - 0,65%	5 344 947	52 330	2 135 404	7 853 208
	over 0,65%	580 349	542 031	3 146 382	6 447 565
					80 792 439
IBNR portfolio- past due					
	1-30 days	905 918	1 047 834	1 115 969	3 069 721
	31-60 days	111 132	258 494	67 968	437 594
	61-90 days	56 179	98 984	31 430	186 593
	> 90 days	4 485	38	7 003	11 526
Gross amount-IBNR portfolio					84 497 873
Impairment					(341 566)
Net amount					84 156 307
Gross amount -total		10 284 288	32 711 667	47 007 266	90 003 221
					(3 082 427)
Other receivables*					181 596
Total net amount					86 982 018

* other receivables are unrated, non-past due and unimpaired

Loans and advances to banks are assessed using ratings. The assessment method was set out in the Bank's internal regulations. Each institutional client (exposure) is assigned a rating by one of the reputable rating agencies (Fitch, S&P, Moody's), in accordance with the CRR. Then, a relevant grade is allocated to the client. Grade 1 is equivalent to 20% risk weight. There are no overdue or impaired instruments in these categories.

Loans and advances to banks	31.12.2017	31.12.2016
Credit quality step:		
1	518 189	410 952
2	1 277 403	2 531 691
3	160 710	322 212
4	3 709	26 675
5	1 241	601
6	-	-
none	50 866	16 671
Total	2 012 118	3 308 802

Financial instruments from the available-for-sale and held-for-trading portfolio are assessed in accordance with the sovereign rating (treasury bonds, securities issued by the National Bank of Poland [NBP], Bank Gospodarstwa Krajowego [BGK], available-for-sale and held-for trading instruments). The sovereign rating is the same as the NBP/BGK rating. All have the same rating as Poland, according to Fitch it is A-.

In 'other assets', items without an assigned rating are shown, the significant majority of them are non-past due and unimpaired.

in thousands of PLN

Credit risk concentration

Bank Zachodni WBK adheres to the standards provided for in the Banking Law with regard to the concentration of risk bearing exposures to a single entity or a group of entities connected in terms of capital or organisation.

As at 31.12.2017, pursuant to art. 71 of the Banking Law Act, the maximum limits for the bank totalled:

- PLN 4,465,845 k (25% of Bank's own funds).

As at 31.12.2016, pursuant to art. 71 of the Banking Law Act, the maximum limits for the bank totalled:

- PLN 3,649,232 k (25% of Bank's own funds).

The policy pursued by the Bank aims at minimising the credit concentration risk, by for example applying more rigorous than regulatory rules in this respect. The effect of this policy is maintenance of high level of diversification of exposures towards individual customers.

The analysis of the Bank's exposures in terms of sector concentrations proved that the Bank does not have any exposures in excess of the limits imposed by the regulator in 2017.

A list of the 20 largest borrowers (or group of capital-related borrowers) of Bank Zachodni WBK (performing loans) as at 31.12.2017.

Industry code (PKD)	Industry description	Total credit exposure	Balance sheet exposure	Committed credit lines, guarantees, treasury limits and capital investments
64	OTHER FINANCIAL SERVICES	6 175 232	5 682 322	492 910
64	OTHER FINANCIAL SERVICES	3 289 220	216 993	3 072 227
64	OTHER FINANCIAL SERVICES	3 009 885	2 913 242	96 643
61	TELECOMMUNICATION	1 739 072	1 654 095	84 977
61	TELECOMMUNICATION	952 545	691 708	260 837
06	MINING	938 025	156 658	781 367
35	POWER INDUSTRY	878 972	458 972	420 000
06	MINING	825 213	214 052	611 161
35	POWER INDUSTRY	792 000	153 100	638 900
68	REAL ESTATE SERVICES	652 521	561 091	91 430
68	REAL ESTATE SERVICES	652 284	630 178	22 106
35	POWER INDUSTRY	619 853	329 853	290 000
41	CONSTRUCTION	616 144	537 731	78 413
19	RAFINERY	568 390	-	568 390
41	CONSTRUCTION	539 000	-	539 000
35	POWER INDUSTRY	513 959	446 857	67 102
70	CONSULTING	454 351	277 400	176 951
35	RAFINERY	398 116	398 116	-
68	REAL ESTATE SERVICES	373 264	353 953	19 311
35	POWER INDUSTRY	361 922	300 436	61 486
Total gross exposure		24 349 968	15 976 757	8 373 211

in thousands of PLN

A list of the 20 largest borrowers (or group of capital-related borrowers) of Bank Zachodni WBK (performing loans) as at 31.12.2016.

Industry code (PKD)	Industry description	Total credit exposure	Balance sheet exposure	Committed credit lines, guarantees, treasury limits and capital investments
64	OTHER FINANCIAL SERVICES	3 354 340	2 788 547	565 793
64	OTHER FINANCIAL SERVICES	3 236 783	216 997	3 019 786
64	OTHER FINANCIAL SERVICES	3 200 000	2 778 617	421 383
64	OTHER FINANCIAL SERVICES	2 302 557	2 164 775	137 782
61	TELECOMMUNICATION	1 857 349	1 612 419	244 930
06	MINING	1 180 593	15 047	1 165 546
07	MINING	1 123 795	216 276	907 519
35	POWER INDUSTRY	878 974	295 974	583 000
68	REAL ESTATE SERVICES	792 496	646 988	145 508
35	POWER INDUSTRY	791 261	253 597	537 664
19	RAFINERY	681 806	-	681 806
41	CONSTRUCTION	657 672	591 312	66 360
35	POWER INDUSTRY	564 615	405 657	158 958
68	REAL ESTATE SERVICES	555 243	342 772	212 471
35	POWER INDUSTRY	545 830	329 830	216 000
35	POWER INDUSTRY	537 789	462 701	75 088
41	CONSTRUCTION	494 001	1	494 000
19	RAFINERY	427 430	163 560	263 870
68	REAL ESTATE SERVICES	414 811	394 328	20 483
68	REAL ESTATE SERVICES	398 521	327 066	71 455
Total gross exposure		23 995 866	14 006 464	9 989 402

Industry concentration

The credit policy of Bank Zachodni WBK assumes diversification of credit exposures. Risk of particular industry affects value of the exposure limit. In order to ensure adequate portfolio diversification and control the risk of overexposure to a single industry, the Bank provides funding to sectors and groups or capital units representing a variety of industries.

As at 31.12.2017, the highest concentration level was recorded in the “distribution” sector (12% of the Bank Zachodni WBK exposure), “financial sector” (11%) and “manufacturing” (9%).

Groups of PKD by industries:

Industry	Gross exposure		
	31.12.2017	31.12.2016	
Distribution	11 206 089	10 068 097	
Financial sector	9 979 473	8 840 305	
Manufacturing	8 282 887	8 001 053	
Property	7 832 541	8 594 381	
Energy	2 510 916	2 224 262	
Transportation	1 373 327	1 199 147	
Agriculture	1 218 554	1 061 495	
Construction	1 040 444	1 019 912	
Other industries	5 421 923	5 706 034	
A	Total Business Loans	48 866 154	46 714 686
B	Retail (including mortgage loans)	44 695 670	43 288 535
A+B	BZ WBK portfolio	93 561 824	90 003 221
C	Other receivables (commercial bonds)	7 304	181 596
A+B+C	Total BZ WBK	93 569 128	90 184 817

in thousands of PLN

Forbearance Policy

Pursuant to the definition set out in the draft Implementing Technical Standards of the European Banking Authority, a forbearance measure (i.e. customer debt restructuring) consists of a concession towards a debtor facing financial difficulties or prospect difficulties which threaten the repayment of debt towards BZ WBK on the existing contractual terms. The concession may involve a modification of the previous terms and conditions of a debt contract or its total or partial refinancing. The purpose of debt restructuring is to better align repayment terms with the current and projected financial standing of the customer, minimise default risk and/or maximise recovery.

Restructuring does not refer to a technical or operational modification of contractual terms, or changes attributable to other factors than payment difficulties (business or market conditions).

The decision on granting a concession towards a customer with insufficient debt service ability is based on an analysis of its financial standing, assessment of repayment capacity under the new terms, analysis of existing collateral, assessment of the willingness to repay and the relationship history. The concessions depend on the results of the assessment and may involve in particular: moratorium on payments, modification of repayment schedule (reduced payments), interest capitalisation, extension of maturity etc. Such solutions may be applied to both personal and business customers.

Each concession (debt restructuring) is adequately reflected in the systems to allow for identification of debt portfolio under restructuring. Debt/customer is classified as under restructuring throughout the restructuring period, i.e. until the Bank establishes that the customer circumstances are sustainable, restructuring conditions have been met, there are no overdue payments above 30 days and the customer has a satisfactory repayment capacity. In accordance with a prudent approach, customers are reported as "subject to restructuring" for the minimum period of two years.

There are specialised units at the bank whose objective is to ensure a better quality of the credit portfolio through early restructuring and facilitation of debt repayment by customers. The effectiveness of actions taken by the above units and the portfolio subject to restructuring are regularly monitored by relevant Committees.

Accounting principles applicable to financial assets subject to forbearance are the same as in the case of other performing or non-performing assets in the Bank, that is loans and receivables are measured at amortised cost using the effective interest method. If the terms of a loan, receivable or held-to-maturity investment are renegotiated or otherwise modified because of financial difficulties of the borrower or issuer, the exposure is measured using the original effective interest rate before the modification of terms (in accordance with IAS 39 AG 84).

		Book value	
		31.12.2017	31.12.2016
Loans and advances to customers- gross amount			
under forbearance measure:		3 081 530	3 620 780
	corporate exposures	1 959 502	2 554 629
	mortgage exposures	946 212	936 319
	individuals exposures	175 816	129 832
Allowance for impairment - forbearance clients		(651 099)	(733 395)
	of which: individually impaired	(413 055)	(502 349)
Loans and advances to forbearance clients- net amount		2 430 431	2 887 385

Analysis of credit quality of financial assets subject to forbearance:

Loans and advances to customers under forbearance	Gross exposure		Collateral value		Allowance for impairment	
	31.12.2017	31.12.2016	31.12.2017	31.12.2016	31.12.2017	31.12.2016
Loans and advances -impaired	1 568 024	1 889 974	9 064 413	6 692 669	(612 227)	(679 872)
Loans and advances -unimpaired	1 513 506	1 730 806	2 789 490	5 073 632	(38 872)	(53 523)
non-overdue	1 196 468	1 053 988	2 281 523	2 667 597	(25 663)	(32 380)
from 1 to 30 days overdue	227 848	567 030	381 650	2 203 805	(10 685)	(17 253)
from 31 to 60 days overdue	61 403	74 744	89 545	91 641	(1 619)	(2 324)
from 61 to 90 days overdue	27 787	35 044	36 772	110 589	(905)	(1 566)
Total gross amount	3 081 530	3 620 780	11 853 903	11 766 301	(651 099)	(733 395)

Interest income on assets subject to forbearance was PLN 69,601 k as at 31.12.2017 and PLN 96,331 k as at 31.12.2016.

in thousands of PLN

Loans and advances to customers under forbearance by geographical region (gross amount)	31.12.2017	31.12.2016
Dolnośląskie	317 404	298 385
Kujawsko-Pomorskie	43 223	43 725
Lubelskie	30 685	27 591
Lubuskie	40 316	38 656
Mazowieckie	1 317 268	1 871 206
Małopolskie	195 950	92 461
Opolskie	23 716	20 615
Podkarpackie	21 918	21 312
Podlaskie	34 566	30 312
Pomorskie	155 802	163 983
Warmińsko-Mazurskie	28 335	25 760
Wielkopolskie	155 554	155 547
Zachodniopomorskie	58 649	55 622
Śląskie	529 202	520 326
Świętokrzyskie	70 008	188 408
Łódzkie	58 934	66 871
Total	3 081 530	3 620 780

Loans and advances to customers under forbearance by industry (gross amount)	31.12.2017	31.12.2016
Construction	224 891	274 516
Distribution	82 793	74 408
Energy	398 913	399 368
Financial sector	557	341
Other industries	179 333	176 376
Property	799 621	1 360 369
Manufacturing	169 215	227 267
Agriculture	69 065	8 410
Transportation	35 114	33 574
Individuals	1 122 028	1 066 151
Total	3 081 530	3 620 780

	31.12.2017	31.12.2016
Net carrying amount as at beginning of the period	2 887 385	2 787 791
Allowance for impairment	82 296	395 391
Loans and advances derecognised during the period	(144 515)	(758 110)
Loans and advances recognised during the period	1 135 017	1 260 732
Other changes/repayments	(1 529 752)	(798 419)
Net carrying amount as at the end of the period	2 430 431	2 887 385

Market risk

Market risk is defined as an adverse earnings impact of changes in interest rates, FX rates, share quotations, stock exchange indices, etc. It arises in trading activity as well as in the ordinary course of transacting business (exchange rate products, interest rate products, equity linked trackers).

Bank Zachodni WBK is exposed to market risk arising from its activity on money and capital markets and services provided to customers. Additionally, the Bank undertakes the market risk related to the active management of balance sheet structure (assets and liabilities management).

The activity and strategies on market risk management are directly supervised by the Risk Management Forum.

General principles of market risk management

The key objective of the market risk policy pursued by the Bank is to reduce the impact of the volatile market environment on the Bank's profitability and to grow income within strictly defined risk parameters while ensuring the Bank's liquidity and market value.

The Bank's market risk policies establish a number of limits and ratios for the purpose of risk assessment and mitigation. Risk limits are periodically reviewed to align them with the Bank's strategy.

in thousands of PLN

Interest rate and FX risks linked to the banking business is managed centrally by the Financial Management Division. The Division is also responsible for acquiring funding, managing liquidity and making transactions on behalf of ALCO. This activity is controlled by the measures and limits approved from time to time by the Risk Management Forum, the Bank's Management Board and the Supervisory Board.

The debt securities and the interest rate derivatives portfolio is managed by ALCO, which takes all decisions on the portfolio's value and structure.

The market risk on the trading portfolio is managed by the Global Corporate Banking Division, which is also responsible for the activities of the Brokerage Services Office.

The Bank's trading activity is subject to a system of measures and limits, including Value at Risk, stop loss, position limits and sensitivity limits. This limits are approved by the Risk Management Forum, the Bank's Management Board and the Supervisory Board.

The Financial Risk Department within the Risk Management Division is responsible for ongoing assessment of the current risk, implementation of control procedures and risk monitoring and reporting. The Department is also responsible for shaping the market risk policy, proposing risk assessment methodologies and ensuring consistency of the risk management process across the Bank. Owing to the fact that the Department is a part of the Risk Management Division, the risk assessment and monitoring processes are separate from the risk-taking units.

Assessment methods

Bank Zachodni WBK uses several methods to assess its market risk exposure. The methods employed for the banking portfolio are the MVE and NII sensitivity measures, while the methods used for the trading portfolio include: Value at Risk (VaR), stop loss, sensitivity measures (PV01) and stress tests. The risk assessment methodology is subject to an independent initial and periodic validation, the results of which are presented for approval to the Models and Methodology Panel (part of the Risk Management Forum).

In Bank Zachodni WBK, VaR is determined by means of a statistical modelling process as a difference between the mark-to-market value of positions and the market values based on the most severe movements in market rates from a determined observation window.

Due to the limitations of the VaR methodology, the Bank augments it by stress tests and by sensitivity measurement that shows how position value changes in reaction to price/profitability movements.

VaR in the banking portfolio is calculated separately as a combined effect of EaR (Earnings-at-Risk) and EVE VaR (value at risk of the economic value of equity).

Interest rate risk in the banking book

The interest rate risk in the banking book is the risk of adverse impact of interest rate changes on the Bank's income and the value of its assets and liabilities. The main source of interest rate risk are transactions entered in the Bank's branches and in the business and corporate centres, as well as the transactions made in the money market by the Financial Management Division. Additionally, interest rate risk can be generated by transactions concluded by other units, e.g. through acquisition of municipal/commercial bonds, or the Bank's borrowings from the interbank market. However, all positions that generate a repricing risk are transferred for management to the Financial Management Division, where the Bank's dealers enter into transactions in the interbank markets so as to manage the overall interest rate risk profile according to the approved risk strategy and in compliance with the allocated risk limits.

The interest rate risk in the banking book is managed based on the following limits:

- NII sensitivity limit (i.e. sensitivity of the net interest income to a parallel shift of the yield curve by 100 bp);
- MVE sensitivity limit (i.e. sensitivity of the market value of equity to a parallel shift of the yield curve by 100 bp).

The sensitivity measures for 2017 and 2016 are presented in the table below. It presents the results of scenarios, in which the impact of changes in interest rates on interest income and the economic value of capital would be negative.

1 day holding period	NII Sensitivity		MVE Sensitivity	
	31.12.2017	31.12.2016	31.12.2017	31.12.2016
Maximum	238	218	377	250
Average	211	184	267	198
as at the end of the period	238	218	347	218
Limit	310	280	380	340

In 2017, the global NII and MVE limits for the banking book were not exceeded.

in thousands of PLN

Interest rate risk in the trading book

The trading book contains securities and derivatives held by the Global Corporate Banking Division for trading purposes. The instruments are marked to market each day, and any changes in their value are reflected in the profit and loss. The key methods of measurement of the interest rate risk in the banking books include the VaR methodology, stop loss, PV01 sensitivity measurement and stress tests.

The VaR in the Bank is calculated for the open positions of the Global Corporate Banking by establishing the difference between the market valuation of the interest rate transactions based on the current yield curves, and the valuation based on the "worst case" yield curve, which is calculated based on the fluctuations in the interest rates.

The "stop-loss" mechanism is used for managing the risk of losses on the items covered by the rules of fair valuation through profit and loss.

Stress tests are used in addition to these measures by providing an estimate of the potential losses in the event of materialisation of the stressed conditions in the market. The assumptions of stress scenarios are based on sensitivity reports and on extreme market rate movement scenarios set using the highest daily and monthly changes in interest rates.

The table below shows risk measures at the end of 2017 and 2016 for 1-day position holding period.

Interest rate risk 1 day holding period	VAR	
	31.12.2017	31.12.2016
Average	1 559	1 706
Maximum	4 777	3 681
Minimum	373	659
as at the end of the period	839	1 509
Limit	6 266	7 523

In 2017, the VAR limit for interest rate risk has not been exceeded.

FX risk

FX risk is the risk that adverse movements in foreign exchange rates will have an impact on results (and result in losses). This risk is managed by the VaR limit for the open currency positions in the Bank's trading portfolio. Stress tests are used in addition to this measure by providing an estimate of the potential losses in the event of materialisation of the stressed conditions in the market. Stress tests use the currency exposure and the scenarios of extreme movements in currency rates based on historical data. Furthermore, the stop loss mechanism is used for managing the risk of losses on the trading positions.

In accordance with its policy, the Bank does not maintain open positions on currency options. Transactions made with clients are immediately closed in the wholesale market thus limiting the Bank's exposure to the market risk on the currency options portfolio.

The table below illustrates the risk measures at the end of December 2017 and 2016.

FX risk 1 day holding period	VAR	
	31.12.2017	31.12.2016
Average	414	393
Maximum	1 725	3 096
Minimum	50	30
as at the end of the period	175	319
Limit	2 611	3 134

In 2017, the VAR limit for FX risk has not been exceeded.

FX Balance Sheet

In 2017, the share of assets in foreign currencies in the bank's balance sheet decreased further compared to the level observed in previous periods. A slight decrease in amounts receivable in EUR and in amounts receivable in CHF were observed as a result of continued amortisation of mortgage loans. A decrease in amounts due from customers in EUR and a decrease in amounts due from customers in CHF were observed as a result of the continuing amortisation of the mortgage loan portfolio, as well as strengthening of the national currency. The above decrease, together with the increase in financing in the form of a subordinated loan, significantly reduced the gap between EUR assets and liabilities.

The resulting funding gap was closed by entering into a swap transaction in the FX market.

in thousands of PLN

The tables below show the Bank's main FX items – as at 31.12.2017 and 31.12.2016.

31.12.2017	PLN	EUR	CHF	USD	Other	Total
ASSETS						
Cash and balances with central banks	3 646 691	316 341	16 408	74 683	60 678	4 114 801
Loans and advances to banks	244 786	1 293 502	2 738	315 221	155 871	2 012 118
Loans and advances to customers	67 445 351	13 898 367	8 414 097	643 975	135 213	90 537 003
Investment securities	24 534 492	803 778	-	445 759	-	25 784 029
Selected assets	95 871 320	16 311 988	8 433 243	1 479 638	351 762	122 447 951
LIABILITIES						
Deposits from banks	301 469	1 061 276	5 103	37 292	9 308	1 414 448
Deposits from customers	82 989 622	13 629 198	342 796	4 101 665	1 092 242	102 155 523
Subordinated liabilities	-	1 488 602	-	-	-	1 488 602
Selected liabilities	83 291 091	16 179 076	347 899	4 138 957	1 101 550	105 058 573
31.12.2016	PLN	EUR	CHF	USD	Other	Total
ASSETS						
Cash and balances with central banks	4 341 719	221 874	18 083	48 073	66 885	4 696 634
Loans and advances to banks	323 153	2 656 552	23 120	207 867	98 110	3 308 802
Loans and advances to customers	59 372 866	16 392 857	10 509 567	675 502	151 598	87 102 390
Investment securities	24 887 081	995 504	-	439 776	-	26 322 361
Selected assets	88 924 819	20 266 787	10 550 770	1 371 218	316 593	121 430 187
LIABILITIES						
Deposits from banks	366 840	790 952	23 652	30 357	964	1 212 765
Deposits from customers	87 041 211	12 207 824	288 917	2 947 761	895 536	103 381 249
Subordinated liabilities	-	440 457	-	-	-	440 457
Selected liabilities	87 408 051	13 439 233	312 569	2 978 118	896 500	105 034 471

Equity investment risk

The unit responsible for equity price risk management is Brokerage Office which now operates within the Financial Markets Area. The source of this risk are transactions conducted on Brokerage Office own account via stock exchanges and MS CTO (shares, futures).

This risk is measured using a Value at Risk model based on the historical method.

The market risk management in Brokerage Office is supervised by BZ WBK Risk Management Forum. The Forum sets the VaR limit for the brokerage house, approves changes in the risk measurement methodology and oversees the risk management process.

The table below presents the risk measures in 2017 and 2016:

Equity risk	VAR Brokerage Office	
	31.12.2017	31.12.2016
1 day holding period		
Average	304	301
Maximum	694	742
Minimum	46	50
as at end of the period	90	77
Limit	3 621	4 346

In 2017, the VAR limit for equity risk has not been exceeded.

Liquidity risk

Liquidity risk is the risk that the Bank fails to meet its contingent and non-contingent obligations towards customers and counterparties as a result of a mismatch of financial cash flows.

Liquidity Risk Management

The BZ WBK Liquidity Risk Policy is designed to:

- ensure the ability to finance assets and satisfy claims, both current and future, in a timely manner and at an economic price;
- manage the maturity mismatch between assets and liabilities;
- set a scale of the liquidity risk in the form of various internal limits;
- ensure proper organization of the liquidity management process in Bank Zachodni WBK;
- prepare the organization for emergence of adverse factors, either external or internal;
- ensure compliance with regulatory requirements, both qualitative and quantitative.

in thousands of PLN

The general principle adopted by the Bank in its liquidity management process is that all expected outflows occurring within 1 month in respect of deposits, current funds, loan drawdowns, guarantee payments and transaction settlements should be at least fully covered by the anticipated inflows or available High Quality Liquid Assets (HQLA) assuming normal or predictable conditions for the bank's operations. The QLA category includes: cash on hand, cash deposited with NBP (National Bank of Poland), securities which may be sold or pledged under repo transactions or NBP lombard loans. As at 31 December 2017, the value of easy resalable assets buffer amounted to PLN 27,8 b.

The purpose of the policy is also to ensure an adequate structure of funding the growing scale of Bank Zachodni WBK's business by maintaining liquidity ratios at pre-defined levels. The bank uses a suite of additional watch limits and indicators with respect to the following:

- loan-to-deposit ratio;
- structural funding ratio, which measures the amount of long-term funding relative to non-liquid assets;
- ratios of reliance on wholesale funding, which are used to assess the concentration of foreign currency funding from the wholesale market;
- concentration of deposit funding;
- regulatory liquidity ratios calculated in accordance with KNF Resolution no. 386/2008;
- ratios laid down in CRD IV/CRR - LCR and NSFR;
- survival horizon under stressed conditions.

As at 31 December 2017, LCR ratio was at 141% and NSFR ratio was at 124%.

The internal liquidity limits, including the limits established in the Risk Appetite Statement, are set on the basis of both historical values of the selected liquidity ratios as well as their future values which are estimated against a financial plan. The limits also take into account the results of stress tests.

Management Process

The responsibility for supervision over the liquidity risk management process rests on the Assets and Liabilities Committee (ALCO), which also provides advice to the Management Board. ALCO prepares management strategies and recommends to the Management Board appropriate actions with regard to strategic liquidity management. Day-to-day management of liquidity is delegated to the Financial Management Division. The Assets and Liabilities Management Department, which is a part of the Division, is responsible for developing and updating the relevant liquidity management strategies, including strategies of Bank's activity's financing..

The Bank has a scenario-based contingency plan approved by the Management and Supervisory Board to cater for unexpected liquidity problems, whether caused by external or internal factors. The plan also contains stress test with system and idiosyncratic scenarios.

Risk Measurement and Reporting

The responsibility for assessment and reporting of the liquidity risk rests on the Risk Management Division, specifically the Financial Risk Department.

The role of the Department is to draft liquidity management policies, carry out stress tests and to measure and report on risk.

Liquidity is measured by means of the modified liquidity gap, which is designed separately for the PLN and currency positions. The reported contract positions are subject to modifications based on: statistical analyses of the deposit and credit base behaviour, evaluation of the possibility to liquidate State Treasury securities by selling or pledging them in repo transactions or using liquidity supporting instruments in NBP, evaluation of transaction rolling in the interbank market.

When measuring liquidity risk, the bank additionally analyses the degree of liquidity outflows arising from potential margin calls due to changes in the value of derivatives transactions and collateral needs related to secured financing transactions resulting from the downgrade of the bank's credit rating, among other things.

Concurrently, liquidity was measured in accordance with binding at 31 December 2017 -KNF Resolution no. 386/2008 on setting liquidity standards for banks, and with the requirements laid down in CRD IV / CRR package together with related implementing acts.

The results of liquidity risk measurement are reported on a daily basis to persons in charge of operational management of the bank's liquidity and to persons responsible for liquidity risk management (information about intraday and current liquidity, including FX funding ratios and LCR) and - on a monthly basis - to senior executives (other liquidity ratios, including regulatory ratios).

Stress tests and the contingency plan

In order to establish a detailed risk profile, the Bank conducts stress tests using the following scenarios:

- Baseline scenario, which assumes non-renewability of wholesale funding;
- Idiosyncratic liquidity crisis scenarios (specific to the bank);
- Local systemic liquidity crisis scenario;

in thousands of PLN

- Global systemic liquidity crisis scenario;
- Combined liquidity crisis scenario (idiosyncratic crisis and local systemic crisis);
- Deposit outflows in a one-month horizon.

For each of the above scenarios, the Bank estimates the minimum survival horizon. For selected scenarios, the bank sets survival horizon limits which are subsequently included in the liquidity risk appetite.

In addition, the Bank performs stress tests for intra-day liquidity as well as reverse stress tests.

The Bank has the Contingency Liquidity Plan in place to ensure that there are mechanisms enabling to take adequate and effective actions in response to unexpected external or internal liquidity problems. The Plan allows the Bank to:

- identify threats to the bank's liquidity on the basis of a set of early warning ratios which are subject to ongoing monitoring;
- effectively manage liquidity / funding, using a set of possible remedial actions and the management structure adjusted to the stressed conditions;
- communicate with customers, key market counterparties, shareholders and regulators.

In 2017, as in previous years, the Bank focused on keeping its loan-to-deposit ratio at a comfortable level (which totaled 89% as at 31 December 2017) and controlling key short- and long-term liquidity measures.

In 2017 and in the comparable period, all key supervisory measures applicable to the Bank were maintained at the required levels.

Contractual liquidity gap analysis as at 31.12.2017 and in comparable period:

31.12.2017	A'vista	up to 1 month	from 1 to 3 months	from 3 to 6 months	from 6 to 12 months	from 1 to 2 years	from 2 to 5 years	above 5 years
Assets	16 285 962	5 487 477	2 737 369	7 877 137	6 474 997	11 747 539	29 354 839	52 897 949
Liabilities and equity	18 843 600	27 882 654	16 438 439	9 538 471	7 722 235	6 373 358	10 297 600	35 766 911
including:								
- Sell-buy-back transactions	-	-	-	-	-	-	-	-
- Deposits from banks	746 740	2 101 959	410 361	73 443	15 400	-	-	-
- Deposits from customers	18 096 859	25 572 150	15 250 513	8 942 409	6 832 174	6 014 336	8 958 040	9 081 624
- Debt securities in issue	-	-	750 000	485 000	-	-	-	-
- Subordinated liabilities	-	-	-	-	-	-	-	1 489 428
Contractual liquidity mismatch/ gap	(2 557 638)	(22 395 177)	(13 701 070)	(1 661 334)	(1 247 239)	5 374 180	19 057 239	17 131 038
Cumulative liquidity gap	(2 557 638)	(24 952 815)	(38 653 886)	(40 315 219)	(41 562 458)	(36 188 277)	(17 131 038)	-
Net derivatives	-	(63 970)	13 782	(76 812)	(33 280)	12 856	(6 049)	(119 732)

31.12.2016	A'vista	up to 1 month	from 1 to 3 months	from 3 to 6 months	from 6 to 12 months	from 1 to 2 years	from 2 to 5 years	above 5 years
Assets	21 977 376	6 015 915	1 818 154	2 780 366	5 651 079	16 734 537	26 288 169	50 152 393
Liabilities and equity	61 200 626	15 721 571	11 352 248	7 971 541	4 624 337	2 966 499	1 847 241	25 733 926
including:								
- Sell-buy-back transactions	-	-	-	-	-	-	-	-
- Deposits from banks	578 557	86 607	118 025	34 237	26 400	-	-	-
- Deposits from customers	60 622 069	15 634 964	10 945 920	7 394 630	3 979 739	1 260 040	70 033	-
- Debt securities in issue	-	-	285 000	-	475 000	485 000	-	530 880
- Subordinated liabilities	-	-	-	-	-	-	-	442 400
Contractual liquidity mismatch/ gap	(39 223 249)	(9 705 656)	(9 534 094)	(5 191 175)	1 026 742	13 768 038	24 440 928	24 418 467
Cumulative liquidity gap	(39 223 249)	(48 928 906)	(58 463 000)	(63 654 174)	(62 627 432)	(48 859 394)	(24 418 467)	-
Net derivatives	-	12 207	(145 252)	(11 535)	(51 183)	(173 801)	(187 448)	(1 018 843)

Operating Risk

Bank Zachodni WBK adopted the operational risk definition of the Basel Committee on Banking Supervision, which states that: operational risk is the risk of a loss resulting from inadequate or failed internal processes, people and systems or from external events.

The objective of the operational risk management is to minimise the likelihood and/or reduce the impact of unexpected adverse events.

in thousands of PLN

Bank Zachodni WBK has implemented an integrated risk management framework to ensure that all risks which have a significant impact on Bank Zachodni WBK business are identified, measured, monitored and controlled. Operational risk management in Bank Zachodni WBK involves employees at all levels of the organisation and consists of a number of interrelated concepts. Operational risk is inherent in all the Bank's business processes, including the outsourced functions or services delivered jointly with third parties.

Bank Zachodni WBK has defined the Operational Risk Management Strategy and as well as other relevant policies regulating operating risk issues. In addition, detailed procedures and guidelines are used to define how risks are identified, estimated, monitored and mitigated.

The Operational Risk Management Committee (ORMCO) established by the Management Board is responsible for setting operational risk management standards for BZ WBK. ORMCO is the main forum for discussions on operational risk. It sets out the strategic direction for operational risk management, determines and monitors objectives for managing operational risk, including business continuity, information security, outsourcing / insourcing and money laundering risk in all business areas of BZ WBK. Within the ORMCO Committee several bodies (Forums) were established to address specific aspects of operational risk e.g. Crime Prevention Forum and the Forum of Insurance. The effects of this work are reported to the Risk Control Committee.

As a result of high and rising cyber risk worldwide new Cyber Risk Committee has been set up. It is a forum for direct cooperation and communication among all organisational units involved in the processes related to cyber security, to ensure effective supervision of the cyber security strategy.

Bank Zachodni WBK uses the following tools:

- Identification and estimation of operational risk

Primary tool for identification and assessment of operational risk is self-assessment. In the self-assessment process, Bank identifies the risks it may be exposed to when delivering its functions, assesses inherent and residual risks in terms of their likelihood and impact, and evaluates efficiency of the existing controls. In addition, action plans are devised to improve the efficiency of the existing and/or new controls.

The process of identification and assessment of operational risk is additionally supported by other tools dedicated to specific risk aspects such as: scenario analyses, business impact analyses, analysis of risk in new initiatives.

- Reporting on operational incidents and lessons learned

Each organisational unit is required to report operational incidents on a monthly basis. For significant operational incidents there is the path for prompt notification to senior management. The Bank runs a database of operational incidents identified across the organisation. The data are used to analyse the root cause and consequences of the incidents, capture lessons learned and take preventive and corrective measures.

The Bank also makes inputs to the external database of operational events run by the Polish Banks Association and uses information about external events from a number of sources. The analysis of external events allows for benchmarking and lesson learning from events identified outside the Bank.

- Analysis of risk indicators

Primary tool for monitoring of operational risk are risk indicators. Bank Zachodni WBK monitors risk indicators, both financial and operational ones. Risk indicators provide early warning of emerging threats and operational losses and depict the risk level present in the Bank. Monitoring is based both on financial and technological and operational meters.

- Defining actions lowering the risk

The process of managing activities limiting operational risk is aimed at eliminating or reducing operational risk. The basis for determining risk mitigation measures are the results of analyzes carried out in various operational risk tools (including operational events database, risk indicators, and risk self-assessment).

- Business continuity management (BCM)

Each organizational unit is required to develop and update their business continuity management plans to ensure that critical business processes remain uninterrupted following an unplanned disruption because of unavailability of systems, locations and staff. Business continuity plans must be tested at least annually to ensure that it is possible to restore critical business processes at the required service level and within the agreed timeframe. There are backup locations where critical processes can be restored and continued should an incident occur.

- Information Security

Ensuring an appropriate level of information security and security of the BCM environment is a key aspect of the bank's operations.

in thousands of PLN

At BZ WBK, there is an Information Security Management System that is certified in accordance with ISO / IEC 27001: 2013. Information security management includes supervision over information security matters in the BZ WBK Group's business environment and assessment of specific information security and information systems requirements.

- Insurance

For the purpose of operational risk mitigation, BZ WBK has an insurance scheme in place which covers financial risks, motor, property and professional indemnity insurance.

- Regular reporting to the Risk Management Committee and Supervisory Board

The aim of operational risk reporting is to provide up-to-date adequate information to the management. Operational risk reports cover, inter alia: operational risk incidents and losses, risk indicators and risk mitigants.

The Bank's Information Security Management System has a certificate of compliance with ISO 27001:2013 standard.

Compliance Risk

Legal and regulatory (compliance) risk is defined in line with the Basel Committee recommendation.

As an universal bank providing a wide array of financial services to retail and business customers, a parent company in a capital group providing a number of additional specialised financial services, and as an important member of the Polish banking system, Bank Zachodni WBK is exposed to the legal and compliance risk mainly in the following areas:

- generally applicable laws regarding the employment law, health and safety at work, taxes, accounting, personal data protection etc. which are binding for all enterprises operating in Poland;
- domestic and international (mainly: EU) trade regulations in the area of reporting, prudential standards, functioning on capital and investment market, prevention of money laundering and terrorist financing etc.;
- domestic and international regulations concerning the type of offered products and service delivery methods applied by the bank and the BZ WBK Group (in particular: the legislation on consumer and competition protection, capital markets, financial markets etc.);
- good practice codes and other regulations implemented by the Bank, including in connection with membership in domestic or international trade associations.

Compliance risk is defined as the risk of legal or regulatory sanctions, significant financial loss or negative impact on reputation that the Bank may suffer due to its failure to comply with the law, internal regulations and market standards. Compliance risk consists of the following risk categories:

- regulatory risk,
- conduct risk,
- money laundering and terrorism financing risk,
- reputational risk.

The Bank attaches particular importance to compliance delivered through management and control of compliance risk in the form of controls, independent monitoring and reporting.

The control function is rendered by the so-called three lines of defence. The first line of defence is the operational risk management, the second line consists in on-going vertical verification and vertical testing, while the internal audit units provide the third line of defence.

Compliance duties of the second line of defence in the Bank are rendered by the Compliance Unit (understood as the Compliance Area and the Anti-Money Laundering Department) and other organisational units operating under internal regulations, in particular:

- compliance with employment law – HR Division;
- compliance with company law – Corporate Governance unit
- compliance with health and safety regulations – the Business Partnership Division.
- compliance with taxation law and reporting requirements – Financial Accounting and Control Division;
- compliance with prudential regulations – Risk Management Division.

In July 2017 The Bank's Management Board adopted an amended policy statement on compliance with legal and regulatory obligations, which was approved by the Supervisory Board. The policy provides the Compliance Area together with Anti-Money Laundering Department forms Compliance Unit operating within the Legal and Compliance Division, with the relevant mandate to support senior managers in effective management of the compliance risk. The Compliance Area escalates all issues to the Risk Management Committee and Audit and Compliance Committee of the Supervisory Board. Both Committees ensure compliance with regulatory obligations and approve internal control rules and the Policy framework as well as provide necessary resources for the Compliance Unit, so that the Compliance Unit may operate independently from business units and has relevant resources to perform its tasks.

in thousands of PLN

The Audit and Compliance Committee regularly reviews key compliance issues identified by the Compliance Unit:

- as part of monitoring of new products;
- as part of compliance monitoring;
- as part of the monitoring of proprietary transactions effected by employees;
- based on the information on regulators' activity;
- as part of the review of upcoming legislative initiatives;
- as part of the review of anti-money laundering initiatives;
- as part of the review of ethical issues;
- as part of the review of customers' complaints.

The Compliance Unit's tasks are delivered through:

- independent identification, assessment and monitoring of compliance risk that the Bank is exposed to (with the focus on new products and services, prevention of money laundering and terrorist financing, protection of confidential information, conflicts of interest or private account shares dealing by employees);
- prevention of using the financial system for money laundering and terrorist financing;
- providing advice and reporting to the Risk Management Committee, bank's Management Board and Audit and Compliance Committee on the effectiveness of the processes established to ensure compliance with laws and regulations within its area of responsibility;
- publication of policies and procedures, providing the management and staff with guidance on compliance risk and adequate risk management policies and procedures;
- centralisation of contacts with market regulators (KNF, UOKiK, GIIF, GIODO),
- centralisation of the approval of new products;
- coordination and support for compliance processes regarding the model of sale of investment products and MiFID Directive;
- strengthening of the principles regarding ethical business conduct as well as health and safety at work, as well as building the corporate governance culture in the organisation.

Apart from the aforementioned activities, the Compliance Unit actively cooperates with the Communications, Marketing and Quality Management Area in terms of managing of the reputational risk defined as the risk of deterioration of the Bank's and Santander Group's image perceived by the Bank's and Group's customers, shareholders and communities arising from materialisation of other risks, including individual types of compliance risk.

The Bank also has specialised committees supporting the management of the compliance risk in specific areas. These committees consist of the representatives of key business units and risk management units who are competent and duly authorised to make informed decisions and provide high-quality advice. The Compliance Area together with Anti-Money Laundering Department coordinate and support the work of individual committees which are chaired by the Management Board member in charge of the Legal and Compliance Division. These committees include:

- Compliance Committee;
- Product Marketing and Monitoring Committee;
- Volcker Local Steering Committee;
- Anti-Money Laundering and Terrorism Financing Committee;
- Business Ethics Commission.

In 2017, the Compliance Unit worked on adapting the Bank to the Regulation of the Minister of Development and Finance of 6 March 2017 on the risk management system and the internal control system, remuneration policy and detailed method of internal capital estimation in banks and KNF Recommendation H issued in April 2017.

in thousands of PLN

4. Capital Management

Introduction

It is the policy of the Bank Zachodni WBK to maintain the level of capital adequate to the type and scale of operations and the level of risk. The level of own funds required to ensure safe operations of Bank Zachodni WBK and capital requirements estimated for the unexpected loss is determined in accordance with the CRD IV / CRR package. The package consists of Regulation (EU) No 575/2013 of the European Parliament and of the Council of 26 June 2013 on prudential requirements for credit institutions and investment firms and amending Regulation (EU) No 648/2012 (CRR) and Directive 2013/36/EU of the European Parliament and of the Council of 26 June 2013 on access to the activity of credit institutions and the prudential supervision of credit institutions and investment firms, amending Directive 2002/87/EC and repealing Directives 2006/48/EC and 2006/49/EC (CRD IV), which became effective on 1 January 2014 by the decision of the European Parliament and the European Banking Authority (EBA). These requirements reflect the recommendations of the Polish Financial Supervision Authority (KNF) regarding the use of national options and a higher risk weight for exposures secured with mortgages on properties, including the exposures secured with a mortgage on a residential property, where the principal instalment or the interest instalment amount depends on fluctuations of exchange rates of currencies other than the currency of the debtor's income, which have a risk weight of 150%, and office property or other commercial properties located in Poland, which have a risk weight of 100%.

The Management Board is accountable for capital management, calculation and maintenance processes, including assessment of capital adequacy vis a vis different economic conditions and evaluations of stress tests results and their impact on internal capital and capital adequacy. Responsibility for general oversight over estimation of internal capital rests with the Supervisory Board.

The Management Board delegated on-going capital management to Capital Committee. Capital Committee conducts regular assessment of capital adequacy of the Bank, also in extreme conditions, monitors the actual and required capital levels and initiates transactions affecting these levels (e.g. by recommending the value of dividends to be paid). The Credit Committee is the first body in the Bank to define capital policy and rules for assessment of capital adequacy for the Bank. Any ultimate decisions regarding increase or decrease of capital are taken by relevant authorities of the Bank in accordance with the applicable law and the Bank's Statutes.

Pursuant to the bank's information strategy, details about the level of own funds and capital requirements are presented in the annual report entitled "Information on capital adequacy of the bank and BZ WBK Group as at 31.12.2017".

In 2017, Bank Zachodni WBK met all regulatory requirements regarding capital management.

Capital Policy

Pursuant to CRR, institutions must at all times satisfy the following own funds requirements:

- a Common Equity Tier 1 capital ratio of 4.5%;
- a Tier 1 capital ratio of 6%;
- a total capital ratio of 8%.

As at 31.12.2017, the minimum capital ratios of the Bank satisfying the regulatory recommendations and additional own fund requirements under Pillar 2 were as follows:

- a Tier 1 capital ratio of 11.16%;
- a total capital ratio of Bank Zachodni WBK of 14.29%.

The above-mentioned capital ratios take into account the KNF recommendation on an additional capital requirement related to home mortgages and an additional capital buffer in connection with the identification of Bank Zachodni WBK as other systemically important institution, plus a conservation buffer.

Pursuant to the KNF decisions of 15 December 2017 and 20 November 2017, Bank Zachodni WBK Group and Bank Zachodni WBK maintain own funds to cover an additional capital requirement for risk attached to foreign currency home mortgages for households. As at 31 December 2017, the buffer was set at 0.54 p.p. above the total capital ratio for Bank Zachodni WBK. The buffer includes at least 75% of Tier 1 capital (which corresponds to the capital requirement of 0.41 p.p. above Tier 1 capital ratio for Bank Zachodni WBK) and at least 56% of the Common Equity Tier 1 capital (which corresponds to the capital requirement of 0.30 p.p. above the Common Equity Tier 1 capital for Bank Zachodni WBK).

The Act of 5 August 2015 on macroprudential oversight of the financial system and crisis management in the financial sector transposes CRD IV into the Polish law with regard to, among other things, additional capital buffers to be maintained by banks. As of 1 January 2016, the minimum capital ratios for the banking sector in Poland will be increased by 1.25 p.p. due to introduction of a conservation buffer. In line with the CRR adaptation, this buffer should reach the level of 2.5 p.p. in 2019.

On 4.10.2017, KNF identified Bank Zachodni WBK as other systemically important institution and imposed an additional capital buffer of 0.5 p.p.

in thousands of PLN

From 01.01.2018, Bank Zachodni WBK will have to comply with the systemic risk buffer of 300 p.p. and the conservation buffer of 1.875 p.p., which in turn will affect the minimum ratios for the bank, i.e.:

- a Tier 1 capital ratio of 11.79%;
- a total capital ratio of 13.92%.

Regulatory Capital

The capital requirement for Bank Zachodni WBK Group is determined in accordance with Part 3 of CRR, which formed a legal basis as at 31.12.2017.

Bank Zachodni WBK uses the standardised approach to calculate the capital requirement for credit risk, market risk and operational risk. According to this approach, the total capital requirement for credit risk is calculated as the sum of risk-weighted exposures multiplied by 8%. The exposure value for these assets is equal to the balance sheet total, while the value of off-balance sheet liabilities corresponds to their balance sheet equivalent. Risk-weighted exposures are calculated by means of applying risk weights to all exposures in accordance with the CRR.

The tables below show capital requirement for the Bank as of 31.12.2017 and 31.12.2016.

	31.12.2017	31.12.2016
I Total Capital requirement (Ia + Ib + Ic + Id), of which:	7 542 254	7 068 621
Ia - due to credit risk & counterparty credit risk	6 606 686	6 183 425
Ib - due to market risk	120 618	103 644
Ic - due to credit valuation adjustment risk	38 337	41 192
Id - due to operational risk	776 613	740 360
II Total own funds*	20 930 984	18 078 713
III Reductions	3 067 603	3 481 785
IV Own funds after reductions (II-III)	17 863 381	14 596 928
V CAD [IV/(I*12.5)]	18,95%	16,52%
VI Tier I ratio	17,37%	16,08%

* On 30.09.2017, the bank included current year profit of PLN 519,865 k for the period between 1.01.2017 and 30.06.2017 to own funds as permitted by KNF.

Internal Capital

Notwithstanding the regulatory methods for measuring capital requirements, Bank Zachodni WBK carries out an independent assessment of current and future capital adequacy as part of the internal capital adequacy process (ICAAP). The purpose of the process is to ensure that the level and nature of own funds guarantee the solvency and stability of the bank's and the Group's operations.

The capital adequacy assessment is one of the fundamental elements of the Bank's strategy, the process of defining risk appetite and the process of planning.

The Bank uses assessment models based on the statistical loss estimation for measurable risks, such as credit risk, market risk and operational risk and its own assessment of capital requirements for other material risks not covered by the model, e.g. reputational risk and compliance risk.

The internal capital is estimated on the basis of risk parameters including the probability of default of BZ WBK customers (PD - probability of default) and loss given default (LGD loss given default).

Bank Zachodni WBK performs an internal assessment of capital requirements, including under stressed conditions, taking into account different macroeconomic scenarios.

Internal capital estimation models are assessed and reviewed annually to adjust them to the scale and profile of the Bank's business and to take account of any new risks and the management judgement.

The review and assessment is the responsibility of the Bank's risk management committees, including: Capital Committee and the Models and Methodology Panel, which is part of the Risk Management Forum.

Subordinated liabilities

In 2016, the bank amended the agreement under which subordinated registered bonds were issued on 5.08.2010 and taken up by the European Bank for Reconstruction and Development. The amendments included the extension of maturity until 5.08.2025, among other things. Pursuant to the KNF decision of 18.05.2016, the foregoing subordinated bonds of EUR 100m were allocated to the Tier 2 capital.

in thousands of PLN

On 2 December 2016, the bank issued bonds worth EUR 120m as part of its strategy aimed at increasing Tier 2 capital. On 24 February 2017, the bank was granted consent from the KNF to allocate the above bonds to Tier 2 capital.

Furthermore, on 22 May 2017, the bank issued additional subordinated bonds with a nominal value of EUR 137.1m. Pursuant to the KNF decision of 19 October 2017, these instruments were allocated to Tier 2 capital.

Detailed information on subordinated liabilities is presented in Note 32.

5. Net interest income

	01.01.2017- 31.12.2017	01.01.2016- 31.12.2016
Interest income		
Loans and advances to enterprises	1 654 877	1 607 575
Loans and advances to individuals, of which:	2 140 362	1 922 895
<i>Home mortgage loans</i>	986 586	842 497
Debt securities incl.:	609 508	576 044
<i>Investment portfolio available for sale</i>	575 907	543 738
<i>Trading portfolio</i>	33 601	32 306
Loans and advances to banks	60 405	63 020
Public sector	6 289	6 881
Reverse repo transactions	27 342	9 149
Interest recorded on hedging IRS	204 404	284 353
Total	4 703 187	4 469 917
Interest expenses		
Deposits from individuals	(433 880)	(495 924)
Deposits from enterprises	(294 514)	(337 316)
Repo transactions	(48 361)	(30 571)
Deposits from public sector	(51 277)	(41 627)
Deposits from banks	(16 486)	(18 999)
Subordinated liabilities and issue of securities	(73 120)	(65 040)
Total	(917 638)	(989 477)
Net interest income	3 785 549	3 480 440

As at 31.12.2017 net interest income includes interest on impaired loans of PLN 167,387 k (as at 31.12.2016 - PLN 192,462 k).

in thousands of PLN

6. Net fee and commission income

	01.01.2017- 31.12.2017	01.01.2016- 31.12.2016
Fee and commission income		
eBusiness & payments	627 961	579 525
Current accounts and money transfer	329 905	329 318
Asset management fees	3 637	4 268
Foreign exchange commissions	346 056	320 003
Credit commissions	247 099	205 485
Insurance commissions	69 397	93 301
Brokerage activities	88 166	71 627
Credit cards	88 275	85 036
Off-balance sheet guarantee commissions	62 396	65 579
Issue arrangement fees	14 865	15 212
Distribution fees	163 891	129 582
Other commissions	6 838	5 170
Total	2 048 486	1 904 106
Fee and commission expenses		
eBusiness & payments	(225 491)	(201 328)
Credit cards	(15 469)	(17 868)
Brokerage activities	(11 175)	(10 368)
Insurance commissions	(7 924)	(8 280)
Finance lease commissions	(135)	(66)
Commissions paid to credit agents	(8 647)	(12 471)
Other	(52 997)	(48 990)
Total	(321 838)	(299 371)
Net fee and commission income	1 726 648	1 604 735

Included above is fee and commission income on credits, credit cards and off-balance sheet guarantee commissions of PLN 397,770 k (2016: PLN 356,100 k) and fee and commission expenses on credits cards and paid to credit agents of PLN (24,116) k (2016: PLN (30,339) k) (other than fees included in determining the effective interest rate), relating to financial assets and liabilities not carried at fair value through profit or loss.

7. Dividend income

	01.01.2017- 31.12.2017	01.01.2016- 31.12.2016
Dividend income		
Dividends from subsidiaries and associates	222 791	343 770
Dividends from equity financial assets available for sale	76 181	94 987
Dividends income from equity financial assets at fair value through profit or loss	546	531
Total	299 518	439 288

in thousands of PLN

8. Net trading income and revaluation

	01.01.2017- 31.12.2017	01.01.2016- 31.12.2016
Net trading income and revaluation		
Derivative instruments and interbank fx transactions	149 114	248 025
Other FX related income	35 854	12 176
Profit on equity instruments	4 265	(1 710)
Profit on debt instruments	(6 004)	7 880
Total	183 229	266 371

Net trading income and revaluation includes the change of the value of derivative instruments in the amount of PLN (10,354) k for 2017 and PLN (5,952) k for 2016.

The amounts included CVA and DVA adjustments which in 2017 and 2016 totaled PLN (11,572) k and PLN(2,748) k respectively.

9. Gains (losses) from other financial securities

	01.01.2017- 31.12.2017	01.01.2016- 31.12.2016
Gains (losses) from other financial securities		
Profit on sale of equity shares available for sale	26 420	307 666
Profit on sale of debt securities available for sale	20 549	92 772
Charge due to impairment losses	-	(1 408)
Total profit (losses) on financial instruments	46 969	399 030
Change in fair value of hedging instruments	23 760	57 503
Change in fair value of underlying hedged positions	(26 115)	(55 344)
Total profit (losses) on hedging and hedged instruments	(2 355)	2 159
Total	44 614	401 189

On 21.06.2016, Visa Inc. announced the completion of its acquisition of Visa Europe Limited. As a result, BZ WBK received:

- EUR 49,974,289 in cash,
- 18,092 series C preference shares of Visa Inc.

Furthermore, the earn-out of EUR 1.12bn payable to all transaction participants was settled. The share of Bank Zachodni WBK in the above amount is 0.3839946336%. The earn-out payable to the Bank may be adjusted within three years of the transaction date in the circumstances stipulated in the agreement.

In 2016, the total profit made by Bank Zachodni WBK on the above transaction was PLN 305,865 k and was recognised under "Gains from other financial securities" in the income statement.

10. Other operating income

	01.01.2017- 31.12.2017	01.01.2016- 31.12.2016
Other operating income		
Income on sale of services	20 612	19 428
Reimbursements of BGF charges	433	54 215
Release of provision for legal cases and other assets	5 430	12 788
Settlements of leasing agreements	944	2 907
Recovery of other receivables	5 598	6 876
Profit on sale or liquidation of fixed assets, intangible assets and assets for disposal	12 314	7 026
Received compensations penalties and fines	821	1 047
Other income from legal cases	24 238	-
Other	13 373	15 178
Total	83 763	119 465

in thousands of PLN

* Following the change in the calculation of contributions to the Bank Guarantee Fund as a result of the introduction of the Bank Guarantee Fund Act of 10 June 2016, the bank changed the method of settlement and therefore the presentation which is now disclosed under fee and commission income.

11. Impairment losses on loans and advances

	01.01.2017- 31.12.2017	01.01.2016- 31.12.2016
Impairment losses on loans and advances		
Collective and individual impairment charge	(512 966)	(609 608)
Incurred but not reported losses charge	(28 111)	(143)
Recoveries of loans previously written off	(2 103)	(1 133)
Off-balance sheet credit related facilities	2 805	27 405
Total	(540 375)	(583 479)

12. Employee costs

	01.01.2017- 31.12.2017	01.01.2016- 31.12.2016
Employee costs		
Salaries and bonuses	(1 042 255)	(1 010 647)
Obligatory salary related costs	(174 422)	(165 456)
Staff benefits costs	(30 252)	(28 431)
Professional trainings	(14 170)	(15 163)
Retirement fund, holiday provisions and other employee costs	6 095	(1 073)
Total	(1 255 004)	(1 220 770)

13. General and administrative expenses

	01.01.2017- 31.12.2017	01.01.2016- 31.12.2016
General and administrative expenses		
Maintenance and rentals of premises	(289 413)	(299 118)
Marketing and representation	(69 549)	(86 624)
IT systems costs	(141 664)	(148 335)
Bank Guarantee Fund, Polish Financial Supervision Authority and National Depository for Securities	(195 838)	(246 326)
Postal and telecommunication costs	(36 725)	(32 642)
Consulting fees	(55 354)	(46 943)
Cars, transport expenses, carriage of cash	(58 546)	(60 089)
Other external services	(82 207)	(75 771)
Stationery, cards, cheques etc.	(17 705)	(20 708)
Sundry taxes	(28 025)	(26 661)
Data transmission	(9 327)	(12 378)
KIR, SWIFT settlements	(25 986)	(25 106)
Security costs	(23 976)	(24 375)
Costs of repairs	(13 210)	(15 942)
Other	(20 668)	(18 421)
Total	(1 068 193)	(1 139 439)

in thousands of PLN

14. Other operating expenses

	01.01.2017- 31.12.2017	01.01.2016- 31.12.2016
Other operating expenses		
Charge of provisions for legal cases and other assets	(42 144)	(93 813)
Impairment loss on property, plant, equipment and intangible assets	(8 342)	(12 359)
Costs of purchased services	(8 177)	(2 775)
Other membership fees	(783)	(675)
Paid compensations, penalties and fines	(2 883)	(1 932)
Donations paid	(4 670)	(4 260)
Other	(14 191)	(12 543)
Total	(81 190)	(128 357)

15. Corporate income tax

	01.01.2017- 31.12.2017	01.01.2016- 31.12.2016
Corporate income tax		
Current tax charge	(459 896)	(569 087)
Deferred tax	(139 447)	(6 806)
Adjustments from previous years	169	8 365
Total	(599 174)	(567 528)

	01.01.2017- 31.12.2017	01.01.2016- 31.12.2016
Corporate total tax charge information		
Profit before tax	2 515 330	2 649 248
Tax rate	19%	19%
Tax calculated at the tax rate	(477 913)	(503 357)
Non-tax-deductible expenses	(8 403)	(20 417)
The fee to the Bank Guarantee Fund	(34 971)	(13 472)
Tax on financial institutions	(73 717)	(67 654)
Sale of receivables	(52 237)	(43 223)
Non-taxable income (dividends)	56 753	83 439
Non-tax deductible bad debt provisions	(10 970)	(8 023)
Adjustment of prior year tax	169	8 385
Other	2 115	(3 206)
Total income tax expense	(599 174)	(567 528)

	01.01.2017- 31.12.2017	01.01.2016- 31.12.2016
Deferred tax recognised directly in equity		
Relating to equity securities available-for-sale	(132 797)	(124 073)
Relating to debt securities available-for-sale	(55 657)	33 645
Relating to cash flow hedging activity	21 446	26 173
Relating to valuation of defined benefit plans	(75)	(1 835)
Total	(167 083)	(66 090)

in thousands of PLN

16. Earnings per share

Earnings per share (PLN/share)	01.01.2017- 31.12.2017	01.01.2016- 31.12.2016
Profit attributable to ordinary shares	1 916 156	2 081 720
Weighted average number of ordinary shares	99 275 197	99 234 534
Earnings per share (PLN)	19,30	20,98
Profit attributable to ordinary shares	1 916 156	2 081 720
Weighted average number of ordinary shares	99 275 197	99 234 534
Weighted average number of potential ordinary shares *	187 456	156 947
Diluted earnings per share (PLN)	19,27	20,94

* The weighted average number of potential ordinary shares takes into account the number of share options granted under the incentive scheme described in Note 49.

17. Cash and balances with central banks

Cash and balances with central banks	31.12.2017	31.12.2016
Cash	2 249 508	2 114 542
Current accounts in central banks	1 857 293	2 535 091
Term deposits	8 000	47 001
Total	4 114 801	4 696 634

Bank Zachodni WBK holds an obligatory reserve on a current account in the National Bank of Poland. The figure is calculated at a fixed percentage of the monthly average balance of the customers' deposits, which was 3.5% as at 31.12.2017 and 31.12.2016.

In accordance with the applicable regulations, the amount of the calculated provision is reduced by the equivalent of EUR 500 k.

18. Loans and advances to banks

Loans and advances to banks	31.12.2017	31.12.2016
Loans and advances	851 061	798 068
Current accounts, other	1 161 057	2 510 734
Total	2 012 118	3 308 802

Fair value of loans and advances to banks is presented in Note 41.

in thousands of PLN

19. Financial assets and liabilities held for trading

Financial assets and liabilities held for trading	31.12.2017		31.12.2016	
	Assets	Liabilities	Assets	Liabilities
Trading derivatives	1 231 990	1 263 859	1 876 563	1 729 840
Interest rate operations	312 783	276 635	971 978	899 009
Forward	-	68	6	20
Options	13 211	13 226	17 744	17 743
IRS	297 054	261 776	947 336	874 150
FRA	2 518	1 565	6 892	7 096
Transactions on equity instruments	6 053	6 053	12 032	12 032
Options	6 053	6 053	12 032	12 032
FX operations	913 154	981 171	892 553	818 799
CIRS	282 186	275 786	226 334	245 130
Forward	41 175	160 814	69 838	61 693
FX Swap	493 265	447 589	429 196	352 967
Spot	1 360	1 832	1 561	2 041
Options	95 168	95 150	156 718	156 718
Other	-	-	8 906	250
Debt and equity securities	2 189 557	-	1 321 624	-
Debt securities	2 174 096	-	1 312 589	-
Government securities:	2 170 048	-	612 233	-
- bonds	2 170 048	-	612 233	-
Central Bank securities:	-	-	699 883	-
- bills	-	-	699 883	-
Commercial securities:	4 048	-	473	-
- bonds	4 048	-	473	-
Equity securities:	15 461	-	9 035	-
- listed	15 461	-	9 035	-
Short sale	-	-	-	80 129
Total financial assets/liabilities	3 421 547	1 263 859	3 198 187	1 809 969

Financial assets and liabilities held for trading - trading derivatives include the change in the value of counterparty risk in the amount of PLN (28) k as at 31.12.2017 and PLN 9,373 k as at 31.12.2016.

Interest income from debt instruments and other fixed rate instruments is disclosed under "interest income".

Profit and loss from fair value changes of financial assets and liabilities held for trading are disclosed under net trading income and revaluation in the consolidated income statement.

All financial assets measured at fair value through profit and loss are assigned to this category due to the trading character of the transactions. At 31.12.2017 and in comparable period there were no cases of instruments designated to financial assets measured at fair value through profit and loss at initial recognition.

Offsetting financial assets and financial liabilities

In accordance with IFRS 7, the information below refers only to financial assets and financial liabilities arising from forward and derivative transactions effected under master agreements such as ISDA Master Agreement or other master agreements providing for the possibility to terminate and settle the transaction with a counterparty in the event of default on the basis of a net amount of mutual receivables and payables.

The Bank has no right to set off financial assets and liabilities in the financial statements. The table below presents fair value amounts of derivative instruments (both held for trading and designated as hedging instruments under hedge accounting) and cash collateral covered by mandate agreements providing for the right of set-off under specific circumstances. The maximum amounts of compensations other than those resulting from collaterals based on framework contracts have been presented separately.

in thousands of PLN

Offsetting financial assets and financial liabilities	31.12.2017		31.12.2016	
	Financial assets	Financial liabilities	Financial assets	Financial liabilities
Fair value measurements of derivative instruments	1 231 990	1 263 859	1 934 442	3 691 420
Value of collateral accepted/provided	(302 711)	(268 306)	(249 791)	(2 131 485)
Assets and liabilities subject to set-offs under a mandate agreement	929 279	995 553	1 684 651	1 559 935
Maximum amount of potential set-off	(388 627)	(388 627)	(924 984)	(924 984)
Assets and liabilities subject to set-offs under a mandate agreement, taking into account the maximum amount of potential set-off	540 652	606 926	759 667	634 951

The table below presents derivatives' nominal values.

Derivatives' nominal values	31.12.2017	31.12.2016
1. Term derivatives (hedging)	23 570 504	30 178 193
a) Single-currency interest rate swap	2 404 709	2 282 240
b) Macro cash flow hedge -purchased (IRS)	1 575 000	2 242 000
c) Macro cash flow hedge -purchased (CIRS)	9 707 988	12 013 523
d) Macro cash flow hedge -sold (CIRS)	9 882 807	13 640 430
2. Term derivatives (trading)	285 338 721	291 909 465
a) Interest rate operations	170 594 604	172 058 392
Single-currency interest rate swap	158 895 602	148 034 909
FRA - purchased amounts	3 260 000	16 680 000
Options	8 370 402	7 314 133
Forward- purchased amounts	-	27 090
Forward- sold amounts	68 600	2 260
b) FX operations	114 744 117	119 851 073
FX swap – purchased amounts	29 904 524	30 143 163
FX swap – sold amounts	29 837 481	30 025 420
Forward- purchased amounts	8 226 882	5 580 260
Forward- sold amounts	8 393 420	5 620 242
Cross-currency interest rate swap – purchased amounts	10 992 948	13 205 081
Cross-currency interest rate swap – sold amounts	10 991 112	13 232 885
FX options -purchased CALL	4 036 440	5 398 974
FX options -purchased PUT	4 162 435	5 623 037
FX options -sold CALL	4 036 440	5 398 974
FX options -sold PUT	4 162 435	5 623 037
3. Currency transactions- spot	2 893 238	1 540 212
Spot-purchased	1 446 436	769 621
Spot-sold	1 446 802	770 591
4. Transactions on equity financial instruments	817 734	1 335 679
Derivatives contract- purchased	401 987	664 431
Derivatives contract - sold	415 747	671 248
Total	312 620 197	324 963 549

In the case of single-currency transactions (IRS, FRA, non-FX options) only purchased amounts are presented.

20. Hedging derivatives

Hedging derivatives	31.12.2017		31.12.2016	
	Assets	Liabilities	Assets	Liabilities
Derivatives hedging fair value	2 283	115 496	3 232	139 973
Derivatives hedging cash flow	144 441	463 302	63 555	1 821 855
Total hedging derivatives	146 724	578 798	66 787	1 961 828

Hedging derivatives – derivatives hedging cash flow include value adjustments day first profit or loss for start forward CIRS transactions in the amount of PLN (9,613) k as at 31.12.2017 and (10,665) k as at 31.12.2016.

For the valuation of hedging transactions, Group uses a valuation model classified to the Level II of fair value, in which data used for valuation are based on observable market parameters (directly or indirectly). Bank treats differences that arise in the initial valuation it

in thousands of PLN

as the Day 1 profit or loss and amortises it in time and indicates the valuation effect in the profit and loss account. Amortisation of adjustment to the valuation of day 1 is recognized in Net trading income and revaluation.

21. Loans and advances to customers

Loans and advances to customers	31.12.2017	31.12.2016
Loans and advances to enterprises	49 011 673	46 811 514
Loans and advances to individuals, of which:	44 322 763	42 995 955
<i>Home mortgage loans</i>	33 723 865	32 711 667
Loans and advances to public sector	227 389	195 752
Other	7 304	181 596
Gross receivables	93 569 128	90 184 817
Allowance for impairment	(3 032 125)	(3 082 427)
Total	90 537 003	87 102 390

As at 31.12.2017 the fair value adjustment due to hedged risk on individual loans was PLN 3,555 k.

Detailed currency analysis of mortgage loans is presented in the consolidated financial statements of Bank Zachodni WBK Group for 2017 released on 13.02.2018.

Fair value of "Loans and advances to customers" is disclosed in Note 41.

Movements on impairment losses on loans and advances to customers	31.12.2017	31.12.2016
Individual and collective impairment		
As at the beginning of the period	(2 740 861)	(3 084 165)
Charge/write back of current period	(512 966)	(609 609)
Write off/Sale of receivables	570 092	938 201
Transfer	(16 684)	26 892
F/X differences	25 657	(12 180)
Balance at the end of the period	(2 674 762)	(2 740 861)
IBNR		
As at the beginning of the period	(341 566)	(340 429)
Charge/write back of current period	(28 111)	(143)
Sale of receivables	3 429	3 182
Transfer	1 204	-
F/X differences	7 681	(4 176)
Balance at the end of the period	(357 363)	(341 566)
Allowance for impairment	(3 032 125)	(3 082 427)

22. Financial assets available for sale

Financial assets available for sale	31.12.2017	31.12.2016
Debt securities	24 889 479	25 467 070
Government securities:	21 419 899	20 472 331
- bonds	21 419 899	20 472 331
Central Bank securities:	1 379 839	2 849 694
- bills	1 379 839	2 849 694
Other securities:	2 089 741	2 145 045
- bonds	2 089 741	2 145 045
Equity securities	894 550	855 291
- listed	-	12 644
- unlisted	894 550	842 647
Total	25 784 029	26 322 361

in thousands of PLN

As at 31.12.2017 fixed interest rate debt securities measured at fair value amount to PLN 16,471,392 k, variable interest rate securities amount to PLN 8,418,087 k.

As at 31.12.2016 fixed interest rate debt securities measured at fair value amount to PLN 18,686,207 k, variable interest rate securities amount to PLN 6,780,863 k.

As at 31.12.2017 fair value adjustment resulting from fair value hedge on available for sale debt securities totaled PLN 107,005 k (as at 31.12.2016 PLN 132,512 k).

Unlisted equity investments classified as available-for-sale for which no active market exists are recognized at cost and tested for impairment or their fair value is assessed based on valuation models. The Bank performs the review of the fair value of its unlisted available-for-sale financial instruments at each balance sheet date.

Fair value of „Financial assets available for sale” is presented in Note 41.

Movements on financial assets available for sale	Financial instruments representing equity rights		Total
	Debt securities		
As at 1 January 2017	25 467 070	855 291	26 322 361
Additions	60 456 329	2 036	60 458 365
Disposals (sale and maturity)	(61 393 423)	(8 691)	(61 402 114)
Fair value adjustment	444 504	45 914	490 418
Movements on interest accrued	30 469	-	30 469
Allowances for impairment	-	-	-
F/X differences	(115 470)	-	(115 470)
As at 31 December 2017	24 889 479	894 550	25 784 029

Movements on financial assets available for sale	Financial instruments representing equity rights		Total
	Debt securities		
As at 1 January 2016	21 471 774	1 104 472	22 576 246
Additions	44 844 381	72 965	44 917 346
Disposals (sale and maturity)	(40 512 751)	(8 616)	(40 521 367)
Fair value adjustment	(446 168)	(312 122)	(758 290)
Movements on interest accrued	57 682	-	57 682
Allowances for impairment	-	(1 408)	(1 408)
F/X differences	52 152	-	52 152
As at 31 December 2016	25 467 070	855 291	26 322 361

23. Investments in subsidiaries and associates

Investments in subsidiaries and associates	31.12.2017	31.12.2016
Subsidiaries	2 340 431	2 340 719
Associates	36 606	36 606
Total	2 377 037	2 377 325

in thousands of PLN

Investments in subsidiaries and associates as at 31.12.2017 *

Name of entity	BZ WBK	BZ WBK	Gieldokracja Sp. z	BZ WBK	Santander	Total
	Inwestycje Sp. z o.o.	Finanse Sp. z o.o.	o.o. in liquidation.	Towarzystwo Funduszy Inwestycyjnych S.A.	Consumer Bank S.A.	
Registered office	Poznań	Poznań	Poznań	Poznań	Wroclaw	
Type of connection	Subsidiary	Subsidiary	Subsidiary	Subsidiary	Subsidiary	
% of holding	100.00	100.00	100.00	50.00	60.00	
Balance sheet value	46 600	130 562	100	6 755	2 156 414	2 340 431
Total assets	42 432	255 407	-	117 631	17 647 014	18 062 484
Own funds of entity, of which:	42 398	248 127	-	85 014	3 190 067	3 565 606
Share capital	100	1 165	-	13 500	520 000	534 765
Other own funds, of which:	42 298	246 962	-	71 514	2 670 067	3 030 841
<i>from previous years</i>	(6 232)	29 445	117	-	270 845	294 175
<i>net profit (loss)</i>	(384)	42 326	(117)	66 503	649 136	757 464
Liabilities of entity	34	7 280	-	32 617	14 456 947	14 496 878
Revenue	(364)	57 051	-	314 031	1 944 552	2 315 270

* unaudited data

Name of entity	Business
BZ WBK Inwestycje Sp. z o.o.	trading in shares of commercial companies as well as other securities; seeking investors for companies
BZ WBK Finanse Sp. z o.o.	centralised management of the bank's subsidiaries: BZ WBK Leasing S.A., BZ WBK Lease S.A., BZ WBK Faktor Sp. z o.o. and BZ WBK F24 S.A.
Gieldokracja Sp. z o.o. in liquidation.	advertising services, educational services related to the capital market, maintenance of internet portals and communication services
BZ WBK Towarzystwo Funduszy Inwestycyjnych S.A.	brokerage activities: managing customer's share portfolios (listed and not listed)
Santander Consumer Bank S.A.	accepting savings and term deposits, granting and taking out loans and advances

Name of associate	Country of incorporation and place of business	The Group's share in capital / voting power		Valuation method	Scope of business
		2017	2016		
BZ WBK - Aviva Towarzystwo Ubezpieczeń na Życie S.A.	Poland	49,00	49,00	Equity method	life insurance
BZ WBK - Aviva Towarzystwo Ubezpieczeń Ogólnych S.A.	Poland	49,00	49,00	Equity method	property and personal insurance

in thousands of PLN

The table below presents condensed financial information regarding associates which have a significant contribution to the Group:

	BZ WBK - Aviva Towarzystwo Ubezpieczeń na Życie S.A.		BZ WBK - Aviva Towarzystwo Ubezpieczeń Ogólnych S.A.	
	2017 *	2016	2017 *	2016
Loans and advances to banks	67 377	44 635	69 888	30 857
Financial assets held for trading	12 079	19 457	1 256	1 230
Financial assets available for sale	318 393	260 392	373 978	348 360
Deferred tax assets	705	646	981	908
Net life insurance assets where the deposit (investment) risk is incurred by the insuring party	387 534	545 539	-	-
Other settlements	22 523	24 512	56 494	42 057
Prepayments	163 842	127 946	-	12 875
Other items	818	1 205	859	1 173
Total assets	973 271	1 024 332	503 456	437 460
Technical insurance provisions	733 747	851 318	164 235	172 589
Reinsurers' share in provisions	(7 444)	(7 322)	(143 055)	(113 294)
Estimated recourses and recoveries (negative value)	-	-	(1 003)	(602)
Other liabilities	136 678	85 565	157 253	105 488
Prepayments and accruals	6 641	2 458	94 618	69 198
Special funds	35	26	33	33
Total liabilities	869 657	932 045	272 081	233 412
INCOME	180 571	201 104	156 972	154 987
Profit (loss) for the period	45 011	37 849	73 173	72 372
Dividends paid to BZ WBK	19 142	10 827	25 719	-

* data are based on estimates of companies

2016 data are based on audit financial report of companies BZ WBK - Aviva Towarzystwo Ubezpieczeń na Życie S.A. and BZ WBK - Aviva Towarzystwo Ubezpieczeń Ogólnych S.A. Data published in Annual Report 2016 were based on estimates of companies. Difference between estimates and real data are irrelevant.

in thousands of PLN

Investments in subsidiaries and associates as at 31.12.2016

Name of entity	BZ WBK			BZ WBK		Santander	Total
	Inwestycje Sp. z o.o.	BZ WBK Finanse Sp. z o.o.	Gieldokracja Sp. z o.o.	Nieruchomości S.A.	BZ WBK Asset Management S.A.	Consumer Bank S.A.	
Registered office	Poznań	Poznań	Poznań	Zakrzewo	Poznań	Wrocław	
Type of connection	Subsidiary	Subsidiary	Subsidiary	Subsidiary	Subsidiary	Subsidiary	
% of holding	100.00	100.00	100.00	99.99	50.00	60.00	
Balance sheet value	46 600	130 097	100	753	6 755	2 156 414	2 340 719
Total assets	61 199	208 106	358	629	85 692	16 386 938	16 742 922
Own funds of entity, of which:	58 652	204 959	334	535	81 414	2 697 829	3 043 723
Share capital	100	1 165	100	750	13 500	520 000	535 615
Other own funds, of which:	58 552	203 794	234	(215)	67 914	2 177 829	2 508 108
<i>from previous years</i>	-	(5 700)	-	(246)	-	236 685	230 739
<i>net profit (loss)</i>	1 467	44 240	85	31	59 585	434 586	539 994
Liabilities of entity	2 547	3 147	24	94	4 278	13 689 109	13 699 199
Revenue	2 110	49 534	497	239	81 137	1 650 974	1 784 491

Name of entity	Business
BZ WBK Inwestycje Sp. z o.o.	trading in shares of commercial companies as well as other securities; seeking investors for companies
BZ WBK Finanse Sp. z o.o.	centralised management of the bank's subsidiaries: BZ WBK Leasing S.A., BZ WBK Lease S.A and BZ WBK Faktor Sp. z o.o.
Gieldokracja Sp. z o.o.	advertising services, educational services related to the capital market, maintenance of internet portals and communication services
BZ WBK Nieruchomości S.A.	organisation of various events, catering and hotel services, agency services
BZ WBK Asset Management S.A.	brokerage activities: managing customer's share portfolios (listed and not listed)
Santander Consumer Bank S.A.	accepting savings and term deposits, granting and taking out loans and advances

in thousands of PLN

24. Intangible assets

Intangible assets Year 2017	Licences, patents etc.	Other	Expenditure on intangible assets	Total
Gross value - beginning of the period	1 334 854	233 428	176 183	1 744 465
Additions from:				
- purchases	-	-	157 194	157 194
- donation	-	-	-	-
- intangible assets taken for use	140 791	-	-	140 791
- transfers	-	-	-	-
Disposals from:				
- liquidation, sale	(44 084)	-	(670)	(44 754)
- intangible assets taken for use	-	-	(140 791)	(140 791)
- transfers	-	-	(2 248)	(2 248)
Gross value - end of the period	1 431 561	233 428	189 668	1 854 657
Accumulated depreciation - beginning of the period	(1 127 440)	(152 717)	-	(1 280 157)
Additions/disposals from:				
- current year amortisation	(133 120)	(25 488)	-	(158 607)
- liquidation, sale	44 084	-	-	44 084
- transfers	-	-	-	-
Write down/Reversal of impairment write down	-	-	-	-
Accumulated depreciation- end of the period	(1 216 476)	(178 205)	-	(1 394 680)
Balance sheet value				
Purchase value	1 431 561	233 428	189 668	1 854 657
Accumulated depreciation	(1 216 476)	(178 205)	-	(1 394 681)
As at 31 December 2017	215 085	55 223	189 668	459 976

in thousands of PLN

Intangible assets Year 2016	Licences, patents etc.	Other	Expenditure on intangible assets	Total
Gross value - beginning of the period	1 257 782	229 370	155 755	1 642 907
Additions from:				
- purchases	-	-	147 398	147 398
- donation	-	-	-	-
- intangible assets taken for use	128 979	4 058	-	133 037
- transfers	-	-	6 174	6 174
Disposals from:				
- liquidation, sale	(51 907)	-	(107)	(52 014)
- intangible assets taken for use	-	-	(133 037)	(133 037)
- transfers	-	-	-	-
Gross value - end of the period	1 334 854	233 428	176 183	1 744 465
Accumulated depreciation - beginning of the period	(1 077 078)	(122 226)	-	(1 199 304)
Additions/disposals from:				
- current year amortisation	(101 753)	(30 491)	-	(132 244)
- liquidation, sale	51 391	-	-	51 391
- transfers	-	-	-	-
Write down/Reversal of impairment write down	-	-	-	-
Accumulated depreciation- end of the period	(1 127 440)	(152 717)	-	(1 280 157)
Balance sheet value				
Purchase value	1 334 854	233 428	176 183	1 744 465
Accumulated depreciation	(1 127 440)	(152 717)	-	(1 280 157)
As at 31 December 2016	207 414	80 711	176 183	464 308

in thousands of PLN

25. Goodwill

As at 31.12.2017 and in the corresponding period, the goodwill covered the following item:

- PLN 1,688,516k - goodwill arising from the merger of Bank Zachodni WBK and Kredyt Bank on 4.01.2013.

In accordance with IFRS 3 the goodwill was calculated as the surplus of the cost of acquisition over the fair value of assets and liabilities acquired.

Test for impairment of goodwill arising from the merger between Bank Zachodni WBK and Kredyt Bank

In 2017 and in the corresponding period, the Bank conducted tests for impairment of goodwill arising from the merger with Kredyt Bank on 4.01.2013. The carrying amount as at 31.12.2017 was PLN 1,688,516 k (the same as at 31.12.2016).

Recoverable amount based on value in use

The recoverable amount of cash-generating units is the higher of fair value less costs of disposal and value in use. Value in use which is higher than the fair value less costs of disposal is measured on the basis of a discounted cash flow model relevant for banks and other financial institutions. The future expected cash flows generated by business segments of Bank Zachodni WBK are in line with the 3-year financial projections of the Bank's management for 2018-2020.

Taking into account the stability of Bank Zachodni WBK and sustainable financial performance, and comparing the value in use with the carrying amount of the cash-generating unit, no impairment was identified.

Key assumptions for measuring value in use

For the purposes of goodwill impairment testing Bank applies the following allocation of goodwill to historical business segments. The allocation results from the initial recognition as at acquisition date:

	Retail Banking	Business and Corporate Banking	Global Banking and Markets	ALM and Centre	Total
Goodwill	781 308	480 946	299 552	126 710	1 688 516

Due to accepted valuation model, assumptions used to determine the value in use for the individual segments are the same.

Financial projection

The financial projection for 2018-2020 was prepared taking into account strategic and operational plans for 2018-2020 and available macroeconomic and market forecasts. According to the macroeconomic forecasts for 2018-2020 underlying the goodwill impairment test, the average GDP growth is projected at 2.5%. Interest rates are expected to continue at the low level at least until the end of 2018 and grow thereafter. The financial projection assumes the continued expansion of products and services, with a special focus on an increase in the main product lines and on services to retail and SME customers who use financing and savings products and transactional banking services.

Discount rate

Depending on the time horizon, the discount rate in the dividend discount model is 8.5% – 9.0%. The discount rate equal to the rate of return was calculated on the basis of the Capital Assets Pricing Model, taking into account: risk-free rate, beta coefficient for BZ WBK published on the Bloomberg site and market risk premium. The risk-free rate for the next three years ranges from 3.8% to 4.16% and is based on the yield of treasury securities commensurate with the discount period. Cash flows beyond the 3-year financial projection are discounted using predicted yield of 10-year treasury securities, after the third year of detailed projection at 4.27%. As at the end of 2017, market risk premium was estimated at 5.5%.

Growth rate in the period beyond the financial projections

The extrapolation of cash flows exceeding the 3-year period of financial projections (residual value) was based on an annual growth rate of 2.5%, i.e. the projected long-term GDP growth rate.

Minimum solvency ratio imposed by the regulator

An increase in the required capital amount results in a decrease in the amount of capital available for distribution as part of the test. On 01.01.2018, the following legal provisions take effect: higher capital requirements for 50% profit distribution, additional capital requirements for risk attached to mortgage loans (0.54 p.p.), additional conservation buffer of 1.25 p.p., buffer of other systemically important institution of 0.5 p.p. (determined individually by the KNF) and systemic risk buffer of 3.0 p.p., increased by 1.5 p.p. In

in thousands of PLN

addition, banks are required to adjust dividend yield depending on the share of FX home loans in the credit portfolio. All the above factors have a negative impact on the capital available for distribution and, consequently, on the results of the goodwill impairment test.

As a consequence, the minimum solvency ratio imposed by the KNF as a criterion for max 50% profit distribution is 14.79%.

Whereas higher capital requirements ensure stability and safety of Bank Zachodni WBK as they increase the capital base, they reduce the amount of dividends attributable to the shareholders, which in turn affects the value in use of the cash-generating unit.

As at 31 December 2017, no goodwill impairment was identified.

26. Property, plant and equipment

Property, plant & equipment Year 2017	Land and buildings	Financial leaseback - land and buildings	Equipment	Transportation means	Other fixed assets	Financial leaseback - expenditure	Capital expenditures	Total
Gross value - beginning of the period	841 324	38 976	624 946	90 187	241 906	20 328	129 226	1 986 893
Additions from:								
- purchases	-	-	-	-	-	57 661	111 316	168 977
- leasing	-	-	-	8 703	-	-	-	8 703
- fixed assets taken for use	24 606	-	117 206	-	13 203	-	-	155 015
- transfers	-	-	113	-	-	-	2 248	2 361
Disposals from:								
- sale, liquidation, donation	(39 553)	-	(26 164)	(629)	(28 551)	-	(225)	(95 122)
- fixed assets taken for use	-	-	-	-	-	-	(155 015)	(155 015)
- transfers	-	-	-	(9 416)	(63)	-	(43)	(9 522)
Gross value - end of the period	826 377	38 976	716 101	88 845	226 495	77 989	87 507	2 062 290
Accumulated depreciation - beginning of the period	(562 449)	(1 618)	(413 647)	(20 510)	(208 803)	-	-	(1 207 027)
Additions/disposals from:								
- current year amortisation	(27 198)	(971)	(65 876)	(11 953)	(10 349)	-	-	(116 347)
- sale, liquidation, donation	31 215	-	26 152	629	27 900	-	-	85 896
- transfers	-	-	(76)	5 112	26	-	-	5 062
Write down/Reversal of impairment write down	(8 342)	-	-	-	-	-	-	(8 342)
Accumulated depreciation- end of the period	(566 774)	(2 589)	(453 447)	(26 722)	(191 226)	-	-	(1 240 758)
Balance sheet value								
Purchase value	826 377	38 976	716 101	88 845	226 495	77 989	87 507	2 062 290
Accumulated depreciation	(566 774)	(2 589)	(453 447)	(26 722)	(191 226)	-	-	(1 240 758)
As at 31 December 2017	259 603	36 387	262 654	62 123	35 269	77 989	87 507	821 532

in thousands of PLN

Property, plant & equipment Year 2016	Land and buildings	Financial leaseback - land and buildings	Equipment	Transportation means	Other fixed assets	Financial leaseback - expenditure	Capital expenditures	Total
Gross value - beginning of the period	865 320	39 480	555 834	85 504	276 846	3 067	127 795	1 953 846
Additions from:								
- purchases	-	-	-	-	-	17 261	131 732	148 993
- leasing	-	-	-	30 480	-	-	-	30 480
- fixed assets taken for use	24 068	-	91 122	-	8 941	-	-	124 131
- transfers	59	-	18 728	-	9	-	-	18 796
Disposals from:								
- sale, liquidation, donation	(48 123)	-	(40 738)	(348)	(25 162)	-	-	(114 371)
- fixed assets taken for use	-	-	-	-	-	-	(124 131)	(124 131)
- transfers	-	(504)	-	(25 449)	(18 728)	-	(6 170)	(50 851)
Gross value - end of the period	841 324	38 976	624 946	90 187	241 906	20 328	129 226	1 986 893
Accumulated depreciation - beginning of the period	(561 469)	(660)	(386 334)	(24 386)	(238 752)	-	-	(1 211 601)
Additions/disposals from:								
- current year amortisation	(25 920)	(982)	(52 656)	(12 901)	(9 414)	-	-	(101 873)
- sale, liquidation, donation	37 299	-	40 709	315	24 007	-	-	102 330
- transfers	-	24	(15 366)	16 462	15 356	-	-	16 476
Write down/Reversal of impairment write down	(12 359)	-	-	-	-	-	-	(12 359)
Accumulated depreciation- end of the period	(562 449)	(1 618)	(413 647)	(20 510)	(208 803)	-	-	(1 207 027)
Balance sheet value								
Purchase value	841 324	38 976	624 946	90 187	241 906	20 328	129 226	1 986 893
Accumulated depreciation	(562 449)	(1 618)	(413 647)	(20 510)	(208 803)	-	-	(1 207 027)
As at 31 December 2016	278 875	37 358	211 299	69 677	33 103	20 328	129 226	779 866

27. Net deferred tax assets

Deferred tax assets	31.12.2017	Changes to equity	Changes to financial result	Changes in temporary differences	31.12.2016
Provisions for impairment of loans and advances	449 499	-	9 365	9 365	440 134
Valuation of derivative financial instruments	364 433	-	(353 779)	(353 779)	718 212
Cash flow hedges valuation	21 446	(4 727)	-	(4 727)	26 173
Other provisions	127 715	-	21 194	21 194	106 521
Deferred income	268 250	-	4 276	4 276	263 974
Unrealized interest on credits, loans and securities	46 777	-	28 089	28 089	18 688
Other negative temporary differences	20 697	-	12 320	12 320	8 377
Total assets of deferred tax	1 298 817	(4 727)	(278 535)	(283 262)	1 582 079

Deferred tax liabilities	31.12.2017	Changes to equity	Changes to financial result	Changes in temporary differences	31.12.2016
Revaluation of financial instruments available for sale	(188 454)	(98 026)	-	(98 026)	(90 428)
Provisions for retirement allowances	(76)	1 760	-	1 760	(1 836)
Valuation of derivative financial instruments	(261 499)	-	105 928	105 928	(367 427)
Unrealised interest income on loans, securities and interbank deposits	(139 443)	-	34 049	34 049	(173 492)
Prepayments regarding amortization of applied investment relief	(1 751)	-	125	125	(1 876)
Difference between balance sheet and taxable value of non-financial assets	8 625	-	3 365	3 365	5 260
Other positive temporary differences	(6 352)	-	(4 379)	(4 379)	(1 973)
Total liabilities deferred tax	(588 950)	(96 266)	139 088	42 822	(631 772)

Net deferred tax assets	709 867	(100 993)	(139 447)	(240 440)	950 307
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As at 31.12.2017 the assets in the calculation of deferred tax assets do not include purchased receivables in the amount of gross PLN 5,114 k and provisions for loans that do not become tax expense in the amount of gross PLN 65,960 k.

in thousands of PLN

	31.12.2016	Changes to equity	Changes to financial result	Changes in temporary differences	31.12.2015
Deferred tax assets					
Provisions for impairment of loans and advances	440 134	-	11 645	11 645	428 489
Valuation of derivative financial instruments	718 212	-	(49 632)	(49 632)	767 844
Cash flow hedges valuation	26 173	(19 906)	-	(19 906)	46 079
Other provisions	106 521	-	(3 810)	(3 810)	110 331
Deferred income	263 974	-	10 073	10 073	253 901
Unrealized interest on credits, loans and securities	18 688	-	(22 164)	(22 164)	40 852
Other negative temporary differences	8 377	-	604	604	7 773
Total assets of deferred tax	1 582 079	(19 906)	(53 284)	(73 190)	1 655 269

	31.12.2016	Changes to equity	Changes to financial result	Changes in temporary differences	31.12.2015
Deferred tax liabilities					
Revaluation of financial instruments available for sale	(90 428)	135 478	-	135 478	(225 906)
Provisions for retirement allowances	(1 836)	(1 222)	-	(1 222)	(614)
Valuation of derivative financial instruments	(367 427)	-	56 063	56 063	(423 490)
Unrealised interests income on loans, securities and interbank deposits	(173 492)	-	(13 613)	(13 613)	(159 879)
Prepayments regarding amortization of applied investment relief	(1 876)	-	327	327	(2 203)
Difference between balance sheet and taxable value of non-financial assets	5 260	-	3 169	3 169	2 091
Other positive temporary differences	(1 973)	-	532	532	(2 505)
Total liabilities deferred tax	(631 772)	134 256	46 478	180 734	(812 506)

Net deferred tax assets	950 307	114 350	(6 806)	107 544	842 763
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As at 31.12.2016 the assets in the calculation of deferred tax assets do not include purchased receivables in the amount of gross PLN 8,500 k and provisions for loans that do not become tax expense in the amount of gross PLN 52,896 k.

	31.12.2017	31.12.2016
Movements on net deferred tax		
As at the beginning of the period	950 307	842 763
Changes recognised in income statement	(139 447)	(6 806)
Changes recognised in other comprehensive income	(100 993)	114 350
Balance at the end of the period	709 867	950 307

Temporary differences recognised in equity comprise deferred tax on available for sale securities, cash flow hedges and provisions for retirement allowances.

Temporary differences recognised in the income statement comprise deferred tax on the valuation of other financial assets, allowance for impairment of loans and receivables and assets in the course of business.

The impact of IFRS 9 implementation on the deferred tax effect is presented in Note 2.

28. Assets classified as held for sale

	31.12.2017	31.12.2016
Assets classified as held for sale		
Land and buildings	8	608
Total	8	608

in thousands of PLN

29. Other assets

Other assets	31.12.2017	31.12.2016
Interbank settlements	142 701	106 835
Sundry debtors	560 421	277 447
Prepayments	55 225	31 715
Repossessed assets	-	24 463
Settlements of stock exchange transactions	31 711	21 385
Other	52	52
Total	790 110	461 897
of which financial assets*	734 833	405 667

* Financial assets include all items of Other assets, with the exception of Prepayments, Repossessed assets and Other.

30. Deposits from banks

Deposits from banks	31.12.2017	31.12.2016
Term deposits	64 023	28 522
Loans from other banks	628 107	664 188
Current accounts	722 318	520 055
Total	1 414 448	1 212 765

Fair value of "Deposits from banks" is presented in Note 41.

Movements in loans received from banks	31.12.2017	31.12.2016
As at the beginning of the period	664 188	195 247
Increase (due to):	4 644	686 148
- drawing of loans	-	648 422
- interest on loans	4 644	7 050
- FX differences	-	30 676
Decrease (due to):	(40 725)	(217 207)
- repayment of loans	-	(211 645)
- interest repayment	(4 785)	(5 562)
- FX differences	(35 940)	-
As at the end of the period	628 107	664 188

31. Deposits from customers

Deposits from customers	31.12.2017	31.12.2016
Deposits from individuals	59 310 847	57 845 383
Term deposits	16 321 736	18 086 495
Current accounts	42 948 226	39 650 731
Other	40 886	108 157
Deposits from enterprises	38 702 801	42 540 494
Term deposits	15 321 645	20 453 339
Current accounts	20 533 707	18 519 563
Credits	2 237 211	3 020 931
Other	610 238	546 661
Deposits from public sector	4 141 874	2 995 372
Term deposits	1 904 467	1 234 058
Current accounts	2 233 410	1 747 709
Other	3 997	13 605
Total	102 155 522	103 381 249

in thousands of PLN

As at 31.12.2017 deposits held as collateral totalled PLN 233,625 k (as at 31.12.2016 - PLN 277,959 k).

Fair value of "Deposits from customers" is presented in Note 41.

Movements in loans received from other financial institutions	31.12.2017	31.12.2016
As at the beginning of the period	3 020 931	2 638 739
Increase (due to):	47 910	849 532
- drawing of loans	42 200	740 198
- interest on loans	5 710	7 714
- FX differences	-	101 620
Decrease (due to):	(831 630)	(467 340)
- repayment of loans	(630 728)	(459 261)
- interest repayment	(5 922)	(8 079)
- FX differences	(194 980)	-
As at the end of the period	2 237 211	3 020 931

32. Subordinated liabilities

Subordinated liabilities	Redemption date	Currency	Nominal value
Tranche 1	05.08.2025	EUR	100 000
Tranche 2	03.12.2026	EUR	120 000
Tranche 3	22.05.2027	EUR	137 100

Movements in subordinated liabilities	31.12.2017	31.12.2016
As at the beginning of the period	440 457	426 507
Increase (due to):	1 133 436	29 231
- interest on subordinated loan	33 564	16 479
- FX differences	-	12 752
- reclassification *	1 099 872	-
Decrease (due to):	(85 291)	(15 281)
- interest repayment	(27 528)	(15 281)
- FX differences	(57 763)	-
Subordinated liabilities - as at the end of the period	1 488 602	440 457
Short-term	11 257	1 604
Long-term (over 1 year)	1 477 345	438 853

*Bonds issued by Bank Zachodni WBK and qualified with the consent of KNF to subordinated liabilities.

Other details on these liabilities are disclosed in Note 4.

33. Debt securities in issue

Issuance of debt securities in 2017(non-matured securities)	Nominal value	Currency	Redemption date
Series F bank securities	750 000	PLN	19.02.2018

Issuance of debt securities in 2016 (non-matured securities)	Nominal value	Currency	Redemption date
Series D	185 000	PLN	26.02.2017
Series C bank securities	100 000	PLN	17.02.2017
Series E	120 000	EUR	03.12.2026

in thousands of PLN

Movements in debt securities in issue	31.12.2017	31.12.2016
As at the beginning of the period	1 783 303	1 698 619
Increase (due to):	2 049 345	1 111 318
- debt securities in issue	1 988 788	1 065 880
- interest on debt securities in issue	44 327	45 438
- FX differences	16 230	-
Decrease (due to):	(2 592 404)	(1 026 634)
- debt securities redemption	(1 430 000)	(980 000)
- reclassification*	(1 099 872)	-
- FX differences	(21 786)	-
- interest repayment	(40 746)	(46 634)
As at the end of the period	1 240 244	1 783 303

* Bonds issued by Bank Zachodni WBK and qualified with the consent of KNF to subordinated liabilities.

34. Provisions

Provisions	31.12.2017	31.12.2016
Provisions for legal claims	57 216	37 639
Provisions for off-balance sheet credit facilities	25 384	28 706
Total	82 600	66 345

Change in provisions 31.12.2017	Provisions for off		Total
	Provisions for legal claims	balance sheet credit facilities	
As at the beginning of the period	37 639	28 706	66 345
Provision charge	47 497	43 265	90 762
Utilization	(12 142)	(517)	(12 659)
Write back	(15 778)	(46 070)	(61 848)
Other changes	-	-	-
Balance at the end of the period	57 216	25 384	82 600
Short-term	57 216	18 425	75 641
Long-term	-	6 959	6 959

Change in provisions 31.12.2016	Provisions for off		Total
	Provisions for legal claims	balance sheet credit facilities	
As at the beginning of the period	27 373	55 276	82 649
Provision charge	77 110	61 054	138 164
Utilization	(66 157)	835	(65 322)
Write back	(687)	(88 459)	(89 146)
Balance at the end of the period	37 639	28 706	66 345
Short-term	37 639	19 712	57 351
Long-term	-	8 994	8 994

in thousands of PLN

35. Other liabilities

Other liabilities	31.12.2017	31.12.2016
Employee provisions	340 770	311 687
Other provisions	3 300	3 300
Interbank settlements	946 867	578 741
Other deferred and suspended income	168 180	171 320
Sundry creditors	490 362	413 579
Accrued liabilities	204 964	137 364
Public and law settlements	79 254	78 248
Settlements of stock exchange transactions	25 851	25 314
Total	2 259 548	1 719 553
of which financial liabilities *	2 012 114	1 469 985

* Financial liabilities include all items of 'Other liabilities' with the exception of Public and law settlements and Other deferred and suspended income.

Change in provisions 31.12.2017	Employee provisions	Other provisions	Total
	<i>of which: Provisions for retirement allowances</i>		
As at the beginning of the period	311 687	3 300	314 987
Provision charge	273 688	-	273 688
Utilization	(220 096)	-	(220 096)
Write back	(24 509)	-	(24 509)
Other changes	-	-	-
Balance at the end of the period	340 770	3 300	344 070
Short-term	273 545	3 300	276 845
Long-term	67 225	-	67 225

Change in provisions 31.12.2016	Employee provisions	Other provisions	Total
	<i>of which: Provisions for retirement allowances</i>		
As at the beginning of the period	319 000	3 306	322 306
Provision charge	275 447	-	275 447
Utilization	(260 805)	(6)	(260 811)
Write back	(21 955)	-	(21 955)
Other changes	-	(3 585)	-
Balance at the end of the period	311 687	3 300	314 987
Short-term	255 950	3 300	259 250
Long-term	55 737	-	55 737

Employee related provisions and accruals consists of items outlined in Note 48.

in thousands of PLN

36. Share capital

31.12.2017

Series/issue	Type of share	Type of preferences	Limitation of rights to shares	Number of shares	Nominal value of series/issue in PLN k
A	bearer	none	none	5 120 000	51 200
B	bearer	none	none	724 073	7 241
C	bearer	none	none	22 155 927	221 559
D	bearer	none	none	1 470 589	14 706
E	bearer	none	none	980 393	9 804
F	bearer	none	none	2 500 000	25 000
G	bearer	none	none	40 009 302	400 093
H	bearer	none	none	115 729	1 157
I	bearer	none	none	1 561 618	15 616
J	bearer	none	none	18 907 458	189 075
K	bearer	none	none	305 543	3 055
L	bearer	none	none	5 383 902	53 839
M	bearer	none	none	98 947	990
				99 333 481	993 335

Nominal value of one share is 10 PLN. All shares in issue are fully paid.

The shareholder having minimum 5% of the total number of votes at the BZ WBK General Meeting of Shareholders was Banco Santander with a controlling stake of 69.34%

31.12.2016

Series/issue	Type of share	Type of preferences	Limitation of rights to shares	Number of shares	Nominal value of series/issue in PLN k
A	bearer	none	none	5 120 000	51 200
B	bearer	none	none	724 073	7 241
C	bearer	none	none	22 155 927	221 559
D	bearer	none	none	1 470 589	14 706
E	bearer	none	none	980 393	9 804
F	bearer	none	none	2 500 000	25 000
G	bearer	none	none	40 009 302	400 093
H	bearer	none	none	115 729	1 157
I	bearer	none	none	1 561 618	15 616
J	bearer	none	none	18 907 458	189 075
K	bearer	none	none	305 543	3 055
L	bearer	none	none	5 383 902	53 839
				99 234 534	992 345

Nominal value of one share is 10 PLN. All shares in issue are fully paid.

The shareholders having minimum 5% of the total number of votes at the BZ WBK General Meeting of Shareholders were Banco Santander with a controlling stake of 69.41% stake and and Nationale - Nederlanden OFE with a share of 5.15%.

in thousands of PLN

37. Other reserve capital

Other reserve capital	31.12.2017	31.12.2016
General banking risk fund	649 810	649 810
Share premium	7 035 424	7 035 424
Other reserves of which:	8 490 949	6 553 441
<i>Reserve capital</i>	8 320 199	6 382 692
<i>Supplementary capital</i>	170 750	170 749
Total	16 176 183	15 132 993

Share (issue) premium is created from surplus over the nominal value of shares sold less costs of share issuance and constitutes the Bank's supplementary capital.

Reserve capital as at 31.12.2017 includes share scheme charge of PLN 118,423 k, as at 31.12.2016 of PLN 120,750 k.

Other movements of other reserve capital are presented in "movements on equity" for 2017 and 2016.

Statutory reserve (supplementary) capital is created from profit allocations in line with the prevailing banking legislation and the Bank's statute. The capital is not subject to split and is earmarked for covering balance sheet losses. Allocations from profit for the current year to reserve capital should amount to at least 8% of profit after tax and are made until supplementary capital equals at least one third of the Bank's share capital. The amount of allocations is adopted by the General Meeting of Shareholders.

Reserve capital is created from profit allocations in the amount adopted by the General Meeting of Shareholders. The decision on reserve capital use is taken by the General Meeting of Shareholders.

38. Revaluation reserve

Revaluation reserve 31.12.2017	Total gross	Deferred tax adjustment	Total nett
Opening balance, of which:	347 845	(66 091)	281 754
Debt and equity securities	475 937	(90 428)	385 509
Valuation related to cash flow hedge	(137 755)	26 174	(111 581)
Actuarial gains/losses on retirement allowances	9 663	(1 837)	7 826
Change in valuation of debt and equity securities available for sale investments	539 429	(102 492)	436 937
Decrease in revaluation reserve related to sale of investments	(23 502)	4 465	(19 037)
Change of cash flow hedges valuations	24 880	(4 727)	20 153
Change of actuarial gains/losses on retirement allowances	(9 264)	1 760	(7 504)
Closing balance, of which:	879 388	(167 085)	712 303
Debt and equity securities	991 864	(188 455)	803 409
Valuation related to cash flow hedge	(112 875)	21 447	(91 428)
Actuarial gains/losses on retirement allowances	399	(77)	322

in thousands of PLN

Revaluation reserve 31.12.2016	Total gross	Deferred tax adjustment	Total nett
Opening balance, of which:	949 687	(180 440)	769 247
Debt and equity securities	1 188 976	(225 905)	963 071
Valuation related to cash flow hedge	(242 522)	46 080	(196 442)
Actuarial gains/losses on retirement allowances	3 233	(615)	2 618
Change in valuation of debt and equity securities available for sale investments	(449 427)	85 391	(364 036)
Decrease in revaluation reserve related to sale of investments	(263 612)	50 086	(213 526)
Change of cash flow hedges valuations	129 416	(24 589)	104 827
Change in available for sale cash flow hedges valuations	(24 649)	4 683	(19 966)
Change of actuarial gains/losses on retirement allowances	6 430	(1 222)	5 208
Closing balance, of which:	347 845	(66 091)	281 754
Debt and equity securities	475 937	(90 428)	385 509
Valuation related to cash flow hedge	(137 755)	26 174	(111 581)
Actuarial gains/losses on retirement allowances	9 663	(1 837)	7 826

39. Hedge accounting

Bank Zachodni WBK uses hedging strategies within hedge accounting in line with the risk management principles set out in note 3 to the consolidated annual financial statements.

Fair value hedges

Bank Zachodni WBK uses fair value hedge accounting with respect to the following classes of financial instruments:

- Debt securities with a fixed interest rate in PLN and denominated in EUR;
- Loans with a fixed interest rate in PLN.

Fair value hedges include Interest Rate Swaps and Overnight Indexed Swap, where the Bank pays a fixed rate and receives a variable rate. The transactions hedge the risk of changes in the fair value of an instrument or a portfolio as a result of movements in market interest rates. The transactions do not hedge fair value changes on account of credit risk.

Hedging items are measured at fair value. Hedged items are measured at amortised cost taking into account fair value adjustments on account of the risk being hedged.

The tables below contain details about individual groups of hedge transactions for 2017 and the comparative period:

31.12.2017	Bonds	Loans
Nominal value of hedging position	1 979 709	425 000
Measurement to fair value of hedging instrument	(104 434)	3 763
Fair value adjustment of hedged instrument due to hedged risk	107 005	(3 817)
Hedged risk	Interest rate risk	Interest rate risk
Period over which the instruments have an impact on the Bank's results	up to 2025	up to 2021
31.12.2016	Bonds	Loans
Nominal value of hedging position	1 982 240	300 000
Measurement to fair value of hedging instrument	(128 789)	4 358
Fair value adjustment of hedged instrument due to hedged risk	132 512	(4 409)
Hedged risk	Interest rate risk	Interest rate risk
Period over which the instruments have an impact on the Bank's results	up to 2025	up to 2021

Since January 2016, Bank Zachodni WBK has used portfolio-based hedge accounting for the fair value of interest rate risk with respect to the portfolio of fixed interest rate loans in PLN. The fair value hedges are Interest Rate Swaps for which the bank pays a fixed rate and receives a variable rate. The purpose of the hedge is to eliminate the risk of changes in the fair value of the fixed interest rate loans resulting from movements in market interest rates. Credit margin is excluded from the hedging relationship.

In December 2015, Bank Zachodni WBK stopped applying fair value macro hedge accounting for a hedge of interest rate risk on fixed interest rate cash loans in PLN (6 relationships in total). By the time the Bank stopped using the hedge accounting, the accumulated

in thousands of PLN

fair value adjustment for the hedged position recognized in the balance sheet was PLN 7,148 k. This amount is amortized against the profit & loss account according to the tenors originally agreed for individual hedging relationships. PLN 1,199 k was recognised in the income statement for 2017 and PLN 262 k will be reflected in the income statement by the end of 2018.

Cash flow hedging

Bank Zachodni WBK uses hedge accounting for its future cash flows with respect to commercial and mortgage credit portfolios based on a variable interest rate, in PLN or denominated in EUR, USD and CHF with maximum maturity of 36 years.

The Bank's hedging strategies are designed to protect the Bank's exposures against the risk of changes in the value of future cash flows resulting from adverse interest rate movements or – in the case of credit portfolios denominated in foreign currency – from currency fluctuations. Hedging relationships are created using Interest Rate Swaps and Cross-Currency Interest Rate Swaps. The Bank uses the hypothetical derivative approach whereby the hedged credit portfolio is reflected by a derivative transaction with specific characteristics.

Hedged items are measured at amortised cost, while hedging items are measured at fair value. Subject to fulfilment of the criteria for effectiveness of hedging relationships, changes in the fair value of hedging instruments are recognised in equity.

As of 31.12.2017, the nominal value of the hedging item was PLN 11,457,807 k (31.12.2016 – PLN 15,882,430) k. Measurement to fair value of the hedging instrument was PLN (112,875) k (31.12.2016 – PLN (137,755) k); the same amount, less deferred tax, is recognised in comprehensive income and accumulated in the Bank's equity under revaluation reserve and are presented in note 38. Hedging instruments have been concluded for a period of time until 2028.

The non-effective portion of fair value of the cash flow hedge was PLN 10,378 k as of 31.12.2017 and PLN (7,235) k as of 31.12.2016. It was taken to the 'Net trading income and revaluation' line of the profit and loss account.

40. Sell-buy-back and buy-sell-back transactions

Bank Zachodni WBK raises funds by selling financial instruments under agreements to repurchase these instruments at future dates at a predetermined price.

Repo and sell-buy-back transactions may cover securities from the Bank's balance sheet portfolio.

The foregoing items are not removed from the balance sheet, because the Bank retains all rewards (i.e. interest income on pledged securities) and risks (interest rate risk and the issuer's credit risk) attaching to these assets.

	31.12.2017	31.12.2016
	Balance sheet value	Balance sheet value
Liabilities valued at amortised cost (contains sell-buy-back)	1 479 667	-
Fair value of securities held as collateral for sell-buy-back/repo transactions	1 480 050	-
Sell-buy-back transactions	31.12.2017	31.12.2016
Sell-buy-back transactions from banks	11 379	-
Sell-buy-back transactions from customers	1 468 288	-
Total	1 479 667	-

All of the above-mentioned risks and costs related to the holding of the underlying debt securities in the sell-buy-back transactions remain with the Bank, as well as power to dispose them.

The Bank also effects reverse repo and buy-sell-back transactions at the same price increased by the pre-determined amount of interest.

Financial instruments covered by reverse repo and buy-sell-back transactions are not recognised in the balance sheet, because the Bank does not retain any rewards or risks attaching to these assets.

These instruments represent a security cover accepted by the Bank which may sell or pledge these assets.

Financial instruments held as security for (reverse repo) repurchase agreements may be sold or repledged under standard agreements, under the obligation to return these to the counterparty on maturity of the transaction.

As at 31.12.2017 and 31.12.2016 statements of financial position contained no financial instruments serving as collateral to repo transactions maturing within a period shorter or equal to that of the main transaction.

in thousands of PLN

41. Fair value

Fair value is the amount for which an asset could be exchanged, or a liability settled, between knowledgeable, willing parties in an arm's length transaction other than in a forced or liquidation sale, and is best reflected by the market price, if available.

Below is a summary of the book values and fair values of the individual groups of assets and liabilities.

Assets	31.12.2017		31.12.2016	
	Book Value	Fair Value	Book Value	Fair Value
Cash and balances with central banks	4 114 801	4 114 801	4 696 634	4 696 634
Loans and advances to banks	2 012 118	2 012 118	3 308 802	3 308 802
Financial assets held for trading	3 421 547	3 421 547	3 198 187	3 198 187
Hedging derivatives	146 724	146 724	66 787	66 787
Loans and advances to customers	90 537 003	91 349 827	87 102 390	87 014 565
Financial assets available for sale	25 784 029	25 784 029	26 322 361	26 322 361
Liabilities				
Deposits from banks	1 414 448	1 414 448	1 212 765	1 212 765
Hedging derivatives	578 798	578 798	1 961 828	2 024 012
Financial liabilities held for trading	1 263 859	1 263 859	1 809 969	1 809 969
Subordinated liabilities	1 488 602	1 500 989	440 457	564 402
Deposits from customers	102 155 522	102 170 483	103 381 249	103 390 563

Below is a summary of the key methods and assumptions used in the estimation of fair values of the financial instruments shown in the table above.

Financial assets and liabilities not carried at fair value in the statement of financial position

The Bank has financial instruments which in accordance with the IFRS are not carried at fair value in the accounts. The fair value of such instruments is measured using the following methods and assumptions.

Apart from assets that are not measured at fair value, all the other fair values fulfil conditions for classification to Level II of fair value.

Loans and advances to banks: The fair value of deposits and placements is measured using discounted cash flows at the current money market interest rates for receivables of similar credit risk, maturity and currency. In the case of demand deposits without a fixed maturity date or with maturity up to 6 months, it is assumed that their fair value is not significantly different than their book value. The process of fair value estimation for these instruments is not affected by the long-term nature of the business with depositors.

Loans and advances to customers: Carried at net value after impairment charges. Fair value is calculated as the discounted value of the expected future cash flows in respect of principal and interest payments. It is assumed that loans and advances will be repaid at their contractual maturity date. The estimated fair value of the loans and advances reflects changes in the credit risk from the moment of sanction (margins) and changes in interest rates.

Financial assets not carried at fair value: The Bank does not use fair valuation for equity securities of unlisted companies for which the fair value cannot be reliably established. In the statement of financial position, equity instruments are presented at cost less impairment. Debt instruments are measured at amortised cost.

Deposits from banks and deposits from customers: Fair value of the deposits with maturity exceeding 6 months was estimated based on the cash flows discounted by the current market rates for the deposits with similar maturity dates. In the case of demand deposits without a fixed maturity date or with maturity up to 6 months, it is assumed that their fair value is not significantly different than their book value. The process of fair value estimation for these instruments is not affected by the long-term nature of the business with depositors.

Debt securities in issue and subordinated liabilities: The Bank has made an assumption that fair value of those securities is based on discounted cash flows methods incorporating adequate interest rates.

Financial assets and liabilities carried at fair value in the statement of financial position

As at 31.12.2017 and in the comparable periods the Bank made the following classification of its financial instruments measured at fair value in the statement of financial position:

Level I (active market quotations): debt, equity and derivative financial instruments which at the balance sheet date were measured using the prices quoted in the active market. The Bank allocates to this level State Treasury bonds, treasury bills, Eurobonds of the German government, Eurobonds of the American government, shares of listed companies and WIG 20 futures.

Level II (the measurement methods based on market-derived parameters): This level includes derivative instruments. Derivative instruments are measured using discounted cash flow models based on the discount curve derived from the inter-bank market.

in thousands of PLN

Level III (measurement methods using material non-market parameters): The level includes equity securities that are not quoted in the active market, measured using the expert valuation model; investment certificates measured at the balance sheet date at the price announced by the mutual fund.

The objective of using a valuation technique is to determine the fair value, i.e., prices, which were obtained by the sale of an asset in an orderly transaction between market participants carried out under current market conditions between market participants at the measurement date.

Valuation of major capital investments classified to Level III:

- a) AVIVA Towarzystwo Ubezpieczeń na Życie SA (AVIVA TUŻ),
- b) AVIVA Powszechne Towarzystwo Emerytalne SA (AVIVA PTE),
- c) AVIVA Towarzystwo Ubezpieczeń Ogólnych SA (AVIVA TUO)

are made semi-annually by specialized units of the Bank using income methods based on discounted cash flows, where the most important variables of the model are the level of forecasted dividends and the risk free rate. During the reporting period revaluation of above equity investments has been made in the total amount of 33.8 million PLN and recognized in the revaluation reserve.

As at 31.12.2017 and in the comparable period the Bank classified its financial instruments to the following fair value levels.

31.12.2017	Level I	Level II	Level III	Total
Financial assets				
Financial assets held for trading	2 189 111	1 231 989	447	3 421 547
Hedging derivatives	-	146 724	-	146 724
Financial investment assets - debt securities	24 856 947	-	32 532	24 889 479
Financial investment assets - equity securities	-	-	894 550	894 550
Total	27 046 058	1 378 713	927 529	29 352 300
Financial liabilities				
Financial liabilities held for trading	-	1 263 859	-	1 263 859
Hedging derivatives	-	578 798	-	578 798
Total	-	1 842 657	-	1 842 657

31.12.2016	Level I	Level II	Level III	Total
Financial assets				
Financial assets held for trading	282 769	2 915 167	251	3 198 187
Hedging derivatives	-	146 724	-	146 724
Financial investment assets - debt securities	15 062 259	10 366 571	38 240	25 467 070
Financial investment assets - equity securities	12 644	-	842 647	855 291
Total	15 357 672	13 428 462	881 138	29 667 272
Financial liabilities				
Financial liabilities held for trading	80 129	1 729 840	-	1 809 969
Hedging derivatives	-	578 798	-	578 798
Total	80 129	2 308 638	-	2 388 767

The tables below show reconciliation of changes in the balance of financial instruments whose fair value is established by means of the valuation methods using material non-market parameters.

in thousands of PLN

Level III	Financial assets			Financial liabilities
	Financial assets held for trading	Financial investment assets - debt securities	Financial investment assets - equity securities	Financial liabilities held for trading
31.12.2017				
Beginning of the period	251	38 240	842 647	-
Profit or losses				
<i>recognised in income statement</i>	(29)	-	-	-
<i>recognised in equity</i>	-	-	68 267	-
Purchase	1 057	-	2 036	-
Sale	(832)	-	(18 400)	-
Matured	-	-	-	-
Impairment	-	-	-	-
Other	-	(5 708)	-	-
At the period end	447	32 532	894 550	-

Level III	Financial assets			Financial liabilities
	Financial assets held for trading	Financial investment assets - debt securities	Financial investment assets - equity securities	Financial liabilities held for trading
31.12.2016				
Beginning of the period	1 839	-	1 086 201	-
Profit or losses				
<i>recognised in income statement</i>	81	-	68 506	-
<i>recognised in equity</i>	-	-	(52 028)	-
Purchase	340	-	4 900	-
Sale	(2 009)	-	(264 932)	-
Matured	-	-	-	-
Impairment	-	-	-	-
Other	-	38 240	-	-
At the period end	251	38 240	842 647	-

42. Contingent liabilities

Significant court proceedings conducted by Bank Zachodni WBK

As at 31.12.2017, no proceedings were instituted by court or by state administration agencies with relation to any claims made by or against the Bank amounting to a minimum of 10% of the Bank's equity.

The value of all litigation amounts to PLN 684,502 k, which is ca. 3.28% of the Bank's equity. This amount includes PLN 371,189 k claimed by the Bank, PLN 313,313 k in claims against the Bank. There were no litigations for bankruptcy or arrangement.

On 20.10.2017, Bank Zachodni WBK received a notice of a class action instituted by the borrowers who had loans indexed to the CHF, originated by the former Kredyt Bank. The total value of the claim, estimated as at the reporting date, is PLN 32.3m. However, this amount is very likely to be changed as new borrowers join the class action.

In 2017 the amount of significant court proceedings which had been completed amounted to PLN 195,733 k.

As at 31.12.2017, the value of provisions for legal risks, for court cases against the Bank was PLN 57,216 k. In 10 cases against the Bank, where the claim value was high, a provision of PLN 40,983 k was raised.

As at 31.12.2016, no proceedings were instituted by court or by state administration agencies with relation to any claims made by or against the Bank amounting to a minimum of 10% of the Bank's equity.

The value of all litigation amounts to PLN 437,175 k, which is ca. 2.30% of the Bank's equity. This amount includes PLN 247,406 k claimed by the Bank, PLN 189,769 k in claims against the Bank. In 2017, there was a significant year-on-year increase in the amount claimed by the Bank (from PLN 93,305 k to PLN 247,406 k) which results from the abrogation of the laws pertaining to the banking writs of execution and the need to refer to the court any unpaid receivables of the bank under ordinary proceedings or proceedings by writ of payment. There were no litigations for bankruptcy or arrangement.

in thousands of PLN

In 2016 the amount of significant court proceedings which had been completed amounted to PLN 246,789 k.

As at 31.12.2016, the value of provisions for legal risks, for court cases against the Bank was PLN 37,639 k. In 8 cases against the Bank, where the claim value was high, a provision of PLN 34,778 k was raised.

The Bank raises provisions for legal risk where an internal risk assessment for a particular case indicates a possible outflow of cash. Provisions for cases disputed in court are presented in Note 34.

Off-balance sheet liabilities

The break-down of contingent liabilities and off-balance transactions into categories are presented below. The values of guarantees and letters of credit as set out in the table below represent the maximum possible loss that would be disclosed as at the balance sheet day if the customers did not meet any of their obligations towards third parties.

Contingent liabilities - sanctioned	31.12.2017	31.12.2016
Liabilities sanctioned		
- financial	21 409 105	21 445 091
- credit lines	17 718 025	17 945 726
- credit cards debits	3 049 456	2 809 662
- import letters of credit	633 773	655 655
- term deposits with future commencement term	7 851	34 048
- guarantees	4 948 545	4 248 934
Allowance for impairment	(25 384)	(28 706)
Total	26 332 266	25 665 319

43. Assets and liabilities pledged as collateral

Assets securing funds to cover the BGF are debt securities.

In order to calculate the contribution to the deposit protection fund, Bank Zachodni WBK applied 0.55% (i.e. the same rate as in 2016) of funds deposited in all accounts with the bank, being the basis for calculating the obligatory reserve.

As at 31.12.2017, assets allocated to that end totalled PLN 561,897k compared with PLN 554,489k a year before.

In 2017, deposits opened with financial institutions to secure the value of transactions totalled PLN 798,350k (PLN 2,131,120k k as at 31.12.2016).

In 2017, the BZ WBK accepted PLN 348,808k worth of deposits securing transactions (vs. PLN 249,871k in 2016).

Other assets pledged and liabilities accepted as collateral are disclosed in Notes 31 and 40.

44. Finance and operating leases

Finance leases

Bank Zachodni WBK acts as a lessee in finance lease agreements where the lessor side is represented by BZ WBK leasing subsidiaries. The leasing contracts finance purchase of cars and furniture.

Finance leases gross liabilities - maturity	31.12.2017	31.12.2016
less than 1 year	13 615	13 340
between 1 and 5 years	40 043	46 913
over 5 years	(27)	422
Total	53 631	60 675

Present value of minimum lease payments - maturity	31.12.2017	31.12.2016
less than 1 year	13 419	13 332
between 1 and 5 years	38 035	43 254
over 5 years	-	374
Total	51 454	56 960

in thousands of PLN

Reconciliation between the gross investment and the present value of minimum lease payments	31.12.2017	31.12.2016
Finance leases gross liabilities	53 631	60 675
Unrealised financial costs	(2 177)	(3 715)
Present value of minimum lease payments	51 454	56 960

Financial leaseback

On 16.04.2016, an agreement was signed between BZ WBK and its subsidiary BZ WBK Leasing providing for a financial leaseback of properties (freehold of a building and land and perpetual usufruct of land) and a lease of a planned project (an office building to be developed during the next three years) located in Wrocław.

The final total value of the assets arising from the lease of the building and land, which was estimated at the time of initiation of the transaction, was PLN 156,278 k.

Current value of the fixed assets obtained under the financial leaseback agreement was PLN 38,976 k as at 31.12.2017, the initial value of fixed assets under construction was PLN 77,989 k.

In accordance with the agreement, the basic lease term was defined as 153 months.

The purchase of assets by BZ WBK Leasing and development of the office building is financed with a loan provided by BZ WBK.

The lease agreement requires that only interest should be paid on the lease and the loan during the term of the respective agreements, while the principal sums will be paid as part of the last tranche, with the pre-financing costs relating to the building and the site where the building is developed are to be capitalised by BZ WBK Leasing, and the bank is to pay them along with the principal payment at the end of contractual period. Both agreements are based on an interest rate equal to BZ WBK Leasing S.A. and the Bank.

Finance leaseback gross liabilities - maturity	31.12.2017	31.12.2016
less than 1 year	424	421
between 1 and 5 years	1 697	1 686
over 5 years	30 415	30 614
Total	32 536	32 721

Present value of minimum lease payments - maturity	31.12.2017	31.12.2016
less than 1 year	420	418
between 1 and 5 years	1 621	1 611
over 5 years	26 225	26 056
Total	28 266	28 085

Reconciliation between the gross investment and the present value of minimum lease payments	31.12.2017	31.12.2016
Finance leaseback gross liabilities	32 536	32 721
Unrealised financial costs	(4 270)	(4 636)
Present value of minimum lease payments	28 266	28 085

Operating leases

The BZ WBK leases offices in compliance with operational leasing agreements. As a standard, agreements are concluded for 5-10 years. A small part of the offices is subleased outside the Bank. In 2017 and 2016 rentals totalled PLN 186,831 k and PLN 192,596 k, respectively. These payments are presented in the profit and loss account under "operating expenses".

The table below shows the total obligations under irrevocable operating lease agreements concluded by the Bank (including the value of perpetual usufruct of land).

Payments - maturity	31.12.2017	31.12.2016
less than 1 year	176 091	197 670
between 1 and 5 years	451 979	462 982
over 5 years	384 471	467 632
Total	1 012 541	1 128 284

in thousands of PLN

45. Statement of cash flows- additional information

Table below specifies components of cash balances of Bank Zachodni WBK.

Cash and cash equivalents	31.12.2017	31.12.2016
Cash and balances with central banks	4 114 801	4 696 634
Receivables from interbank deposits*	2 011 387	3 308 344
Debt securities held for trading*	-	699 883
Debt securities available for sale*	1 379 839	2 849 694
Total	7 506 027	11 554 555
The impact of changes in currency exchange rates during the financial year on cash and cash equivalents	(89 985)	85 118

* financial assets with initial maturity below three months

Bank Zachodni WBK holds restricted cash, which are the funds accumulated on obligatory reserve account in the Central Bank.

In the periods presented in the financial statement Bank Zachodni WBK has received and made interest payments in the following amounts:

Interests received and interests paid	01.01.2017- 31.12.2017	01.01.2016- 31.12.2016
Interests received, including:	4 697 242	4 636 840
- operating activities	4 096 842	4 036 599
- investing activities	600 400	600 241
Interests paid, including:	(894 898)	(958 223)
- operating activities	(815 917)	(882 667)
- financing activities	(78 981)	(75 556)

in thousands of PLN

46. Related parties

The tables below present intercompany transactions. Most of the transactions are banking transactions made as part of ordinary business activities and mainly include loans, deposits, guarantees, leases. In the case of internal Group transactions, a documentation is prepared in accordance with requirements of tax regulations for transfer pricing.

Transactions with subsidiaries	31.12.2017	31.12.2016
ASSETS	8 867 211	7 986 464
Loans and advances to banks	28 948	3 312
Financial assets held for trading	5 438	17 820
Loans and advances to customers	8 816 531	7 952 284
Other assets	16 294	13 048
LIABILITIES	479 234	322 073
Deposits from banks	129 461	51 406
Financial liabilities held for trading	26 169	911
Deposits from customers	154 529	152 939
Other liabilities	169 075	116 817
INCOME	351 121	288 380
Interest income	174 332	147 114
Fee and commission income	167 320	133 083
Other operating income	9 469	8 183
EXPENSES	52 376	21 605
Interest expenses	4 850	5 035
Fee and commission expenses	2 228	4 384
Net trading income and revaluation	45 195	12 163
Operating expenses incl.:	103	23
<i>Bank's staff, operating expenses and management costs</i>	91	-
<i>Other</i>	12	23
CONTINGENT LIABILITIES	1 185 390	1 837 552
Sanctioned:	1 185 390	1 837 552
- <i>financial</i>	1 121 936	1 770 561
- <i>guarantees</i>	63 454	66 991
DERIVATIVES' NOMINAL VALUES	2 727 340	1 868 845
FX swap – purchased amounts	89 180	-
FX swap – sold amounts	92 010	-
Cross-currency interest rate swap – purchased amounts	249 704	288 211
Cross-currency interest rate swap – sold amounts	270 900	270 900
Single-currency interest rate swap	2 025 546	1 309 734

Transactions with associates	31.12.2017	31.12.2016
LIABILITIES	120 146	78 414
Deposits from customers	90 102	78 414
Sell-buy-back transactions	30 044	-
INCOME	13 451	17 755
Fee and commission income	13 451	17 755
EXPENSES	3 713	7 783
Interest expenses	1 806	1 313
Fee and commission expenses	79	89
Operating expenses incl.:	1 828	6 381
<i>General and administrative expenses</i>	1 828	6 381

in thousands of PLN

Transactions with Santander Group	with the parent company		with other entities	
	31.12.2017	31.12.2016	31.12.2017	31.12.2016
ASSETS	598 411	981 961	9 854	3 674
Loans and advances to banks, incl:	308 691	594 042	9 831	274
<i>deposits</i>	95 993	353 911	-	-
<i>current accounts</i>	212 698	240 131	9 831	274
Financial assets held for trading	282 036	387 727	-	3 371
Hedging derivatives	7 469	-	-	-
Other assets	215	192	23	29
LIABILITIES	403 807	633 941	86 398	90 859
Deposits from banks incl.:	62 996	271 312	23 539	3 683
<i>current accounts</i>	62 996	271 312	23 539	3 683
Hedging derivatives	-	54 503	-	-
Financial liabilities held for trading	322 933	308 126	-	7 365
Deposits from customers	-	-	52 577	71 079
Other liabilities	17 878	-	10 282	8 732
INCOME	14 914	16 747	394	274
Interest income	11 321	14 268	95	28
Fee and commission income	3 593	2 096	299	239
Other operating income	-	-	-	7
Net trading income and revaluation	-	383	-	-
EXPENSES	84 818	1 721	73 404	26 101
Interest expenses	1 050	446	960	1 276
Fee and commission expenses	1 171	1 106	1	5
Net trading income and revaluation	64 720	-	57 672	2 420
Operating expenses incl.:	17 877	169	14 771	22 400
<i>Bank's staff, operating expenses and management costs</i>	17 877	-	14 763	22 400
<i>Other operating expenses</i>	-	169	8	-
CONTINGENT LIABILITIES	-	10 706	-	-
Sanctioned:	-	10 706	-	-
- <i>financial</i>	-	10 706	-	-
DERIVATIVES' NOMINAL VALUES	51 859 866	57 761 351	-	634 312
Cross-currency interest rate swap – purchased amounts	3 478 300	5 645 125	-	-
Cross-currency interest rate swap – sold amounts	3 414 864	5 424 101	-	-
Single-currency interest rate swap	18 298 033	16 517 900	-	633 412
Options	8 001 216	7 285 846	-	-
FX swap – purchased amounts	4 719 697	5 363 317	-	-
FX swap – sold amounts	4 762 299	5 344 715	-	-
FX options -purchased CALL	2 010 291	2 643 269	-	-
FX options -purchased PUT	1 950 686	2 798 804	-	-
FX options -sold CALL	2 026 149	2 755 705	-	-
FX options -sold PUT	2 211 749	2 824 233	-	-
Spot-purchased	162 894	162 456	-	-
Spot-sold	163 182	162 876	-	-
Forward- purchased amounts	138 027	101 365	-	-
Forward- sold amounts	135 771	74 665	-	900
Capital derivatives contract - purchased	386 708	656 974	-	-

Transactions with key management personnel

Remuneration of Bank Zachodni WBK Management Board Members, Supervisory Board Members and key management. Loans and advances made by the Bank to the key management personnel

As at 31.12.2017 and 31.12.2016 members of the Management Board were bound by the non-compete agreements which remain in force after they step down from their function. If a Member of the Management Board is removed from their function or not appointed for another term, he/she is entitled to a once-off severance pay. The severance pay does not apply if the person accepts another function in the Bank.

Loans and advances have been sanctioned on regular terms and conditions.

in thousands of PLN

Remuneration of Management Board Members and Key Management	Management Board Members		Key Management	
	2017	2016	2017	2016
Remuneration	12 774	10 162	21 824	20 601
Additional benefits (e.g among others, life insurance cover without pension option, medical cover, accommodation, travel expenses and school fees)	1 136	894	951	877
The awards paid in 2017 and 2016 *	8 186	6 910	8 906	6 224
Equivalent paid for unused annual leave	125	199	-	108
Additional compensation for termination of the contract and the non-competition clause	-	1 092	-	-
Loans and advances made by the Bank to the Members of the Management Board/Key Management	11 054	7 158	22 683	25 694
Deposits from The Management Board and their relatives/Key management	17 328	13 312	13 106	14 199
Provisions for unused holidays	797	567	1 119	1 181
The number of conditional rights to shares	34 670	17 671	37 274	28 615

* included part of the award for 2016, 2015, 2014, 2013 and 2012 which was conditional and deferred in time

The category of key management personnel includes the persons covered by the principles laid down in the "Policy on variable components of remuneration paid to the individuals holding managerial positions at Bank Zachodni WBK".

BZ WBK Group applies the Policy on variable components of remuneration for individuals holding managerial positions in BZ WBK Group. The Policy has been approved by the bank's Management Board and Supervisory Board and is reviewed annually or each time significant organisational changes are made.

Persons holding managerial positions are paid variable remuneration once a year following the end of the settlement period and release of the bank's results. Variable remuneration is awarded in accordance with applicable bonus regulations and paid in cash and phantom stock. The latter shall represent min. 50% of the total amount of variable remuneration. Payment of min. 40% of variable remuneration referred to above is conditional and deferred for the period of three years (13.3% per annum). Variable remuneration is paid in arrears in equal annual instalments depending on individual performance in the period subject to assessment and the value of the phantom stock.

In 2017, the total remuneration paid to the Supervisory Board Members of Bank Zachodni WBK totalled PLN 1,556 k (PLN 1,712 k in 2016). Mr John Power received remuneration for the supervision over acquisition of a carve-out business of Deutsche Bank Poland by BZ WBK in the amount of PLN 84.0 k. Mr John Power received remuneration of PLN 28.7 k from subsidiaries for his membership in their Supervisory Boards (PLN 35 k in 2016).

47. Acquisitions and disposals of investments in subsidiaries

Acquisitions and disposals of investments in subsidiaries 2017 and 2016

Agreement on the acquisition of a carve-out of Deutsche Bank Polska by Bank Zachodni WBK

On 14 December 2017, Bank Zachodni WBK and Banco Santander signed a transaction agreement with Deutsche Bank AG (DB AG) to purchase a part of Deutsche Bank Polska (DBPL) business, consisting of retail banking, private banking, SME banking and DB Securities. DBPL's corporate and investment banking business and foreign-currency mortgage portfolio are excluded from the transaction and will remain in DBPL (retained business).

On the same day, the bank signed a pre-demerger agreement with DBPL and DB AG setting out the terms of cooperation between the bank and DBPL to finalise the transaction.

Pursuant to the transaction agreement, DBPL's branch network and external sales channels (agents and intermediaries) are to be integrated with the bank's structures. Asset management contracts will also be transferred along with the carve-out, which will enable the transfer of open-ended investment funds.

Before the demerger, Bank Zachodni WBK will buy DBPL's shares from DB AG, representing 10% of votes at the DBPL's General Meeting of Shareholders. Next, the bank and DBPL will file requests for the registration of the demerger with relevant registry courts.

The demerger will be effected on the following terms:

- DBPL will be a demerged company and BZ WBK will be an acquiring company;

in thousands of PLN

- The share capital of DBPL will be decreased by at least an equivalent of the total nominal value of the shares purchased by Bank Zachodni WBK. On the date of the registration of such capital decrease, all the shares purchased by the bank will cease to exist and DB AG will become the sole shareholder of DBPL;
- In exchange for the transfer of the carved-out business to Bank Zachodni WBK, DB AG will receive a stated number of BZ WBK shares (demerger shares) on the demerger date, calculated based on the agreed formula which will be used to determine a share exchange ratio in the demerger plan. The demerger will be effective as of the date of registration of the bank's capital increase by way of the issuance of demerger shares;
- On the demerger date, the carved-out business will be transferred to the bank and the business which is not subject to the transaction will remain in DBPL. DBPL's assets and liabilities will be allocated between the carved-out business and the retained business based on the terms specified in the transaction agreement and the demerger plan.

The preliminary purchase price is PLN 1,289,799,000 and has been calculated on the basis of a capital requirement for carved-out risk weighted assets (excluding DB Securities' shares), determined using financial projections as at the date close to the execution of the transaction agreement. The portion of the preliminary purchase price related to the value of DB Securities' shares has been calculated on the basis of the company's net asset value.

The consideration for the transaction will be paid in:

- cash, through the payment of a price for the purchased shares (20% of the preliminary purchase price);
- newly issued shares of the bank representing approx. 2.7% of the bank's share capital (80% of the preliminary purchase price).

Once the transaction agreement is executed, the preliminary purchase price will be adjusted to reflect changes in relevant assets and liabilities that have taken place between the transaction agreement date and the demerger date.

The transaction is subject to regulatory approvals, including consents from the Polish Financial Supervision Authority (KNF) and the President of the Office of Competition and Consumer Protection (UOKiK), as well as resolutions of the General Meetings of Shareholders of BZ WBK and DBPL, signing of the demerger plan and fulfilment of certain operational conditions. The transaction is expected to close in Q4 2018. The migration of IT systems is planned to be completed immediately after closing.

Conclusion of the agreement will not lead to a take-over of control or significant influence over Deutsche Bank Polska S.A., nor will it give rise to any obligations that would need to be disclosed.

Contribution in kind of BZWBK F24 S.A. (formerly BZ WBK Nieruchomości S.A.) shares to BZWBK Finanse sp. z o.o

On 24.11.2017, BZ WBK S.A. made contribution in kind of BZWBK F24 S.A. (formerly BZ WBK Nieruchomości S.A.) shares to BZWBK Finanse sp. z o.o. to cover the acquisition of BZWBK Finanse sp. z o.o. shares by BZWBK S.A. In the second half of 2017, BZ WBK F24 S.A. changed its business model. The main profile of the business activity focused around financing of consumer car purchase – the company was registered by the Polish Financial Supervision Authority (KNF) as a lending institution.

The changed ownership structure will allow to limit the cost of business management and it is consistent with the strategy of extending the business activity of BZ WBK Group whereby BZ WBK F24 S.A. will offer financial products addressed to personal customers (consumers) on the market of so-called "light vehicles".

On 12.01.2018, in the Nation Court Register was registered increase of share capital BZWBK Finanse sp. z o.o to PLN 1,630k. Share capital was fully paid.

Liquidation of AKB Marketing Services sp. z o.o. in liquidation

On 28.03.2017, AKB Marketing Services sp. z o.o. in liquidation, a subsidiary of Santander Consumer Bank S.A., was liquidated.

The subsidiary's assets and liabilities were finally accounted for. Profit on liquidation of PLN 3,757 k was presented in the consolidated income statement under 'Net gains/(losses) on subordinated entities'.

AKB Marketing Services sp. z o.o. in liquidation carried out ancillary business operations in respect of banking services. On 20.11.2017, the company AKB Marketing Services sp. z o.o. was deleted. from the National Court Register.

Merger of BZWBK Leasing S.A. and BZWBK Lease S.A.

On 28.02.2017, BZ WBK Leasing S.A. and BZ WBK Lease S.A. merged.

The companies merged by way of absorption of BZ WBK Lease S.A. (the absorbed entity) by BZ WBK Leasing S.A. (the absorbing entity). All the assets of BZ WBK Lease S.A. were transferred to BZ WBK Leasing S.A. In connection with the merger, BZ WBK Lease S.A. ceased to exist legally, while BZ WBK Leasing S.A., being the absorbing entity, assumed, under the law, all the rights and obligations of the absorbed entity. As a result, BZ WBK Leasing S.A. continues business operations which previously were carried out by BZ WBK Lease S.A. and assumed, under the law, all the rights and obligations of absorbed BZ WBK Lease S.A.

in thousands of PLN

Registration of SC Poland Consumer 16-1 sp. z o.o.

On 17.05.2016, a subsidiary of Santander Consumer Bank trading as SC Poland Consumer 16-1 sp. z o.o. was registered. This is a special-purpose vehicle formed for the purpose of securitisation of a part of the credit portfolio, its shareholder being a Polish legal person that is not associated with the Group. As the control criteria set out in IFRS 10.7 are met, the company is considered as an entity controlled by Santander Consumer Bank.

A merger of BZ WBK Towarzystwo Funduszy Inwestycyjnych S.A. and BZ WBK Asset Management S.A. was completed, as a result of which BZ WBK TFI has acquired AM.

On 31.03.2016, a merger of BZ WBK Towarzystwo Funduszy Inwestycyjnych S.A. (BZ WBK TFI) and BZ WBK Asset Management S.A. (BZ WBK AM) was completed, as a result of which BZ WBK TFI has acquired AM.

The merger was executed by way of transfer of all assets of AM (the acquired company) to BZ WBK TFI (the acquiring company) in return for shares which BZ WBK TFI has allotted to the shareholders of the acquired company. The merger of the companies took effect on the date of entry of the merger into the register of businesses. Upon recording of the merger, AM has been deleted from the register of businesses. As of the merger date BZ WBK TFI has taken over all rights and obligations of its legal predecessor, i.e. AM. Business combinations under common control have no material impact on the financial statements.

Metrohouse Franchise S.A. shares sale transaction

On 22.01.2016, BZ WBK Inwestycje Sp. z o.o. sold all its shares of Metrohouse Franchise S.A. and ceased to be a shareholder of Metrohouse Franchise S.A.

48. Employee benefits

Staff benefits include the following categories:

- Short-term benefits (remuneration, social security contributions, paid leaves, profit distributions and bonuses and non-cash benefits). Value of short-term employee benefits are undiscounted,
- Post-employment benefits (retirement benefits and similar payments, life insurance or medical care provided after the term of employment).

Within these categories, the Bank Zachodni WBK creates the following types of provisions:

Provisions for unused holidays

Liabilities related to unused holidays are stated in the expected amount (based on current salaries) without discounting.

Provisions for employee bonuses

Liabilities related to bonuses system are stated in the amount of the probable payment without discounting.

Provisions for retirement allowances

Based on internal regulations in respect to remuneration, the employees of the Bank are entitled to defined benefits other than remuneration:

- a) retirement benefits,
- b) retirement pension.

The present value of such obligations is measured by an independent actuary using the projected unit credit method.

The amount of the retirement benefits and death-in-service benefits is dependent on length of service and amount of remuneration. The expected present value of the benefits is calculated, taking into account the financial discount rate and the probability of an individual getting to the retirement age or die while working respectively. The financial discount rate is determined by reference to up-to-date market yields of government bonds. The probability of an individual getting to the retirement age or die while working is determined using the multiple decrement model, taking into consideration the following risks: possibility of dismissal from service, risk of total disability to work and risk of death.

These defined benefit plans expose the Bank to actuarial risk, such as:

- interest rate risk – the decrease in market yields on government bonds would increase the defined benefit plans obligations,
- remuneration risk – the increase in remuneration of the Bank's employees would increase the defined benefit plans obligations,
- mobility risk – changes in the staff rotation ratio,

in thousands of PLN

- longevity risk – the increase in life expectancy of the Bank's employees would increase the defined benefit plans obligations.

The principal actuarial assumptions as at 31.12. 2017 are as follows:

- the discount rate at the level of 3.3% (3.6% as at 31.12.2016),
- the future salary growth rate at the level of 2.0% (2.0% as at 31.12.2016),
- the probable number of leaving employees calculated on the basis of historical data concerning personnel rotation in the Bank,
- the mortality adopted in accordance with Life Expectancy Tables for men and women, published the Central Statistical Office, adequately adjusted on the basis of historical data of the Bank.

Reconciliation of the present value of defined benefit plans obligations

The following table presents a reconciliation from the opening balances to closing balances for the present value of defined benefit plans obligations.

	31.12.2017	31.12.2016
Balance as at 1 January	55 737	59 322
Current service cost	308	1 073
Interest expense	1 916	1 772
Actuarial (gains) and losses	9 264	(6 430)
Balance as at 31 December	67 225	55 737

Sensitivity analysis

The following table presents how the impact on the defined benefits obligations would have increased (decreased) as a result of a change in the respective actuarial assumptions by one percent as at 31.12.2017.

Defined benefit plan obligations	1 percent increase	1 percent decrease
Discount rate	9,00%	-9,78%
Future salary growth rate	-9,91%	7,04%

The following table presents how the impact on the defined benefits obligations would have increased (decreased) as a result of a change in the respective actuarial assumptions by one percent as at 31.12.2016

Defined benefit plan obligations	1 percent increase	1 percent decrease
Discount rate	10,86%	-11,94%
Future salary growth rate	-12,10%	9,51%

Other staff-related provisions

These are provisions for the National Fund of Rehabilitation of the Disabled, redundancies, overtime and staff training. These liabilities are stated at the amounts of expected payment without discounting.

The balances of the respective provisions are shown in the table below:

Provisions	31.12.2017	31.12.2016
Provisions for unused holidays	45 297	51 700
Provisions for employee bonuses	213 451	195 663
Provisions for retirement allowances	67 225	55 737
Other staff-related provisions	14 797	8 587
Total	340 770	311 687

Detailed information about movements on staff-related provisions is available in Note 35.

49. Share based incentive scheme

The fifth edition of the BZW BK incentive scheme vested as at 30.06.2017. The vesting level is 63% for participants having significant impact on the Group's risk profile and at the level of 67% for participants not having significant impact on the Group's risk profile. Its

in thousands of PLN

realization through issuance of new shares and their allocation to individual accounts of entitled individuals was processed in Q3 2017.

On 17.05.2017, Annual General Meeting of the Shareholders of Bank Zachodni WBK S.A. approved three-year Incentive Scheme no. VI which participants are employees of the Bank Zachodni WBK Group (including Members of the Management Board), however not more than 250 individuals. On 26.06.2017 the Supervisory Board approved the list of entitled individuals ("grant date").

Vesting condition will be considered from two perspectives, separately for every year of operation of the scheme and on a cumulative basis after 3 years.

In every single year annual award not exceeding one third on total award will be considered. Shares will vest on a linear pattern between 25% and 100% contingent on profit after tax (PAT) growth and on RORWA ratio growth. The range of the scale requires PAT growth between "lower level" set to 80% of assumed level of realization in 2017 and "upper level" of nominal growth at 17,8% in first year and between "lower level" set to 80% of assumed level of realization in 2018 and 2019 and "upper level" of nominal growth at 13,4% in second and third year of duration of scheme. The range of the scale requires RORWA ratio growth between "lower level" set to 80% of assumed level of realization in 2017 and "upper level" of nominal growth at 2,24% in first year, between "lower level" set to 80% of assumed level of realization in 2018 and "upper level" of nominal growth at 2,37% in second year and between "lower level" set to 80% of assumed level of realization in 2019 and "upper level" of nominal growth at 2,5% in third year of duration of scheme.

Additionally the qualitative factors will be taken into account – participants are entitled to annual award depending on the level of customer satisfaction and engagement survey results. The level of customer satisfaction will be met when in the peer group Bank will be on second place in first and second year and on the first place in third year of duration of the scheme. The engagement survey results will not be lower than 50% in first year, 60% in second year and 70% in third year of duration of scheme.

Additionally, after 3 years cumulative award will be considered. Shares will vest on a linear pattern between 25% and 100% contingent on PAT compound annual growth rate in 3 years' time between 11,7% and 15% and on average value of RORWA ratio in 3 years' time between 1,9% and 2,38%. If number of shares resulting from cumulative assessment will be higher than sum of annual awards vested to date, additional shares will be allocated to individuals up to the amount resulting from cumulative assessment.

The Black Scholes model has been used to value awards granted at the grant date. The expected volatility of the values of shares is based on an analysis of historical volatility of share prices based on 160 sessions preceding the grant date. The following table details the assumptions used, and the resulting fair value.

Share based payments granted in 2017:

	2017
Number of share based payments	131 262
Share price (PLN)	350,00
Exercise price	10
Vesting period	3 years
Expected volatility of share prices	30,07%
Award life	3 years
Discounted risk free rate	2,12%
Fair value per award	323,36 zł
Dividend yield	1,71%

The following table summarizes the share based payments activity:

	12 months of 2017 based payments	12 months of 2016 based payments
Outstanding at 1 January	157 254	168 784
Granted	131 912	-
Exercised	(100 233)	-
Forfeited	(3 958)	(11 530)
Expired	(55 176)	-
Outstanding at 31 December	129 799	157 254
Exercisable at 31 December	-	-

The expired rights presented in the table for 12 months of 2017 represent the lower level of the vested rights for the Incentive Scheme V.

For the share based payments outstanding as at 31.12.2017 and as at 31.12.2016 the average remaining contractual life is approximately 2.5 years and 0.5 year respectively.

The expenses of sixth edition of equity settled share-based payments scheme recognized in profit and loss account for 12 months of 2017 amounts to PLN 6,957 k.

in thousands of PLN

The table below presents information about the number of conditional rights to shares vested in BZ WBK Management Board members under the 5th Incentive Scheme and the 6th Incentive Scheme launched in 2017. The rights may be exercised only in part depending on the future performance of the Group. Information about the rights exercised in full or in part will be provided in the future reports.

No. of awards	2017	2016
Outstanding at 1 January	17 671	17 918
Granted	35 687	1 253
Expired	(6 053)	-
Exercised	(10 541)	-
Resignation from the function	(2 094)	(1 500)
As at 31 December	34 670	17 671

The table below presents information about the number of conditional rights to shares vested in BZ WBK Key Management.

No. of awards	2017	2016
Outstanding at 1 January	28 615	27 550
Granted	40 214	1 065
Expired	(8 451)	-
Exercised	(17 849)	-
Resignation from the function	(5 255)	-
As at 31 December	37 274	28 615

50. Dividend per share

As of the date of publication of this report, the Management Board of Bank Zachodni WBK has not finalised its analysis in respect of recommendation on dividend payout for 2017.

On 17.05.2017 Annual General Meeting of Bank Zachodni WBK S.A. adopted a resolution on dividend payment.

It was decided to allocate PLN 535,866k from the Bank's undivided net profit for 2014 and 2015 to dividend for shareholders.

Dividend per share was PLN 5.40.

51. Operating segments reporting

Operating segments reporting were presented in "Consolidated Financial Statement of Bank Zachodni WBK Group for 2017" released on 13.02.2018.

52. Events which occurred subsequently to the end of the period

Issuance of own bonds by Bank Zachodni WBK

The Management Board of Bank Zachodni WBK S.A. informed that on 7.02.2018, it adopted a resolution approving the issuance by the Bank of subordinated bonds with a total nominal value not higher than PLN 1,000,000 k, to be qualified as Tier II instruments of the Bank subject to the consent from the Polish Financial Supervision Authority.

The Bonds will be offered solely on the territory of Poland. The Bonds may be issued in one or several series. The Bank plans to carry out the issuance by 30.06.2018. Details of the issuance will be communicated at a later date.


Signatures of Members of the Management Board

Date	Name	Function	Signature
12.02.2018	Michał Gajewski	President	
12.02.2018	Andrzej Burliga	Vice-President	
12.02.2018	Michael McCarthy	Vice-President	
12.02.2018	Juan de Porras Aguirre	Vice-President	
12.02.2018	Miroslaw Skiba	Vice-President	
12.02.2018	Feliks Szyszkowiak	Vice-President	
12.02.2018	Artur Chodacki	Member	
12.02.2018	Carlos Polaino Izquierdo	Member	
12.02.2018	Marcin Prell	Member	
12.02.2018	Arkadiusz Przybyl	Member	
12.02.2018	Maciej Reluga	Member	
12.02.2018	Dorota Strojowska	Member	

Signature of a person who is responsible for maintaining the book of account

Date	Name	Function	Signature
12.02.2018	Wojciech Skalski	Financial Accounting Area Director	