

# Report on the activity of the Supervisory Board Santander Bank Polska S.A.

Warsaw, April 2019



# Spis treści

	1
<b>I. ACTIVITIES OF THE SUPERVISORY BOARD OF SANTANDER BANK POLSKA S.A. IN 2018 .....</b>	<b>3</b>
1. SUPERVISORY BOARD COMPOSITION; DISCHARGE OF DUTIES AND RESPONSIBILITIES	3
1.2. Changes in the Supervisory Board's composition	3
1.3. Independence of the Supervisory Board members	3
2. STATISTICAL DATA ON THE SUPERVISORY BOARD'S ACTIVITY IN 2018	4
3. MAJOR AREAS OF THE SUPERVISORY BOARD'S ACTIVITY IN 2018	4
4. ACTIVITIES OF THE SUPERVISORY BOARD AND ITS COMMITTEES	7
4.1. NOMINATIONS COMMITTEE	8
4.2. REMUNERATION COMMITTEE	9
4.3. AUDIT & COMPLIANCE COMMITTEE	10
4.4. RISK COMMITTEE	14
5. SELF-ASSESSMENT OF THE SUPERVISORY BOARD ACTIVITY IN 2018	16
<b>II. REPORT OF THE SUPERVISORY BOARD ON THE EXAMINATION OF 2018 FINANCIAL STATEMENTS, THE MANAGEMENT BOARD REPORT ON PERFORMANCE IN 2018 AND THE BANK'S MANAGEMENT BOARD'S MOTION WITH REGARD TO THE DISTRIBUTION OF PROFIT FOR 2018 AND UNDISTRIBUTED PROFIT FOR 2016 AND 2017.....</b>	<b>17</b>
1. EXAMINATION OF 2018 FINANCIAL STATEMENTS, THE MANAGEMENT BOARD REPORT ON PERFORMANCE IN 2018	17
2. REVIEW OF THE BANK'S MANAGEMENT BOARD MOTION WITH REGARD TO DISTRIBUTION OF PROFIT FOR 2018 AND UNDISTRIBUTED PROFIT FOR 2016 AND 2017	18
<b>III. ASSESSMENT OF SANTANDER BANK POLSKA GROUP'S PERFORMANCE IN 2018 .....</b>	<b>20</b>
1. SANTANDER BANK POLSKA GROUP PERFORMANCE IN 2018	20
2. ASSESSMENT OF THE INTERNAL CONTROL SYSTEM	23
3. ASSESSMENT OF COMPLIANCE	26
4. ASSESSMENT OF THE INTERNAL AUDIT FUNCTION	27
5. ASSESSMENT OF THE RISK MANAGEMENT SYSTEM	29
6. ASSESSMENT OF SPONSORING AND CORPORATE GIVING POLICY OF SANTANDER BANK POLSKA S.A.	30
7. SUPERVISORY BOARD'S ASSESSMENT OF THE MANNER OF FULFILLING BY SANTANDER BANK POLSKA S.A. THE DISCLOSURE REQUIREMENTS WITH REGARD TO THE CORPORATE GOVERNANCE RULES SET OUT IN THE WSE RULES AND REGULATIONS PERTAINING TO CURRENT AND PERIODIC INFORMATION PUBLISHED BY ISSUERS OF SECURITIES	31
8. SUMMARY	31
<b>IV. ASSESSMENT OF COMPLIANCE WITH THE CORPORATE GOVERNANCE RULES FOR SUPERVISED INSTITUTIONS.....</b>	<b>33</b>
<b>V. ASSESSMENT OF THE REMUNERATION POLICY OF SANTANDER BANK POLSKA S.A</b>	<b>34</b>

# I. ACTIVITIES OF THE SUPERVISORY BOARD OF SANTANDER BANK POLSKA S.A. IN 2018

## 1. SUPERVISORY BOARD COMPOSITION; DISCHARGE OF DUTIES AND RESPONSIBILITIES

In the period from 1 January to 31 December 2018, the Supervisory Board of Santander Bank Polska S.A. worked in the following composition

- Gerry Byrne – Chairman of the Supervisory Board
- Jose Luis de Mora - Vice-Chairman of the Supervisory Board
- José Garcia Cantera
- Danuta Dąbrowska
- David Hexter
- Witold Jurcewicz
- John Power
- Jerzy Surma
- Marynika Woroszyńska-Sapieha
- José Manuel Campa

All Supervisory Board members were appointed for a joint three-year term of office by the Annual General Meeting of Shareholders on 17 April 2017.

On 10 December 2018, the Nominations Committee of the Supervisory Board confirmed the validity of the individual assessments for the Supervisory Board members as well as their collective assessment that was recommended on 11 May 2017 to the Annual General Meeting in view of nominating members of the Supervisory Board for their current term of office. This Assessment was made in line with the Policy on selection and suitability assessment of Supervisory Board members in Santander Bank Polska S.A. adopted by the Annual General Meeting on 20 April 2016.

The diversified personal composition of the Supervisory Board, with members having both business experience as well as expert knowledge in different areas, evidenced by many years of practical professional experience, ensures adequate and effective discharge of supervisory duties and warrants the due performance of the vested duties and responsibilities. The curricula vitae of the Supervisory Board members are available at the Bank's website.

Information on the composition of the Supervisory Board's committees is presented in point 4 below.

### 1.1. Changes in the Supervisory Board's composition

In 2018, there were no changes in the Supervisory Board's composition.

### 1.2. Independence of the Supervisory Board members

In line with the criteria of independence for the Supervisory Board members set out in paragraph 25 (2) of the Bank's Statutes, the Supervisory Board Regulations and in the Audit and Compliance Committee's terms of reference, the following individuals held the status of the independent members:

- Danuta Dąbrowska,
- Marynika Woroszyńska-Sapieha,
- David Hexter,
- Witold Jurcewicz,

- Jerzy Surma

Each of the listed persons made a relevant written statement.

1.3. The Supervisory Board activities and manner of discharging its duties and responsibilities are governed by the Supervisory Board's Regulations available in the Board's Office and on the Bank's Internet site.

## 2. STATISTICAL DATA ON THE SUPERVISORY BOARD'S ACTIVITY IN 2018

In the period from 1 January to 31 December 2018, 11 Supervisory Board meetings were held at which 99 resolutions were passed. Average attendance of the Supervisory Board members was 95.45%.

## 3. MAJOR AREAS OF THE SUPERVISORY BOARD'S ACTIVITY IN 2018

The Supervisory Board carried out its activities based on the adopted schedule of meetings and the general work plan. The agenda of each meeting was extended (if required) by current business matters, issues submitted by the Bank's Management Board for consideration and any other issues the Board deemed necessary to be covered by the agenda. The Supervisory Board requested and received from the Bank's Management Board comprehensive materials and reports on issues covered by the agenda of meetings as well as those pertaining to other matters important to the Bank's operations.

The Supervisory Board's activities are described in detail in the minutes of its meetings which together with the adopted resolutions are kept in the Bank's registered office.

Irrespective of regular meetings, the Supervisory Board members stayed in regular contact with the Bank's Management Board which facilitated comprehensive oversight of the Management Board's operations.

In 2018, the Supervisory Board focused both on strategic matters as well as on the supervision of the Bank's day-to-day business. Individual issues were also discussed by the relevant Supervisory Board's committees which issued required opinions and recommendations to the Supervisory Board.

In 2018, the Supervisory Board activities concerned in particular the following areas:

### Strategic projects

The Supervisory Board exercised on-going oversight of strategic projects progressed in the Bank in 2018, including Agile, rebranding, establishment of the Mortgage Bank (including approval of setting it up as the Bank's subsidiary), acquisition of the organised part of the enterprise of Deutsche Bank Polska S.A. (including a positive opinion on the Management Board's resolution re. seeking the Polish Financial Supervision Authority's permit for the demerger of Deutsche Bank Polska S.A. and supervision of preparations for the operational and legal merger).

The Supervisory Board member, John Power, seconded by the Supervisory Board to exercise ongoing, individual oversight of the process presented regular reports in this respect to the Supervisory Board. Particular attention was paid to the management of risk attached to the taken-over exposures, models' calibration, ensuring liquidity of assets upon their acquisition, calculating and reporting provisions and allowances for expected credit losses, mitigation of the operational risk triggered by the merger of the portfolios and data migration.

### Finance

The Supervisory Board assessed the actual and forecast financial performance of the Bank and Santander Bank Polska S.A. Group on an on-going basis. The assessment was based on financial reports regularly presented by the Bank's Management Board. As part of the reports presented by the Management Board President, at each meeting the Supervisory Board was updated on the key developments referring to the Bank and its environment, including up-to-date macroeconomic and market forecasts and their impact on the Polish economy as well as on the Bank's and Santander Bank Polska Group's financial and business performance.

The Supervisory Board was also updated by the Bank's Management Board about current priorities and the approach adopted to management of funding, liquidity, capital, risk (including credit risk) and costs. Given the key importance of liquidity and funding, the related information covered the scenarios / strategies developed by the Management Board as well as actions taken to manage liquidity and diversify funding sources, also in the context of the liquidity management strategy given the acquisition of the organised part of enterprise of the Deutsche Bank Polska S.A.



In particular, the Supervisory Board:

- assessed the Financial Statements of Bank Zachodni WBK S.A. for 2017, Consolidated Financial Statements of the Bank Zachodni WBK S.A. Group for 2017 and the Management Board Report on the Performance of Bank Zachodni WBK S.A. Group for 2017 comprising the Management Board Report on the Bank Zachodni WBK S.A. Performance in 2017,
- approved the "Financial Plan Policy – balance sheet planning",
- approved the "ALM Strategy for 2018 – 2020",
- approved the "Group's Financial Plan for 2018" and its updates,
- approved the Management Board's Resolution re. approval of disclosures with regard to the capital adequacy of Bank Zachodni WBK S.A. Group as at 31 December 2017,
- approved the "Rules for assessing the internal capital adequacy in Bank Zachodni WBK S.A.(BZ WBK ICAAP Policy) and ICAAP Report as at 31 December 2017,
- approved the Report on the Internal Liquidity Adequacy Assessment Process (ILAAP Report),
- issued an opinion with regard to the Management Board's motion on the distribution of profit for 2017 and the undistributed profit for 2016,
- reviewed and approved "Bank Zachodni WBK S.A. Group Strategic Plan 2025",
- approved "2019-2021 Financial Plan of Santander Bank Polska S.A. Group" and reviewed the assumptions of "2019 Financial Plan",
- approved "Santander Bank Polska S.A. Group Strategy for 2018-2020" and "Santander Bank Polska Group Strategy for 2019-2021" as well as "2019 Business Plan",
- reviewed and approved the "Financial Plan Document – ALM Strategy for 2019 – 2021".

## Relationship with the External Auditor

The Supervisory Board reviewed and accepted the Bank Management Board's and the Audit and Compliance Committee's recommendations on positive assessment of the relationship with PricewaterhouseCoopers sp. z o.o. (now:PricewaterhouseCoopers Polska sp. z o.o. Audyt sp. k.), hereinafter "**PwC**".

By force of Resolution No 82/2018 of 12 December 2018, the Supervisory Board reappointed PwC to perform the semi-annual audit of the Bank's financial statements and semi-annual audit of consolidated financial statements of the Bank's Group for H1 2019 as well as to perform the annual audit of the Bank's financial statements and annual audit of consolidated financial statements of the Bank's Group for 2019.

## Internal Audit

The Supervisory Board was provided with regular updates on the Internal Audit Area's (IAA) operations, in particular on the results of the carried out audits and performance against the post-audit recommendations in reports given by the Chairman of the Audit and Compliance Committee, reports presented directly at the Supervisory Board meetings by the Chief Audit Executive as well as in reports given by the internal audit of Santander Broker Poland. The results of the Supervisory Board's assessment of the Internal Audit function are presented below.

The Supervisory Board *inter alia*:

- approved the IAA Strategic (long-term) Plan for 2018 – 2020 and the Operational (annual) Plan for 2018 as well as changes to these plans that were reported throughout 2018,
- approved the IAA Strategic (long-term) Plan for 2019 – 2021 and Operational Plan for 2019,
- considered and approved the Internal Audit Quality Assurance and Improvement Program Report,
- approved the internal regulations concerning the Internal Audit function and their amendments, including the Audit Charter, Methodology Manual of Internal Audit Area, Policy of co-operation with the Parent entity, Santander Brokerage Poland's Internal Audit Terms of Reference.

## Regulatory and Compliance issues

The Supervisory Board was regularly updated on the operations of the compliance unit and on compliance risk issues, both in reports given by the Chairman of the Audit and Compliance Committee and reports presented directly at the Supervisory Board meetings by the head of that unit as well as in the reports on the compliance function in Santander Brokerage Poland. The results of the Supervisory Board's assessment of the compliance unit and compliance risk management function are presented below.

In particular, the Supervisory Board:

- approved the Compliance Programme for 2018 as well as new and amended internal regulations of the compliance unit, including its Terms of Reference and Compliance Policy, the Reputation Risk Management Model comprising the "Reputation Risk Management Methodology" and "Reputation Risk Management Procedure", a document defining the rights and duties of the Chief Compliance Officer, and the compliance unit's reporting rules,
- positively assessed the whistleblowing procedure,
- received reports on material court proceedings to which the Bank was a party, on proceedings instigated by regulators, on the status of delivering the KNF's post-inspection recommendations along with assurance that the process was executed in an adequate and timely manner, information on the results of the supervisory review and evaluation (BION) and on the course of this process in the Bank,
- acknowledged the report on supervision of compliance of custodian services for 2017,
- in line with Recommendation U and the Bancassurance Policy applicable in the Bank, the Supervisory Board was provided with regular updates on that business and on bancassurance risk management issues and reviewed them.

## Risk management system and internal control system

As part of supervision exercised over the risk management system, during each meeting the Supervisory Board carried out a review of the main risk areas based on the Risk Dashboard report and paid special attention to, amongst others, trends, consumption of limits set in the Risk Appetite Statement, supervision over individual risk types, compliance with internal regulations and the KNF recommendations, the EU and the EBA regulations, as well as, to adequate identification of threats and determination of management actions. The Supervisory Board was also provided with information on the credit strategy, credit risk and condition of the credit portfolio, operational risk and other risks embedded in the Bank's operations.

Based on the conducted review, the Supervisory Board approved the risk appetite for 2018, expressed as limits set out in the Risk Appetite Statement (RAS), approved RAS updates throughout the year and monitored compliance with it..

The Supervisory Board received updates on risk management and control environment in the Bank's individual units and subsidiaries, including a report on annual ICM/SOX certification. IT security issues and Cybersecurity Strategy were given special attention.

The assessment of the internal control system and risk management system made by the Supervisory Board is presented below.

In particular, the Supervisory Board approved the following internal regulations or amendments to them:

- Santander Bank Polska S.A. Group Operational Risk Management Strategy,
- Concentration Risk Management Policy,
- Scenario Analyses Framework,
- Credit Risk Management Policy,
- policies concerning structural, market, liquidity and fx risks as well as the treasury products valuation,
- Internal Control System Policy, Control Function Matrix Methodology, Assurance and Quality Model,
- Risk Management Strategy.

## Appointment of the Management Board for the new term of office

Given the expiry of the Management Board's term of office on the date of holding the Annual General Meeting of Shareholders approving the financial statements for 2017, the Supervisory Board appointed the Management Board for the new term of office in the following composition:

- Michał Gajewski – President of the Management Board
- Andrzej Burliga – Vice President of the Management Board
- Michael McCarthy – Vice President of the Management Board
- Carols Polaino Izquierdo – member of the Bank Management Board
- Arkadiusz Przybył – Vice President of the Bank Management Board
- Maciej Reluga – member of the Bank Management Board
- Dorota Strojowska – member of the Bank Management Board
- Feliks Szyzkowski – Vice President of the Management Board

- Juan de Porras Aguirre – Vice President of the Bank Management Board

The Supervisory Board assessed suitability of each of the above mentioned individuals as compliant with the requirements of Article 22aa of the Banking Law and performed collective suitability assessment of the Management Board. The Supervisory Board approved also the internal allocation of powers in the Bank's Management Board.

## Other issues

- The Supervisory Board reviewed the strategy and activity of individual business segments, areas of the Bank and its subsidiaries, and was regularly informed about progress in implementing regulatory projects significant for the Bank,
- The Supervisory Board monitored the status of work on preparing the Recovery Plan and approved the Group's Recovery Plan along with the related Policies,
- Apart from the regulations indicated above, the Supervisory Board approved other internal regulations and amendments to them as recommended by relevant committees, e.g.: Management Board Diversity Policy, Management Board members' Induction and Training Policy, Procedure for Setting Objectives and Evaluating Performance for members of Management Board, policies on nominating, selecting and assessing the suitability of the Management Board members and key function holders,
- The Supervisory Board considered and approved the level of remuneration and bonuses for the Management Board members and other key function holders in line with the applicable regulations, changes to the Remuneration Policy of the Bank's Group and other internal regulations in this respect,
- The Supervisory Board issued positive opinions on the Management Board motions with regard to changing the Bank's name to Santander Bank Polska S.A and relocating the Bank's seat to Warsaw, changes to the Bank's Statutes, approval of the Organisational Regulations as well as draft AGM resolutions. The Supervisory Board approved the consolidated text of the Bank's Statutes.

## 4. ACTIVITIES OF THE SUPERVISORY BOARD AND ITS COMMITTEES

In 2018, the Supervisory Board members worked in the following Supervisory Board's committees:

- Nominations Committee,
- Remuneration Committee,
- Audit and Compliance Committee,
- Risk Committee.

The Committees' respective procedures are set out in their Terms of Reference, introduced by relevant resolutions of the Supervisory Board. Terms of Reference of individual committees are available in the Board Office.

The members of individual Committees have knowledge and experience suitable for their roles and adequate discharge of their duties and responsibilities.

The Committees contribute a lot to improving the effectiveness of the Supervisory Board's work by supporting it in the discharge of its statutory duties, including the preparation of opinions and recommendations on specific matters considered by the Supervisory Board.

In order to enable the Supervisory Board members to appraise in full the Committees' work and give them insight into the Committees' current operations, the Chairpersons present relevant reports at the meetings of the Supervisory Board and the Supervisory Board members are provided with copies of the minutes of each meeting of the Committees.

Individual Committees received adequate information and reports from the Management Board in a timely manner allowing them to discharge their responsibilities in 2018.

## 4.1. NOMINATIONS COMMITTEE

### Role and Tasks of the Committee

The role of the Nominations Committee is to support the Supervisory Board in performing its tasks by issuing recommendations on appointing and removing members of the Supervisory Board, Management Board and other key function holders by the Bank's relevant body as well as by engaging in discharging the Bank's duties related to assessing the suitability of members of the Supervisory Board, Management Board and key function holders.

### Terms of Reference

The Committee operates based on the Terms of Reference approved by the Supervisory Board and updated in 2018 by force of the Supervisory Board Resolution No 51/2018 of 11 July 2018; the introduced changes resulted from amendments to the Banking Law and Regulation of the Minister of Finance on specific tasks of the nomination committees in systemically important banks of 7 May 2018 and consisted in introducing new duties of the Committee (setting a target for the gender underrepresented in the Management Board and developing a diversity policy to reach the target gender representation).

### Committee composition

In 2018, the Nominations Committee worked in the following composition:

- Witold Jurcewicz – Chairman of the Committee
- Gerry Byrne,
- Danuta Dąbrowska,
- José Luis de Mora,
- Marynika Woroszyńska-Sapieha,
- Jerzy Surma

### Number of meetings and attendance

In the period between 1 January and 31 December 2018, the Nominations Committee held 4 meetings with the full attendance of all members.

### The Committee's activity in 2018

In its activities in 2018, the Committee focused in particular on the following issues:

- Changes in the Management Board's composition – given the expiry of the current term of office of the Management Board on the day of approving the Bank's Financial Statements for 2017 by the Bank's Annual General Meeting of Shareholders, the Committee recommended to the Supervisory Board changes in the Management Board's composition and allocation of duties within the Management Board for the new term of office, including the reduction of the number of members from 12 to 9. In execution of the then applicable "Policy on Selection and Suitability Assessment of Management Board members and Key Function Holders in Bank Zachodni WBK S.A.", the Committee recommended individual suitability assessment of candidates to the Management Board for the new term of office as well as collective suitability assessment of the Management Board;
- "Management Board Diversity Policy" – given the stipulations of the Regulation of Minister of Finance on specific tasks of the nomination committees in systemically important banks of 7 May 2018 as well as joint ESMA and EBA Guidelines on the assessment of the suitability of members of the management body and key function holders EBA/GL/2017/12, the Committee defined the target for representation of the underrepresented gender on the Management Board, developed the Management Board Diversity Policy and recommended its approval to the Supervisory Board;
- "Santander Bank Polska Management Board members' Induction and Training Policy" and "Policy on selection and suitability assessment of Management Board members and key function holders in Santander Bank Polska S.A." – the



Committee provided the Supervisory Board with a recommendation to approve these policies in view of the requirements arising from the above mentioned Guidelines EBA/GL/2017/12;

- Assessment of the individual and collective suitability of the Supervisory Board members – the Committee confirmed the validity of the individual suitability assessment for the Supervisory Board members as well as its collective suitability assessment that was recommended on 11 May 2017 to the Annual General Meeting of Shareholders in view of nominating members of the Supervisory Board for its current term of office.

## 4.2. REMUNERATION COMMITTEE

### Role and Tasks of the Committee

The role of the Remuneration Committee is to support the Supervisory Board in performing its tasks concerning remuneration of the members of the Bank's governing bodies and key function holders, to review and monitor the Remuneration Policy and to support the Annual General Meeting of Shareholders, Supervisory Board and Management Board in designing and executing this Policy.

### Terms of Reference

The Committee operates based on the Terms of Reference approved by the Supervisory Board and updated in 2017 by force of the Supervisory Board Resolution No 40/2017 of 17 May 2017.

### Committee composition

In 2018, the Remuneration Committee worked in the following composition:

- Danuta Dąbrowska – Chairperson of the Committee
- Gerry Byrne,
- José Luis de Mora,
- Witold Jurcewicz,
- Marynika Woroszyńska-Sapieha

### Number of meetings and attendance

Between 1 January and 31 December 2018, the Remuneration Committee held 5 meetings with the full attendance of all members.

### The Committee's activity in 2018

In its activities in 2018, the Committee focused in particular on the following issues:

- Evaluation of the Management Board members' performance – in line with the applicable "Procedure for setting objectives and evaluating performance of the Management Board members", the Committee approved the evaluation of the Management Board President's and other members' performance for 2017 as well as provided the Supervisory Board with recommendations on setting objectives and development plans for the Management Board members for the entire 2018;
- Recommendation to the Supervisory Board on bonuses to be awarded to the Management Board members for 2017 and on the approval of rules for setting and allocating the bonus pool in 2018;
- Recommendation to the Supervisory Board with regard to awarding a bonus to the Chief Audit Executive, Director of the Compliance Area and review of remuneration of these individuals as well as other employees in charge of risk management in line with the requirements of the Regulation of the Minister of Development and Finance of 6 March 2017 on the risk management system and internal control system, remuneration policy and detailed method of internal capital estimation in banks;
- The Committee reviewed and assessed the compliance with the triggers for payment of variable remuneration to the individuals with the status of Identified Employees and recommended that the Supervisory Board approved 2014, 2015 and 2016 deferred payments to be made in 2017;

- The Committee reviewed the bonus schemes for the senior executives, management cadre, employees of the Business Support Centre and the Branch Banking;
- The Committee confirmed the allocation of shares for 2017 under the Incentive Scheme VI (2017 – 2019) as well as analysed the external review of that scheme and confirmed its compliance with the regulations on variable components of remuneration for the Identified Employees;
- The Committee reviewed changes proposed to the Bank Group's Remuneration Policy introduced to align it to MiFID and EBA Guidelines on remuneration policies and practices and recommended their approval to the Supervisory Board;
- The Committee reviewed the Bank Group's Remuneration Policy and the Policy on remuneration for the Management Board members and presented a related recommendation to the Supervisory Board;
- Given the appointment of the Management Board for the new term of office, the Committee recommended a template employment contract to be signed with the Management Board members and provided the Supervisory Board with recommendations with regard to the remuneration for the Management Board members, including base salaries and base bonuses, and with regard to adjusting the maximum ratio of variable to fixed components at 100% for the Management Board members performing independent control functions;
- The Committee provided the Supervisory Board with recommendations with regard to the approval of Malus clause procedure that defines how to identify the events for risk-adjustment of remuneration as well as the rules for preventing the vesting of bonus entitlement (either in full or in part) to the Identified Employees whose activities have a significant impact on the Bank's risk profile (Material Risk Takers); The Committee also reviewed and recommended to the Supervisory Board the list of Identified Employees, i.e. the Material Risk Takers for 2018 and its update;
- The Committee reviewed the rules for remuneration for the Identified Employees performing control functions in order to ensure the maximum ratio between the variable and the fixed components of remuneration at the level of 100% in line with the applicable regulations;
- The Committee provided the Supervisory Board with a recommendation with regard to the update of "Procedure for setting objectives and performance evaluation for the Management Board members";
- The Committee provided recommendations with regard to the compensation for the Supervisory Board member seconded to exercise individual ongoing oversight of the project consisting in acquiring an organised part of the enterprise of Deutsche Bank Polska S.A.

### 4.3. AUDIT & COMPLIANCE COMMITTEE

#### Role and Tasks of the Committee

The purpose of the Audit and Compliance Committee is to support the Supervisory Board in discharging its oversight responsibilities to shareholders and other stakeholders in relation to: (i) the quality and integrity of the accounting policies, financial statements and disclosure practices; (ii) the Bank's compliance with laws and internal regulations; (iii) the independence of internal and external auditors and evaluating their performance; (iv) the assessment of the effectiveness of the system of internal control and the management of financial and non-financial risks.

#### Terms of Reference

The Committee operates under the Terms of Reference approved by the Supervisory Board, which were amended twice in 2018 – by force of resolution of the Supervisory Board Resolution No 69/2018 of 26 September 2018 primarily in relation to the internal audit function and Resolution No 85/2018 of 12 December in relation to the compliance unit; these amendments were introduced to comply with the KNF's instructions and Recommendations, including Recommendation H.

#### Committee composition

From 1 January 2018 to 31 December 2018, the Audit and Compliance Committee was composed of:

- David Hexter – Chairman,
- Danuta Dąbrowska,
- Witold Jurcewicz,
- Marynika Woroszyńska-Sapieha,

- Jerzy Surma

All members appointed by the Supervisory Board to the Committee for the Supervisory Board's term of office meet the independence criteria of the Poland's Auditors Act of 11 May 2017 and the Bank's Statutes, which was confirmed by written statements provided by all the Committee members.

## Number of meetings and attendance

In 2018, the Committee met 6 times and the attendance was as follows:

- |                                |     |
|--------------------------------|-----|
| • David Hexter                 | 6/6 |
| • Danuta Dabrowska             | 6/6 |
| • Witold Jurcewicz             | 6/6 |
| • Marynika Woroszylska-Sapieha | 6/6 |
| • Jerzy Surma                  | 6/6 |

Apart from the Committee's members, the regular attendees are also representatives of the Bank's Auditor, the Vice President of the Management Board in charge of the Risk Management Division, the member of the Management Board in charge of Accounting and Financial Control Division, the member of the Management Board in charge of the Financial Management Division, the Director of the Internal Audit Area (Chief Audit Executive) and Bank Director in charge of Legal and Compliance Division. Other members of the Management Board and executives are also invited to attend as appropriate in order to present reports and discuss issues related to the areas under their management, including the explanation of the reasons for those reports of the Internal Audit that indicate areas for improvement as well as proposed remediation plans.

## The Committee's activity in 2018

The Committee reviewed key areas of material controls, especially those relating to financial, operational, and regulatory compliance controls. The Committee monitored the operations of the internal audit function, compliance unit and control function as well as reviewed regularly the legal and regulatory issues, compliance issues, corporate governance matters, anti-money laundering, ICM/SOX certification and other issues in order to make the assessment and present to the Supervisory Board the opinion on the effectiveness and adequacy of internal control system.

The main areas reviewed in more detail by the Audit and Compliance Committee in 2018 included:

### Financial reporting

The Committee reviewed the Bank's and the Bank Group's audited Financial Statements for 2017 and discussed their content with the Management Board. Particular attention was paid to the level of IBNR provisions for each credit portfolio and the impact of key changes in the accounting standards on the financial statements such as the quantitative impact of the implementation of IFRS9 in relation to capital adequacy, the implementation status of IFRS 16 in relation to leases and the different method of Bank Guarantee Fund cost calculation as a consequence of the amended Act on the Bank Guarantee Fund.

The Committee discussed with the Auditor the results the Financial Statements' review and issues reported in this respect to the Management Board as well as reviewed the additional Report to the Audit and Compliance Committee, and thereafter, monitored the performance against the External Auditor's recommendations presented therein.

Based on the detailed review of the Financial Statements and the additional Report to the Committee, it was decided to recommend that the Supervisory Board approve the audited Financial Statements for inclusion in the Company's annual report for the year ended 31 December 2017, and the Supervisory Board endorsed the Committee's recommendation.

The Committee reviewed the reports on the Capital Adequacy and the work of the Disclosure Committee in 2017 and noted that capital ratios were above the KNF's minimum requirements.

### Internal Audit

The activity of the Internal Audit Area was subject to regular supervision and assessment of the Committee.

The Committee receives, through the Chief Audit Executive, reports on the operation of internal controls within the Group. The scope, timing and frequency of such reports depend on the Audit Plan.

The Committee positively assessed the strategic (long-term) Audit Plan 2018 – 2020 and the Operational Audit Plan 2018 and recommended their approval to the Supervisory Board.

The reports are presented in a manner that allows the Committee to focus on high risk areas which need improved controls. Objective indicators to track the delivery of remediation commitments across the Group were developed, whilst the Chief Audit Executive presented to the Committee regular reports on compliance with these indicators.

The Committee monitored on a on-going basis the performance against the Audit Plan and post-audit recommendations as well as analysed and presented to the Supervisory Board recommendations on changes to that Plan across 2018.

The Committee approved the Internal Audit Area's budget for 2018 as well as reviewed the remuneration and staffing levels in the Internal Audit Area. This process was of particular importance in 2018 given labour market pressures, the changing skill requirements in the audit world and the need to fully comply with regulatory requirements regarding independence. In the Committee's opinion the staffing levels in the Internal Audit Area were adequate and the Area maintained its independence, also as required under Standard 110 of the International Standards for the Professional practice of Internal Auditing and the KNF's Recommendation H.

The Committee was also presented with the external assessment of the Internal Audit Area made by an independent entity to confirm compliance with the KNF's Recommendation H and correctness of implementing the post-inspection recommendations.

The Committee reviewed the Internal Quality Assurance and Improvement Program Report in line with the KNF's recommendation H (overall assessment – satisfactory).

The Committee also analysed proposed changes to internal regulations concerning the Internal Audit Area and recommended their approval to the Supervisory Board.

## External Audit

There is a process in place whereby the Audit and Compliance Committee reviews and approves, within parameters established by the Supervisory Board, any non-audit services undertaken by the Auditor, and the related fees. The process ensures that the objectivity and independence of the Auditor is safeguarded.

In 2018, Santander Bank Polska Group paid PLN 5 223 619 PLN (net) to the External Auditor for audit and review services relating to the statutory audit of the Group and Bank financial statements and subsidiaries (including Santander Consumer Bank) pursuant to legislation.

The fees for non-audit services amounted to PLN 1 401 600 (net). The total fees paid to PWC were PLN 6 625 219m (net).

The Committee is satisfied that the External Auditor provides an effective independent assessment of the integrity of the Bank's Financial Statements and the adequacy of its internal control systems. Moreover, the Auditor's Report from the review of the Financial Statements and additional Report to the Audit and Compliance Committee provide valuable recommendations regarding the improvement of internal controls. Ensuring adequate and timely follow-up of these recommendations is part of the regular business of the Committee. The Committee was also provided with a written statement from the External Auditor confirming their independence pursuant to Articles 69-74 of Poland's Auditor Act of 11 May 2017.

Based on the Audit and Compliance Committee's recommendation, the Supervisory Board appointed PricewaterhouseCoopers spółka z ograniczoną odpowiedzialnością Audytyt sp.k. (PWC) as the audit firm entitled to perform semi-annual audit of the Bank's financial statements and semi-annual audit of consolidated financial statements of Santander Bank Polska Group for H1 2019 and the annual audit of the Bank's financial statements and the Group's consolidated financial statements for 2019.

When recommending PWC's reappointment, the Committee took into account the KNF's stance requiring the change of the auditor every five years. The process was conducted in line with the Bank's policy on appointing the auditor and included, among others, the assessment of the PWC's independence and the quality of services provided to-date.

The Bank is fully compliant with the Poland's Auditor's Act of 11 May 2017 which refers to selection of the External Auditor and determines the scope of audit and non-audit services.

## Compliance

The operations of the compliance unit were subject to on-going monitoring by the Committee which acknowledged the report of the unit's activity in 2017 as well as assessed and recommended to the Supervisory Board the approval of 2018 Compliance Programme. The performance against the Programme was supervised by the Committee also as part of the unit's reports presented at each Committee's meeting.

The Committee positively assessed actions taken to implement the Target Operating Model as well as changes in the unit's organisational structure that took place in 2018.

The Committee analysed and recommended to the Supervisory Board the approval of new and amended internal regulations governing the compliance unit, including its Terms of Reference and Compliance Policy as well as the establishment of the General Compliance Committee responsible for setting common standards for compliance risk management across the Santander Bank

Polska Group, the strategic direction, monitoring of performance against compliance risk management objectives as well as for compliance and anti-money laundering issues.

The issues related to the organisational structure and staffing levels in the compliance unit were closely analysed in terms of the unit's independence.

The Committee analysed the Reputational Risk Management Model, which consists of the "Reputational Risk Management Methodology" and the "Reputational Risk Management Procedure" in Santander Polska and recommended their approval to the Supervisory Board.

The analyses also covered the reports on compliance risk (including the self-assessment), commercialisation of products, regulatory proceedings, anti-money laundering issues, delivery of the KNF's and Internal Audit's recommendations, monitoring of conduct and reputational risk indicators as well as customer complaints ratios.

## Other Matters

In 2018, the Committee also reviewed the reports on:

- status of the implementation of recommendations issued by the Polish Financial Supervision Authority (KNF) and Internal Audit;
- confirmation of compliance of policies, bonus and incentive schemes with the KNF's and EBA's guidelines;
- cases reported by employees via dedicated whistleblowing channels under the Respect and Dignity Policy,
- supervision of compliance with legal requirements on custodian services;
- the Financial Plan Policy, introduced in 2018, which develops the Asset and Liability and Interest Rate Risk Management policies;
- the development of the Bank's insurance business, with particular reference to claims rejection indicators and early termination of policies,
- capital and liquidity position, also in the context of acquisition of organised part of the enterprise of Deutsche Bank Polska S.A.,
- counteracting money laundering, including the impact of amendments to the AML Act in 2018 and its implications for staffing levels in the AML unit as well as the status of implementing the STIR Act;
- BION's rating and steps taken to improve it;
- brokerage activity, including reports on supervision and internal control as well as the report on the KNF's inspection in Dom Maklerski (Brokerage House) carried out in 2017 together with the KNF's recommendations and status of compliance, and the changes to the operation of the business arising from the implementation of MIFID 2;
- staff attrition rates;
- key tax issues from the Bank's perspective.

The Committee also analysed (i) progress in the implementation of Regulation (EU) 2016/679 with regard to the processing of personal data and on the free movement of such data (GDPR); (ii) issues related to the integration of the organised part of the enterprise of Deutsche Bank Polska S.A.; (iii) the implementation of the amended Payment Services Act that refers to the implementation of the PSD2 directive along with the ensuing implications for the Bank; (iv) the governance framework to mitigate cybersecurity risks.

In line with its Terms of Reference, the Committee held closed meetings individually with the Vice President of the Bank's Management Board in charge of the Risk Management Division, Bank Director in charge of the Legal and Compliance Division, the Director of the Internal Audit Area (Chief Audit Executive) and the External Auditor (PwC).

The Committee conducts a continuous review of its process and performance. The form of the review involves a discussion on the format of the meetings and effectiveness of the reporting process.

## Focus for 2019

- Ensuring that the control framework of the acquired organised part of the enterprise of Deutsche Bank Polska S.A meets Santander Bank Polska S.A. standards.
- Regular monitoring of the staffing levels adequacy in the Internal Audit Area in order to ensure the effectiveness of the audit function and high quality of the delivered services with the simultaneous maintenance of its independence.
- Making sure that the control framework for cybersecurity is adjusted to the rapid digitalisation of the Bank's processes and customer interactions.



- Ensuring full compliance of the internal control system with the law and the KNF's Recommendation H.

## 4.4. RISK COMMITTEE

### Role and Tasks

The Risk Committee's role is to assist the Supervisory Board in discharging its responsibilities to the shareholders and other stakeholders in relation to: (i) appropriate risk management philosophy, as articulated in relevant legal regulations and regulatory recommendations and market standards; (ii) risk appetite, as reflected in policies and risk limits; (iii) a sharpened and focused oversight on the more significant business risks undertaken by the Bank; and (iv) the appropriateness of the overall risk governance framework.

The primary responsibilities of the Committee are:

- issuing opinions on the current and future readiness of the Bank to take up risk;
- issuing opinions on the risk management strategy developed by the Bank's Management Board and the information tabled by the Management Board on its execution;
- supporting the Supervisory Board in overseeing the implementation of the risk management strategy in the Bank's operations by the senior management;
- verifying if the prices of assets and liabilities offered to customers fully reflect the Bank's business model and risk strategy; otherwise, the Committee presents to the Management Board proposals to ensure that the price of assets and liabilities is adequate to relevant risk types.

The Committee's tasks are reflected in the adopted annual work plan, in line with which the Committee discharges its responsibilities.

### Terms of Reference

The Committee acts pursuant to the Terms of Reference introduced by force of the Supervisory Board's resolution no. 14/2017 of 16 February 2017. In 2018, the ToR were not amended.

### Committee composition

In 2018, the Risk Committee worked in the following composition:

- Jerzy Surma (Chairman),
- José Manuel Campa,
- David Hexter,
- John Power.

In 2018, there were no changes in the Committee's composition.

### Number of meetings and attendance

The Committee met 5 times in 2018.

In 2018, the attendance rate was as follows:

- Jerzy Surma 5/5
- Jose Manuel Campa 4/5
- David Hexter 5/5
- John Power 5/5

Apart from the Committee's members, the regular attendees are also representatives of the Bank's Auditor, the Vice President of the Bank's Management Board in charge of the Risk Management Division, the Management Board member in charge of the

Accounting and Financial Control Division, the Management Board member in charge of the Financial Management Division and the Director of the Internal Audit Area (Chief Audit Executive). Other members of the Management Board and the Bank's executives are also invited to attend as appropriate in order to present reports and discuss issues related to the areas under their management.

## The Committee's activity in 2018

Discharging their responsibilities, the Committee members take into account that the Bank is in the risk-taking business, whilst the risk level has to be adequate to the scale and type of business undertaken as well as governed by the industry standards, regulatory guidance and recommendations, referring to operational risk, credit risk, market risk and liquidity risk.

The key areas of the Committee's work in 2018 were:

- review and evaluation of Santander Bank Polska Group's Risk Appetite Statement and recommendations for the Supervisory Board with regard to approving the risk appetite,
- verification of the current risk profile of Santander Bank Polska S.A Group based on Risk Dashboards and monitoring the consumption of internal limits bearing in mind the current business strategy and the macroeconomic environment,
- comprehensive assessment of the credit portfolio and credit policies,
- review and recommendations for the Supervisory Board with regard to approving the Internal Capital Adequacy Assessment Report (ICAAP Report) for Santander Bank Polska Group (ICAAP Report),
- review of the operational risk management, including the management of business continuity, information security, outsourcing and insourcing risk and fraud prevention in all areas of the Bank's business,
- review of the risk management and internal control in subsidiaries (Santander-AVIVA, Santander TFI, Santander Consumer Bank and Santander Factoring) and the Bank's different areas of operations (Central Operations Area, Treasury, Business and Corporate Banking Division, Branch Banking – branch network and partner outlets),
- treasury risk management – compliance with the KNF's Recommendation P,
- review of and recommendation for the Supervisory Board with regard to Internal Liquidity Adequacy Assessment Report (ILAAP) as well as models and processes for assets and liabilities management,
- assessment of prices for assets and liabilities offered to customers,
- recommendations for the Supervisory Board with regard to approval of the strategy and policies referring to risks embedded in the Bank's business.

The issues subject to an in-depth review by the Committee in 2018 included also: (i) managing security of ICT environment, incl. the review of challenges arising from growing cyber threats, also as part of Cybersecurity Strategy's review; (ii) managing risk and control functions in the context of the business model transformation, incl. digital transformation and implementation of Agile methodology; (iii) acquisition of the organised part of enterprise of Deutsche Bank Polska S.A.

Reviews of the key risks embedded in the Bank's business covered also the mode of identifying threats and the process of defining and monitoring remedial actions, including those taken up as the follow up of the KNF inspections and Internal Audit reviews as well as the timeliness of their delivery.

One of the Committee's tasks is the oversight of the stress testing undertaken by the Bank in line with its own assumptions and benchmarked against the requirements set by the KNF. These tests are one of the elements of the credit risk management process and are used to evaluate (i) potential impact of specific events on the markets, movements in financial and macroeconomic ratios as well as changes in the risk profile on the condition of the Bank and BZ WBK S.A. Group; (ii) changes of quality of credit portfolios should adverse events materialise. The results of the stress testing are linked closely with the review of the Group's Risk Appetite Statement and provide management information on the adequacy of the set limits and allocated internal capital.

On a regular basis the Committee receives reports on Santander Bank Polska Group's risk profile. In particular, the reports refer to (i) performance against the defined risk appetite and exceptions in this respect, (ii) risk trends, (iii) risk concentrations; (iv) key performance indicators.

## Focus for 2019

In 2019, the Committee will review amendments to the Santander Bank Polska Group's Risk Appetite Statement and continue its comprehensive review of the emerging risks in both the core business of the Group and the overall banking industry. The Committee will continue to pay special attention to management of risk related to IT processes, including the cybersecurity issues.

It will focus on top risks: conduct regulations, political risk, fx mortgage, capital requirements, concentration risk, credit risk, operational risk including cyberattacks, as well as on fraud detection in electronic banking, risk management in multichannel banking, PSD II strategy and threats analysis, Business Continuity Management and Credit portfolio risk analysis.

## 5. SELF-ASSESSMENT OF THE SUPERVISORY BOARD ACTIVITY IN 2018

The Supervisory Board assessed its activities in 2018 in accordance with point II.Z.10.2 of *2016 Code of Best Practice for WSE Listed Companies*.

The Supervisory Board stated that it had duly discharged its responsibilities laid down in the Commercial Companies Code, the Banking Law, the Bank's Statutes and the KNF recommendations as it held its meetings at a frequency that ensured that all matters within the Supervisory Board's remit were duly addressed. In their actions, the Supervisory Board members were guided by the interest of the Bank and the independence of judgements and opinions. Both the composition of the Supervisory Board and knowledge and experience of its individual members, their active participation in the meetings of the Supervisory Board and its committees ensured sound and effective performance of the Supervisory Board as well as proper and effective supervision over the Bank's operations in 2018.

## II. REPORT OF THE SUPERVISORY BOARD ON THE EXAMINATION OF 2018 FINANCIAL STATEMENTS, THE MANAGEMENT BOARD REPORT ON PERFORMANCE IN 2018 AND THE BANK'S MANAGEMENT BOARD'S MOTION WITH REGARD TO THE DISTRIBUTION OF PROFIT FOR 2018 AND UNDISTRIBUTED PROFIT FOR 2016 AND 2017

### 1. EXAMINATION OF 2018 FINANCIAL STATEMENTS, THE MANAGEMENT BOARD REPORT ON PERFORMANCE IN 2018

Pursuant to Article 382 (3) of the Commercial Companies Code and paragraph 32 (1) (6) of the Bank's Statutes, the Supervisory Board examined the Bank's Financial Statements and Group's Consolidated Statements for 2018 as well as the Report on the Group's Performance in 2018, incorporating the Bank's Management Board report on the Bank Performance in 2018 as regards their consistency with the books, documents and the actual status. These documents will be submitted by the Bank's Management Board to the Bank's Annual General Meeting of Shareholders convened for 16 May 2019.

By force of Resolution no. 31/2017 of 19 April 2017, the Supervisory Board vested PricewaterhouseCoopers Sp. z ograniczoną odpowiedzialnością Audyt sp. k. (PwC, statutory auditor) with the examination of the foregoing Statements.

Having thoroughly reviewed the Financial Statements of Santander Bank Polska S.A. for 2018 and the Consolidated Financial Statements of Santander Bank Polska Group for 2018, and having read the auditor's opinion and report, the Supervisory Board positively assessed the financial statements in terms of their conformity with the books of account, documents and factual circumstances.

Furthermore, the Supervisory Board stated that the financial statements had been prepared within the regulatory time frame and in accordance with the International Financial Reporting Standards as adopted by the European Union. The accuracy of the financial statements does not raise any reservations and is confirmed by an auditor's unqualified opinion in terms of their conformity with the books of account, documents and factual circumstances.

Pursuant to the opinion of an independent statutory auditor, both standalone and consolidated financial statements of Santander Bank Polska S.A. give a true and fair view of the assets and financial position of the Bank and the Group as at 31 December 2018 as well as the standalone and consolidated financial performance and cash flows for the accounting year of 2018. They comply in terms of form and substance with the applicable laws and the Bank's Statutes.

Having thoroughly reviewed the Management Board Report on Santander Bank Polska Group Performance in 2018 (including the Management Board Report on Santander Bank Polska S.A. Performance), the Supervisory Board positively assessed the report in terms of its conformity with the books of account, documents and factual circumstances. The report gives an accurate view of the development and achievements as well as assets, financial position and financial performance of the Bank and Santander Bank Polska Group.

Furthermore, the Supervisory Board stated that the report had been prepared in accordance with the Accounting Act of 29 September 1994 and the Finance Minister's Regulation of 29 March 2018 on current and financial reports published by the issuers of securities and the rules of equal treatment of the information required by the laws of a non-member state.

Pursuant to the opinion issued by an independent statutory auditor, the Management Board Report is consistent with the information presented in the Bank's and the Group's financial statements and does not contain any material misstatements. The

Statement on Corporate Governance in 2018 included in the report contains all the required elements, while the Statement on Non-Financial Information is an independent section of the Management Board report.

PwC opinions referred to above are consistent with the external auditor's additional report for the Audit and Compliance Committee.

When making the above assessment, the Supervisory Board also took into account the Audit and Compliance Committee's recommendation presented at the Supervisory Board meeting held on 22 February 2019.

Given the above, by force of Resolution no. 16/2019 of 22 February 2019, the Supervisory Board decided to submit the following documents for the Annual General Meeting's approval:

- Financial Statements of Santander Bank Polska S.A. for 2018,
- Consolidated Financial Statements of Santander Bank Polska Group for 2018,
- the Management Board Report on Santander Bank Polska Group Performance in 2018 (containing the Management Board report on Santander Bank Polska S.A. operations).

## 2. REVIEW OF THE BANK'S MANAGEMENT BOARD MOTION WITH REGARD TO DISTRIBUTION OF PROFIT FOR 2018 AND UNDISTRIBUTED PROFIT FOR 2016 AND 2017

On 5 March 2019, the Supervisory Board assessed the Bank's Management Board recommendation on allocating to dividend:

- 25% of the profit earned in 2018, i.e.: PLN 541,068,016.50,
- PLN 957,588,300.90 from the undistributed profit for 2017,
- PLN 514,026,364.32 from the undistributed profit for 2016.

Taking account of the above and the resolution of the Annual General Meeting of Shareholders no. 43 of 17 May 2017 stipulating that the dividend paid out of profit earned in 2016 should not include the series M shares, the proposed dividend:

- 1) per share of the series: A, B, C, D, E, F, G, H, I, J, K, L and N will be PLN 19.72,
- 2) per share of the series M, it will be PLN 14.68.

Bearing in mind the individual recommendations made by the Polish Financial Supervision Authority addressed to the Bank in the letter of 25 February 2019 as well as a sound capital position of the Bank and the Group, the Supervisory Board approved the above stance of the Management Board.

In its assessment, the Supervisory Board relied also on the following capital ratios reflecting a sound capital position of the Bank and Santander Bank Polska Group as at 31 December 2018:

- the Bank's Tier I ratio of 15.85%,
- the Bank's TCR of 18.04%,
- the Group's Tier I ratio of 14.11%,
- the Group's TCR of 15.98%,

as well as the fact that capital ratios on the standalone and consolidated basis are above the minima required under the KNF's capital decisions and recommendations.

The Supervisory Board also took account of the level and risk of excessive leverage defined in Regulation no. 575/2013. As at 31 December 2018, the financial leverage was 9.53% and 9.50% on the standalone and consolidated basis, respectively. The leverage ratio is much above the regulatory requirement and dividend eligibility level of 5%.

The Supervisory Board accepted the Management Board recommendation to allocate 50% of net profit (PLN 1,083,580,684.24) to reserve capital and to allocate 25% of net profit (PLN 542,512,667.73) to retained earnings, taking into consideration the Polish Financial Supervision Authority's recommendation to retain 75% of net profits earned between 1 January 2018 and 31 December 2018.

The Supervisory Board accepted also the Management Board recommendation to: i) allocate retained earnings resulting from recognition on financial assets in accordance with IFRS 9 in the accounting year commenced on 01.01.2018 and ended on 31.12.2018 in the amount of PLN 17,808,764.53 to the reserve capital, ii) allocate PLN 489,834.64 of the undivided net profit generated by the Bank in 2017 to the reserve capital, iii) allocate PLN 740,611.77 of the undivided profit generated by the Bank in 2016 to the reserve capital.



The Supervisory Board took into consideration the Bank's dividend policy and the KNF's permission dated 28 September 2018 to allocate 50% of net profits earned in H1 2018 to common equity Tier I capital.

In Supervisory Board's opinion, higher own funds are intended to build the Bank's strong capital position ensuring its stable and secure growth. In its capital policy, the Management Board takes into consideration the Bank's classification as an Other Systematically Important Institution on the local market and the resulting Bank's impact on the local banking market's security and development.

In addition, the Supervisory Board took into account that: (i) the level of the retained profit is sufficient to deliver the strategy adopted by the Bank/Group and ensures adequate balance between the capital consumption and growth; (ii) the existing capital base reflects the prudent approach and acceptable level of risk associated with the Bank's current and future operations and ensures safety of customer deposits.

## III. ASSESSMENT OF SANTANDER BANK POLSKA GROUP'S PERFORMANCE IN 2018

Acting in compliance with 2016 Code of Best Practice for WSE Listed Companies, the Supervisory Board assessed the Bank's and Santander Bank Polska Group's standing in 2018, covering the internal control system, risk management, compliance risk management, internal audit function, including financial reporting and operational business as well as the assessment of the reasonableness of the Bank's sponsoring and corporate giving policy and the assessment of the manner of discharging disclosure requirements by the Bank with regard to the application of the corporate governance rules.

### 1. SANTANDER BANK POLSKA GROUP PERFORMANCE IN 2018

#### Economic growth

In 2018, the Polish economy expanded by 5.1% YoY, with business sentiment indicators pointing to an approaching slowdown. Global economy developed at a similar pace as in 2017, but the forecasts for future periods worsened, *inter alia* due to the rising protectionism in international trade. The eurozone rose slightly slower, which negatively affected the demand for Polish exports.

The main 2018 growth factor in Poland was private consumption, supported by the strong labour market, high growth of disposable income and consumer optimism. Investments rebounded, rising by 7.3% YoY in 2018, but increased investment activity was seen mainly in the public sector, especially in local governments, while private investments remained stagnant. The main challenge facing Polish companies in 2018 was difficulties in finding skilled workforce, which translated into a strong surge in salaries. Despite the above, industrial output rose by approx. 6% YoY and construction output by approx. 20% YoY. The current account balance worsened slightly (-0.7% of GDP vs +0.1% in 2017), mostly due to a negative trade balance. At the same time, a decline of gross external debt was recorded, while the net international investment position improved relative to the GDP. The solid economic results encouraged S&P to upgrade the Poland's rating from BBB+ to A-.

#### Inflation

Inflation proved weaker than expected in 2018. It dropped significantly in Q1 to 1.3% YoY, soon after recording 2.5% in November 2017. In the middle of the year, CPI growth rebounded to 2% YoY, but then again it started to decrease faster than expected. Food and energy prices were responsible for most of the changes, while core inflation, excluding the above items, remained at the level of 0.5-1.0% observed also in 2017. Its readings did not signal an upward trend despite the labour market pressure and rising costs for businesses.

#### Monetary policy

In 2018, the rhetoric of the Polish Monetary Policy Council remained "dovish" and the NBP governor suggested that the main reference rate might stay at a record low 1.50% beyond 2019. The MPC's stance remained unchanged even after publication of NBP's forecasts in November, which showed inflation above 3% in 2019 and still above the target in 2020. Thus, the motion to raise rates, which was voted in November, does not mean that the expected timing of tightening is drawing closer.

#### Deposit and credit market

In 2018, deposit growth accelerated from 4.5% YoY in January to almost 9% YoY at the year-end. This happened thanks to higher growth rate of household deposits, which jumped from 3.5% YoY at the start of the year to almost 9% YoY in December. Corporate deposits accelerated to 6-7% YoY in Q3 2018, but the remaining part of the year witnessed a growth at 4%. Total loan growth accelerated from approx. 4% YoY to almost 8% YoY, with more visible acceleration in household loans (from approx. 2% YoY to approx. 7.5% YoY), while corporate loan growth stayed fairly stable at approx. 6-7% YoY. PLN-denominated housing loans maintained a robust growth of 10-12% YoY recorded also in the previous two years. Consumer loans accelerated from 7.5% YoY in 2017 to 9.5% YoY in H2 2018 (FX adjusted). Corporate investment loans slowed down from above 10% at the start of the year to a

slight decline in H2 2018 (FX adjusted). Current loans of companies accelerated from approx. 7% YoY in January to over 13% YoY in December.

## Acquisition of a demerged business of Deutsche Bank Polska S.A.

On 9 November 2018, following the registration of an increase in its share capital, Santander Bank Polska S.A. assumed all rights and obligations of a demerged part of Deutsche Bank Polska S.A., including retail banking, private banking, business (SME) banking and DB Securities S.A. (currently Santander Securities S.A.). The transaction did not cover investment and corporate banking, global transactional banking as well as foreign currency mortgage-backed credit facilities, which continue to be serviced by Deutsche Bank Polska S.A.

## Income statement

In 2018, Santander Bank Polska Group posted a profit before tax of PLN 3,426.2m, up 2.7% YoY. Profit attributable to the shareholders of Santander Bank Polska S.A. increased by 6.9% YoY to PLN 2,365.2m.

## Income

Total income of Santander Bank Polska Group for 2018 increased by 11.9% YoY to PLN 8,683.9m. Adjusting for a gain of PLN 387.7m from the acquisition of an organised part of Deutsche Bank Polska S.A., the underlying total income grew by 6.9% YoY on account of an increase in the Group's income from the core business.

Net interest income for 2018 amounted to PLN 5,742.4m and increased by 8.8% YoY, impacted by a sound balance sheet structure and flexible pricing management amid fast growth of net earning assets, their funding deposits and other instruments.

The quarterly net interest margin (annualised on a quarterly basis) gradually declined starting from Q2 2018 to 3.52% in Q4 2018 (-0.41 p.p. YoY). The underlying cause was the growing costs of asset funding in connection with the accelerated acquisition of deposits as well as enhanced activity in the area of own securities issue as part of preparations for the acquisition of a demerged business of Deutsche Bank Polska S.A. Increasing credit volumes (cash loans, mortgage loans and business loans) and investment portfolios of debt securities fuelled the growth of interest income, which was nevertheless outpaced by a YoY increase in interest expenses.

Net fee and commission income for 2018 amounted to PLN 2,057.8m and increased by 2.2% YoY driven by the performance of business lines of the Bank and its subsidiaries. The net fee and commission income from the lending business grew by 19.1% YoY on account of dynamic sales of loans and management of the schedule of fees and charges. An increase was also observed in agency costs connected with the operating model acquired along with a demerged part of Deutsche Bank Polska S.A.

FX fee income rose by 14.4% YoY due to exchange rates and measures taken by the Group to support foreign trade and develop e-FX services in iBiznes24.

Income from distribution and asset management was broadly flat (+0.8% YoY) thanks to high value of average annual net assets under management.

Net fee and commission income aggregated under the "eBusiness and payments" line item rose by 3.7% YoY as a result of an increase in income from issuance and management of debit cards driven by the growth of this instrument base (+9.9 YoY) and non-cash transactions.

Brokerage fees went down by 23.4% YoY along with a decline in trading in the secondary market amid deteriorating investor sentiment observed since February 2018.

Net trading income reported by Santander Bank Polska Group for 2018 was PLN 144.5m, down 25.9% YoY.

In 2018, the Group disclosed dividend income of PLN 100.1m, i.e. up PLN 30.3% YoY on account of higher dividends from Aviva Group companies from the portfolio of equity investments of Santander Bank Polska S.A.

Gains on other financial instruments and subordinate entities decreased by 26.8% YoY to PLN 37.5m due to the lack of significant transactions in equity instruments in 2018. Lower trading in the capital market was partly offset by higher gains on the sale of bonds (PLN 28.3m in 2018 vs. PLN 20.8m in 2017) and PLN 12.6m on account of changes in the fair value measurement arising from reclassification of Visa Inc.'s shares.

Other operating income totalled PLN 213.9m and increased by 42.0% YoY, mainly on account of the profit of PLN 44.3m from the sale of the bank's real estate and higher income from the sale of services.

## Expenses

In 2018, total costs were significantly impacted by delivery of the Group's strategic projects, in particular rebranding and acquisition and integration of a demerged part of Deutsche Bank Polska S.A.

The cost of rebranding amounted to PLN 66.4m, whereas the impact of the acquisition and integration of an organised part of Deutsche Bank Polska S.A. was PLN 108.9m

The total costs of Santander Bank Polska Group for 2018 amounted to PLN 3,769.0m, and were 11.8% higher YoY, which was attributed to all key cost items. The cost base was mostly affected by strategic development and transformation projects (including the above-mentioned projects and IT projects) as well as competitive and regulatory pressure and provisions for legal claims.

Excluding the two flagship projects, i.e. rebranding (PLN 66.4m) and acquisition of a demerged part of Deutsche Bank Polska S.A. (PLN 108.9m), the underlying total costs of the Group were up 7.0% YoY, largely impacted by a 110.5% YoY increase in provisions for legal disputes and other assets recognised in other operating costs. Adjusting for the above-mentioned provisions, the cost base grew by 5.1% YoY mainly on account of staff and general expenses.

The underlying staff and general expenses were up 4.9% YoY primarily due to salary review, introduction of new bonus schemes for employees, implementation of IT projects supporting the digital transformation and strategic and operating programmes.

The Group's cost to income ratio was stable YoY, both on comparable and non-comparable basis (43.3% and 43.4%, respectively).

## Assets

As at 31 December 2018, the total assets of Santander Bank Polska Group were PLN 205,852.9m, up 34.8% YoY. The value and structure of the Group's financial position was determined by the parent entity, which held 88.9% of the consolidated total assets vs. 87.0% as at the end of December 2017.

## Credit portfolio

As at 31 December 2018, consolidated gross loans and advances to customers were PLN 141,844.7m and increased by 25.9% vs. 31 December 2017.

Loans and advances to individuals went up by 29.2% to PLN 74,696.4m. Home loans, the largest constituent item, increased by 32.0% YoY to PLN 49,211.0m, with the portfolio of Santander Bank Polska S.A. growing by 36.2% and the portfolio of SCB S.A. decreasing by 5.0%. The second significant constituent item, i.e. cash loans, went up by 37.2% YoY to PLN 17,910.9m.

Loans and advances to enterprises and public sector entities were PLN 58,929.5m, 22.8% higher YoY, mainly driven by lending to retail, SME and corporate customers.

## Equity and liabilities

The total equity of Santander Bank Polska Group increased by 14.2% as the Bank's profit generated in the current period and the whole profit for 2017 were retained in accordance with guidelines issued by the regulator. The equity value was reduced by a dividend payout of PLN 307.6m from the retained profit for 2016.

As part of the acquisition of an organised part of Deutsche Bank Polska S.A., the share capital was increased by the share issue of PLN 27.5m and the value of sale of shares of PLN 1bn at premium. The retained profit and the revaluation reserve reflect the differences in the carrying amounts of financial assets and liabilities as at 1 January 2018 arising from adoption of IFRS 9, in the total amount of PLN -254.5m.

As regards liabilities, an upward trend was observed in the case of subordinated liabilities and debt securities in issue (+62.7% YoY). This item grew as a result of the Group's increased activity in relation to the issue of own securities. In 2018, Santander Bank Polska S.A. issued three series of certificates of deposit with a total nominal value of PLN 1,150m as part of its issue programme, subordinated series F bonds with a nominal value of PLN 1bn and eurobonds with a nominal value of PLN 2,145.6m (the equivalent of EUR 500m) as part of the EMTN programme. Santander Factoring Sp. z o.o. and SCB S.A. issued bonds with a nominal value of PLN 1,700.0m and PLN 451m, respectively. Furthermore, Santander Leasing Poland Securitization 01 issued senior bonds of EUR 230m as part of securitisation of receivables arising from lease and loan agreements.

In the same period, Santander Bank Polska S.A., Santander Factoring Sp. z o.o. and SCB S.A. redeemed matured own securities for a total amount of PLN 1,235m, PLN 1,550m and PLN 190m, respectively.

Pursuant to the KNF's decision, subordinated series F bonds with a nominal value of PLN 1bn, maturing on 5 April 2028, were taken from debt securities in issue to subordinated liabilities.

## Deposits

In 2018, consolidated deposits from customers increased by 34.2% YoY to PLN 149,616.7m at the end of December 2018.

The Group's total term deposits from customers amounted to PLN 58,695.8m and increased by 41.5% vs. 31 December 2017. Current account balances rose by 29.8% to PLN 85,201.2m, and other liabilities were PLN 5,719.6m, up 32.0%.

The retail deposit base stood at PLN 88,211.4m, higher by 35.7% YoY as a result of a fast increase in term deposit balances (+49.3%) and current account balances (+28.8%).

Deposits from enterprises and the public sector grew by 32.1% to PLN 61,405.3m as a result of an increase of 32.7% YoY in term deposits to PLN 25,980.7m and 31.6% YoY in current account balances to PLN 29,892.2m.

## Share price of Santander Bank Polska S.A.

The share price of Santander Bank Polska S.A. was affected by negative trends on the WSE observed in 2018. Aside from global trends, share prices of companies from the banking sector, including Santander Bank Polska S.A., were influenced by the announcements of the Monetary Policy Council suggesting no intention to increase interest rates even until the end of 2020.

Like the entire stock market, the Bank's shares came under the demand pressure for the greater part of the year. Similarly to the main stock indexes (WIG and WIG20), in H2 2018 the Bank's share price improved after the weak first half of the year, with the YoY decrease reduced to 9.6% (from PLN 396.25 as at the end of December 2017 to PLN 358.20 as at the end of December 2018). It is still better performance than that of WIG-Banks, the industry index, which lost 12.5% in the same period, pointing to a significant decrease in market capitalisation of other sector companies and its relative weaknesses versus the main WSE indexes.

During the year, the share price of Santander Bank Polska S.A. ranged from PLN 442.00 on 24 January 2018 to PLN 327.60 on 19 June 2018.

On 14 June 2018, the Bank paid out a dividend of PLN 3.10 per share from undistributed profit for 2016.

As at 31 December 2018, market capitalisation of Santander Bank Polska S.A. amounted to PLN 36,568.0m vs. PLN 39,360.9m a year before.

## Rating

On 30 August 2018, Fitch assigned a rating for the Bank's Euro Medium-Term Note Programme ("EMTN Programme"). An unsecured debt issued as part of the EMTN Programme (Senior Notes) was assigned a rating of BBB+ and short-term debt was assigned a rating of F2. At the same time Fitch assigned planned senior unsecured notes an expected long-term rating of BBB+(EXP).

In its announcement of 12 October 2018, Fitch Ratings affirmed the ratings of Santander Bank Polska S.A. at BBB+ in view of the lack of major changes to the Bank's key financial metrics over the past 12 months.

Ratings of Santander Bank Polska S.A. were updated by Moody's Investors Service on 29 January 2018. The agency changed the outlook on long-term deposit rating of Santander Bank Polska S.A. from stable to positive and affirmed existing ratings. The above change reflected improving asset quality, resilient capitalisation and strong profitability of the Bank. It also factored in positive implications of the acquisition of the demerged business of Deutsche Bank Polska S.A. and estimated costs associated with the legislation regarding foreign currency mortgage portfolio.

On 31 August 2018, Moody's Investors Service assigned a provisional rating for the Bank's Euro Medium-Term Note Programme ("EMTN Programme"). The EMTN Programme was assigned a (P)Baa1 provisional rating for local and foreign-currency debt, while senior unsecured foreign-currency notes to be issued as part of the programme were assigned a long-term Baa1 rating with a positive outlook.

On 27 December 2018, Moody's affirmed the ratings of Santander Bank Polska S.A. including the Bank's standalone baseline credit assessment (BCA) of baa3, which reflects favourable economic conditions in Poland, gradually improving asset quality, good liquidity buffer, adequate capitalisation supported by retained earnings and strong profitability. The Bank's BCA is constrained by the material, albeit declining, legacy portfolio of FX mortgages, which entails risks from potential legislations and regulations on such exposures.

## 2. ASSESSMENT OF THE INTERNAL CONTROL SYSTEM

The Supervisory Board performed the annual adequacy and effectiveness assessment of the Internal Control System in Santander Bank Polska S.A. for 2018, including annual assessment of the adequacy and effectiveness of the control function, compliance unit and the internal audit unit, taking into account in particular:

- the Audit and Compliance Committee's opinion presented at the Supervisory Board meeting held on 22 February 2019,
- the information obtained from the Bank's Management Board with regard to the manner of delivering tasks referred to in recommendations 1.1 – 1.6, the KNF's Recommendation H,
- periodical reports of the compliance unit and internal audit unit as well as information from subsidiaries, including information reported by Chairpersons of Audit and Compliance Committee, and Risk Committee based on the reviews made by these Committees,



- findings of the chartered auditor, including those presented when debating the report from the audit of the financial statements,
- findings from supervisory activities performed by authorised institutions, including findings and recommendations from the KNF issued after their inspections in the Bank,
- opinion from an external entity – positive assessment of the internal audit unit carried out in November 2018,
- assessment of adequacy and effectiveness of the internal control system and the risk management system presented by the Internal Audit Area.

The Supervisory Board positively assessed the Bank's internal control system (including the control function, compliance unit and internal audit unit) and deemed it adequate and effective, adjusted to the Bank's organisational structure, risk management system as well as to the size and complexity of the Bank's business.

It covers all units across the Bank as well as its subsidiaries deemed material. The internal control system covers all significant controls, including those related to the Bank's financial reporting and operational activity.

As required by the Statutes, the Bank operates an internal control system which supports the decision-making processes and contributes to the Bank's efficient operations, compliance with risk management rules, reliability of financial reporting as well as compliance with the law, international standards, internal regulations and best practice.

The Bank's Management Board is responsible for designing and implementing the effective and adequate internal control system for all organisational units and positions in the Bank, comprising a control function, a compliance unit and the internal audit unit. The Management Board also ensures the system's independence, financial resources and validity of documented procedures in this respect, and sets criteria for assessing the adequacy and effectiveness of the internal control system.

The Management Board ensures that the Internal Control System is in place in subsidiaries. Subsidiaries deemed material have a documented internal control model within which elements such as tasks, function controls are described and managed. These elements are subject to an annual assessment and certification process.

At Santander Bank Polska S.A. there is an internal control system that takes into account solutions operating in Santander Group. The Bank's Management Board ensured conformance of the system with the national legislation and Recommendation H, which is evidenced by a documented analysis certifying such conformance (mapping of the adopted system to respective recommendations contained in Recommendation H).

The Internal Control System comprises:

- a) the control function responsible for ensuring that controls, in particular those related to risk management, are observed; it may include individual positions, groups of employees or organisational units;
- b) the compliance unit responsible for identification, assessment, control and monitoring of the risk of the Bank's potential failure to comply with the legal regulations, internal rules and market standards, and for presentation of reports in that respect;
- c) the independent internal audit function responsible for autonomous and impartial assessment of the adequacy and effectiveness of the Risk Management System and the Internal Control System (except for the internal audit unit).

The control function is an element of the Internal Control System and comprises:

- a) all controls in the Bank's processes which are defined by the organisational units as part of the Operational Risk Self-Assessment;
- b) independent horizontal and vertical monitoring of compliance with these controls (including ongoing verification and testing); controls subject to independent monitoring are covered by the Group Internal Control Model;
- c) reporting as part of the control function.

The Bank's Management Board takes regular actions to keep continuity of the Internal Control System uninterrupted by a duly designed, introduced and ensured adequate and effective internal control system, including proper interaction among all employees of the Bank within the control function and their collaboration with the compliance and the internal audit units, and to provide the units' employees with an access to the required data and source documents, including documents that contain classified information subject to professional secrecy.

If deficiencies are identified by the internal control system, the Bank's Management Board takes adequate actions to eliminate them, including corrective and disciplinary measures.

The Bank's Management Board ensures that the Internal Control System is designed, introduced and operational in Santander Bank Polska Group and that it is adequately adjusted to its organisational structure and Risk Management System as well as to the size and complexity of the Group's business. The system covers all units across the Bank as well as its subsidiaries. In particular, the following is taken into account when ensuring the adequacy and effectiveness of the Internal Control System in Santander Bank Polska Group:

- a) the complexity of the processes in place;
- b) available resources;
- c) the risk of deficiencies occurring in particular processes, including significant processes;
- d) assessment of the adequacy and effectiveness of the first, second and third line of defence.

The Bank's Management Board defined the criteria for assessing the adequacy and effectiveness of the internal control system that were approved by the Supervisory Board.

Having analysed the established criteria:

- a) the performance against the objectives of internal control system,
- b) the performance against the controls which consist in independent monitoring of key control mechanisms defined in the Control Function Matrix,
- c) the performance against the control plans for processes not covered by the Control Function Matrix but covered by the Group Internal Control Model,
- d) timeliness and efficiency of the delivery of remediation and disciplinary actions,

it can be concluded that the internal control system of Santander Bank Polska S.A is adequate and effective. There should be focus on timely implementation of remediation actions defined for deficiencies under the assessment and certification process.

When making the assessment of the control function, the Supervisory Board took also into account the manner in which the Management Board discharged the duties referred in part B the KNF's Recommendation H.

The internal control and risk management systems are based on the three lines of defence.

The first line of defence covers risk management in the Bank's operations and is based on business units which in their BAU generate the risks impacting the achievement of the Bank's objectives. The first line includes activities performed by each employee to ensure the quality and correctness of the completed tasks. The first line of defence checks adherence to the procedures and responds to any identified irregularities. The second line of defence consists in risk management by employees in dedicated roles or organisational units and the operations of the compliance unit. Risk management in the second line of defence is independent from risk management in the first line of defence. The second line of defence is formed by functions which support the Bank's managerial cadre in risk identification and management by providing the relevant tools, internal regulations and mechanisms for managing, monitoring, ongoing verification, testing and reporting risk as well as specialised functions which assess the effectiveness of the first line controls. The second line of defence is also responsible for vertical monitoring, including ongoing vertical verification and vertical testing. The purpose of vertical monitoring is to verify whether the first line of defence applies the required controls.

The third line of defence is the Internal Audit Area, whose activity is supervised by the Audit and Compliance Committee of the Supervisory Board. The Internal Audit Area provides independent and objective examination and assurance on the first and second tier controls and on the Bank's management system, including the effectiveness of managing the risk related to the Bank's business. To that end, the Internal Audit Area verifies whether Santander Bank Polska Group's risks are adequately covered, in compliance with the applicable management policies, procedures and internal and external regulations. Using its own risk matrix and knowledge, the Internal Audit Area performs a regular assessment of the present and future risks across the Bank and Santander Bank Polska Group, developing annual audit plans to cover it. Also, priorities highlighted by the Bank's management, the Audit and Compliance Committee, the external auditor, and banking supervision institutions are taken into account.

The Supervisory Board is responsible for the supervision over the implementation and maintenance of the internal control system. The Supervisory Board performs annual adequacy and effectiveness assessment of the Internal Control System, including annual assessment of the adequacy and effectiveness of the control function, compliance unit and the internal audit unit, taking into account in particular:

- a) opinion of the Audit and Compliance Committee,
- b) the information from the Bank's Management Board on the manner of discharging these duties,
- c) periodical reports of the compliance unit and internal audit unit,
- d) information significant from the point of view of adequacy and effectiveness of the Internal Control System obtained from Santander Group and subsidiaries;
- e) findings of the chartered auditor;
- f) findings of audit and control activities carried out by authorised institutions;
- g) any reviews and opinions significant from the point of view of adequacy and effectiveness of the internal control function carried out by third parties.

The Supervisory Board receives current and accurate information on identified deficiencies and on the measures taken to eliminate them, on the extent of compliance with internal and external regulations and on adequacy and security of the IT systems.

The Supervisory Board monitors the effectiveness of the Internal Control System based on the information obtained from the compliance unit, internal audit unit, the Bank's Management Board and the Audit and Compliance Committee.

The control findings are taken into account and used to improve the existing processes and safety by making relevant changes to internal processes and regulations. These are regularly verified by the Internal Audit Area.

The Audit and Compliance Committee is informed about the results of assessing the risk of failure to comply with the overall objectives of the internal control system. The analysis of the design and effectiveness of controls made in 2018 indicates the low impact of the identified deficiencies relative to the delivery of the internal control targets.

In 2018, the deficiencies identified in the process of the internal control model certification were estimated at the lowest materiality level (Control Deficiency). The number of deficiencies increased from 8 to 23, yet it is still lower than in 2017 due to the analysis of the internal audit's recommendations and their impact on the results of the assessment of the internal control model certification. Nonetheless, this is still a low number of deficiencies relative to the total number of controls (1.1%) which confirms the maturity of the Bank's internal control system and the effectiveness of the controls in place.

The internal control system addresses, among others, compliance with the requirements of the Sarbanes-Oxley Act, Volcker Rule (section 619 of the Dodd-Frank Wall Street Reform and Consumer Protection Act) as well as requirements of RDA/RRF (Basel Committee on Banking Supervision 239: Principles for effective risk data aggregation and risk reporting).

In order to manage risk associated with the preparation of financial statements, the Bank tracks legal and regulatory changes related to reporting obligations for banks and updates its accounting rules and disclosures accordingly. The Bank, through its representatives sitting on supervisory boards of individual subsidiaries, exercises oversight of its consolidated subsidiaries. Financial statements are approved by the Disclosure Committee, which is responsible for ensuring that the financial disclosures of Santander Bank Polska Group comply with all legal and regulatory requirements before they are released. Annual reports on operations of the Disclosure Committee are subject to a review by the Audit and Compliance Committee.

The Audit and Compliance Committee reviews Financial Statements, Management Board Report on the Group's Performance and additional reports (such as Information on Capital Adequacy of the Group) prepared as part of financial reporting on a half-yearly and yearly basis, and submits them to the Supervisory Board for acceptance/ approval. As part of its reviews, the Audit and Compliance Committee gets acquainted with the outcome of external auditor's work (review or audit of financial statements, respectively), in particular with key risks within the scope the auditor's analysis and conclusions arising from auditing activities.

In the Supervisory Board's opinion, which is consistent with that of the Management Board, the controls implemented in the Bank effectively address the risk of a material misstatement in the financial statements. Moreover, the effectiveness of controls in financial reporting is additionally assessed by an independent external auditor as part of the annual certification process for compliance with the Sarbanes-Oxley Act.

Detailed information on the assessment made by the Supervisory Board with regard to compliance (including the adequacy and effectiveness of the compliance unit and the compliance risk management system) as well as with regard to the adequacy and effectiveness of the internal audit unit and the risk management system is presented below in points 3 – 5.

### 3. ASSESSMENT OF COMPLIANCE

The applicable compliance risk management system covers the units listed below together with their scope of responsibilities:

- Compliance unit – compliance with legal and regulatory requirements in individual areas of the business activity, in particular with regard to: protection of consumer rights, implementation and sale of new products, prevention of money laundering, ethical issues, protection of confidential information and management of conflicts of interest.
- Specialist units dedicated to identifying and interpreting other legal and regulatory requirements that the Bank is obliged to fulfil as a legal entity (labour regulations, tax and reporting, prudential standards).
- Specialist committees that are supervised by the Risk Management Committee.

The Santander Bank Polska Compliance Policy adopted by the Management Board and approved by the Supervisory Board provides the compliance unit with a mandate to effectively support the process of managing compliance risk that includes the following risk categories: regulatory risk, conduct risk, money laundering and terrorism financing risk and reputational risk.

In February 2019, the Supervisory Board conducted the overall review and assessment of the compliance unit for 2018.

The Supervisory Board stated that:

- The compliance unit is a function independent from any other function and unit whose activities support the Management Board, Supervisory Board and other members of senior management with regard to the discharge of regulatory obligations and approval of internal control principles and compliance policy framework.
- The independence of the compliance unit is confirmed to the Management Board and to Audit and Compliance Committee on an annual basis and is ensured in particular by the following:

- the compliance unit's direct reporting line to Bank Director in charge of the Legal and Compliance Division who was empowered by the Management Board President to supervise the compliance risk and who was not vested with powers referred to in Article 22a(4) and (6)(2) of the Banking Law;
  - a direct and unlimited access of the compliance unit's head to the Chairman of the Audit and Compliance Committee and his participation in all meetings of that committee and the Risk Committee; holding, at least once a year, a meeting with the Audit and Compliance Committee by the compliance unit's head in absence of the Management Board members;
  - participation of the unit's head in meetings of the Management Board and his membership in the Risk Control Committee and Risk Management Committee (without the voting rights in both bodies) which provides him with a full insight into the operations of those governing bodies and opportunity to express his opinion;
  - a detailed procedure of appointing and removing the unit's head in place;
  - unlimited access of the compliance unit to all information, documents, systems, applications and physical locations necessary to properly perform its tasks;
  - reports presented directly by the compliance unit to the Management Board, Audit and Compliance Committee/Supervisory Board; the reports are delivered periodically to all these bodies.
- The compliance risk management is adequate and effective given the scale of the Bank's business. The compliance unit has resources sufficient to carry out responsibilities set out in the Compliance Programme both in terms of the number of employees (taking into account that the optimisation and automation of compliance processes is needed) and the adequacy of skills.
  - The compliance unit's regulations are adequate, taking into account the commonly applicable law, the Bank's internal regulations and supervisory recommendations.

The unit's regulations were updated, including the Compliance Charter, to adapt them to requirements arising from the KNF's Recommendation H. Minor enhancements are yet to be implemented as result of the Internal Audit review.

- As a part of mandatory, independent testing, the compliance unit carried out controls in line with the annual testing plan which is a part of the Compliance Programme:
  - the annual testing plan is based in particular on the risk assessment and legal requirements;
  - in the opinion of the Bank's Management Board, the compliance unit testing plan for 2018 covered all necessary issues and ensured an independent and objective manner of reviewing and assessing controls applied as part of the first and second line of defence in terms of compliance risk;
  - as a result of its testing activity, the compliance unit did not identify any significant and critical risks; all other identified risks were addressed to controlled units and action plans were prepared to mitigate those risks.
- The compliance unit is periodically audited by the Internal Audit Area.

This assessment took also into account that each quarter, as part of the compliance risk management process, the Audit and Compliance Committee reviews key compliance issues identified by the compliance unit as well as those arising from the unit's business as usual. Information in this respect as well as the Committee's opinions and recommendations are presented to the Supervisory Board as part of the Committee's report.

## 4. ASSESSMENT OF THE INTERNAL AUDIT FUNCTION

The Supervisory Board assesses the adequacy and effectiveness of the internal audit function upon each presentation of the report on the performance of the Internal Audit Area (IAA) to the Audit and Compliance Committee.

At its meeting in February 2019, the Supervisory Board conducted the overall review and assessment of the Internal Audit function.

Given the above, the Supervisory Board stated that:

- The Internal Audit function is adequate and effective.
  - The existing IAA regulations are adequate, comply with the commonly applicable law, the Bank's internal regulations, supervisory recommendations and market standards adopted in the Bank. The IAA operates in line with the "International Standards for the Professional Practice of Internal Auditing" issued by the Institute of Internal Auditors which was confirmed by an independent external assessment.
  - The IAA regulations, including the Internal Audit Charter, were updated to adapt them to requirements arising from the KNF's Recommendation H.

- The internal audit methodology reflects the current professional standards and enables identification of significant risks in Santander Bank Polska Group.
- The annual audit planning is based on a comprehensive risk assessment process and clearly identifies audit objectives and scope of work. In line with the adopted internal audit methodology both the requirements of the Bank's senior governing bodies (Supervisory Board, Management Board) and of the Regulator were covered in the Audit Plan. Moreover, as part of the annual risk assessment process, a strategic and operational audit plan was developed.
- In the opinion of the Bank's Management Board and the Audit & Compliance Committee, the Audit Plan for 2018 covered all significant issues and ensured an independent and objective manner of reviewing and assessing controls applied as part of the first and second line of defence and the Bank's management system, including the effectiveness of managing risk related to the Bank's operations. Moreover, audit findings are used to improve the existing processes and operational security.
- There are adequate policies and practices to monitor the quality of internal audit work that are compatible with professional standards and the approved methodology. The quality assurance report is presented to the Supervisory Board, Bank's Management Board and the Audit and Compliance Committee on an annual basis.
- In November 2018, an independent assessment of the internal audit function was performed by independent consulting company with good results confirming compliance with Polish regulations and international standards.
- Audit findings indicating deficiencies in internal control and risk management system identified in conducted audits are presented in audit reports and represent the basis for issuing a recommendation for the audited unit aimed at eliminating the identified irregularities.

Actions taken by audited units in response to audit findings and delivery of issued recommendations are each time verified by the IAA. The status of recommendations' implementation is monitored and reported to the Bank's Management Board and the Audit and Compliance Committee on a regular basis.

The audit findings are presented to the Audit and Compliance Committee, Management Board and Supervisory Board on a periodical basis.

The IAA presentation to the Supervisory Board (on 22 February 2019) included the assessment of the internal audit function in terms of adequacy and effectiveness of the internal control and risk management system as part of the summary of the IAA's activity in 2018. This information was also presented to the Audit and Compliance Committee and to the Management Board.

- The IAA is a function independent of any other functions and units whose activity is to provide assurance to the Management Board, Supervisory Board and other members of senior management with regard to the quality and effectiveness of internal control, management of risks (current or new), processes and systems helping thus to protect the company's goodwill, solvency and reputation.

The independence of the IAA is confirmed to the Management Board and to the Audit and Compliance Committee on an annual basis and is ensured in particular by the following:

- In line with the Bank's Statutes, the IAA reports directly to the President of the Management Board. Audit and Compliance Committee supervises the activity of the internal audit function.
  - The Head of the Internal Audit Area has a direct and unlimited access to the Chairman of the Audit and Compliance Committee and participates in all meetings on this Committee as well as the Risk Committee. At least once a year, a meeting with the Audit and Compliance Committee is held in absence of the Management Board members.
  - The IAA Head participates in meetings of the Management Board and is a member of the Risk Control Committee and Risk Management Committee (without the voting rights in both committees) which provides him with a full insight into the operations of those governing bodies and opportunity to express his opinion.
  - A detailed procedure of appointing and removing the IAA Head has been developed.
  - The IAA has unlimited access to all information, documents, systems, applications and physical locations necessary to complete assigned tasks.
- The Internal Audit Area has sufficient resources to carry out its responsibilities:
    - set out in the Audit Plans, both in terms of the number of auditors and the adequacy of their skills; the Chief Audit Executive prepares periodically (at least once a year) a skill gap analysis to ensure adequate human resources;
    - the auditors' qualifications are continuously enhanced with professional certifications;
    - the budget of the internal audit function, presented by the Chief Audit Executive, is annually approved by the Audit and Compliance Committee;

- the remuneration of the Internal Audit Area's employees as well as the performance against the area's training plans are regularly reported to and reviewed by the Audit and Compliance Committee; results of these exercises are also presented to the Management Board and the Supervisory Board.

## 5. ASSESSMENT OF THE RISK MANAGEMENT SYSTEM

Santander Bank Polska S.A. has an integrated risk management framework ensuring that all risks having material impact on the Bank's operations are identified, measured, monitored and controlled.

In the opinion of the Supervisory Board, the risk management system in the Bank is adequate and effective, the risk management structure is adequate given the size of the Bank and the risk it is exposed to. It is also being optimised on an ongoing basis, and adjusted to the evolving external environment, as well as the risk profile deriving from the adopted strategy.

The responsibility for the management of individual risks was split between the Bank's organisational units that are supported by relevant Committees. The risk management strategy is set by the Management Board of the Bank and supported by the Risk Management Committee (RMC) and the Risk Control Committee (RCC) overseeing the activity of other Committees having risk management authority. Additionally, the Risk Management Sub-Committee was established within the Risk Management Committee to ratify the key decisions of lower-level committees (mostly with regard to large ticket credit transactions). The fact that members of the Management Board and senior management sit on key Committees ensures senior management engagement in the risk management of the Bank as representatives of both first and second line of risk management.

One of the basic elements of the risk management framework of Santander Bank Polska S.A. is setting and regular monitoring of the levels of risk that the Bank is ready to accept in its day-to-day business (the so-called risk appetite). The acceptable risk level is expressed in the form of quantifiable limits set out in the Santander Bank Polska Group Risk Appetite Statement approved by the Management Board and the Supervisory Board. The Bank conducts a detailed review of the limits with regard to the existing and potential risks, market conditions as well as the financial and capital plan at least once a year. Stress-testing and scenario analyses represent the key tools used to analyse the limits and ensure that the Bank retains an adequate capital position even in extreme and severe circumstances.

The Bank has methodologies and processes in place to identify and assess risks to determine their potential impact on the Bank's operations now and in the foreseeable future. With a view to identifying and assessing risks for the entire organisation, the review of material risks is carried out as part of the Internal Capital Adequacy Assessment Process (ICAAP). The identified risks are managed using policies and best practice to keep them at an acceptable level.

The Bank uses various risk assessment and measurement techniques depending on risk type and materiality, including:

- Customer and/or transaction grading models – for credit risk assessment purposes;
- VAR methodology for market risk; and
- Operational risk self-assessment methodologies.

The comprehensive risk management framework is supported by a consistent and transparent system aimed at monitoring and reporting risk levels and excesses against defined limits. The reporting system covers key management levels. The Supervisory Board receives regular reports assessing the level of identified risks and reports assessing the effectiveness of actions taken by the Bank's Management Board.

The Bank aims to keep the right risk/reward balance. Support for the Bank's development strategy, while retaining best in class risk management standards and compliance with the regulatory environment, is amongst the key assumptions underlying the risk management process.

In 2018 the Bank analysed thoroughly the developments in the macroeconomic environment, monitored credit exposures in individual customer segments and sectors of economy in order to ensure adequate and prompt response and to align the risk management policy parameters accordingly so that the Bank's security can be maintained. The year 2018 was quite stable in this respect, and the introduced changes modified the policy only moderately, mainly optimising and harmonising the existing elements of the risk management processes as well as reflecting changes arising from new regulations.

The key regulation affecting the measurement of credit risk was the entry into force of International Financial Reporting Standard 9 as of 1 January 2018. For several years the Bank was doing a number of projects to prepare the organisation in terms of operations, accounting and reporting to adopt the new standard. After finalisation of the projects in early 2018, in H1 2018, the Bank focused on analytical work to implement IFRS 9, including an analysis of the Bank's adaptation to the emerging market practice and industry interpretations aimed at ensuring consistent application of the standard. At the same time, the Bank took relevant measures to guarantee the stability of implemented models.



In 2018, the Group improved its credit exposure monitoring tools to ensure faster identification of potential threats both at the portfolio level and at the level of individual exposures. At the same time, the Group modified its monitoring strategies, focusing on early measures designed to limit the effects of potential risk materialisation.

The tight monitoring of the fx home loans continued to be one of the priorities in 2018. In response to numerous draft legislations, the Bank carried out comprehensive analyses and actively participated in the related consultations.

For many months, there were very intensive preparations underway to ensure smooth takeover of a part of the portfolio of Deutsche Bank Poland S.A. in November 2018. A number of projects were finalised such as the integration of data for sound risk management with respect to the acquired credit exposures, calibration of models for risk assessment of the combined customer base, ensuring liquidity following the takeover of assets as well as compliance with provision and impairment allowance calculation and reporting standards. In addition, a lot of measures were applied to mitigate the operational risk and the reputational risk attached to the consolidation of portfolios. The work on acquisition of the portfolio of Deutsche Bank Polska S.A. was successfully completed – the portfolios were integrated in the IT systems of Santander Bank Polska S.A. and no crisis situations occurred during the merger process.

The Supervisory Board and the Risk Committee were informed on the progress in implementing the most important risk programmes and projects on an ongoing basis in the form of Risk Dashboard (Unit Report).

## 6. ASSESSMENT OF SPONSORING AND CORPORATE GIVING POLICY OF SANTANDER BANK POLSKA S.A.

The Bank's sponsoring and corporate giving policy is set out in the document "Strategy behind sponsoring actions and sponsoring action plan of Santander Bank Polska S.A." (the "Policy"). The Policy's implementation is the responsibility of the Sponsorship and Relationship Projects Office and the Foundation of Santander Bank Polska S.A.

In the opinion of the Supervisory Board, the sponsoring and corporate giving policy of the Bank has been implemented in a reasonable and responsible manner, building the Bank's image as a socially responsible and trustworthy corporate citizen and contributing to the Bank's reputation and prestige among all stakeholders. Such values are core factors contributing to an enhanced corporate image.

Launched projects are primarily intended to strengthen the Bank's image as the second largest financial institution in the banking sector in Poland, the best commercial bank in Poland and a trustworthy, reliable, economically resilient institution with a nationwide footprint. The projects areas and scope are focused on:

- sharing the Polish culture values with a wide audience (bank supporting aspiring customers, affluent segment);
- supporting development of education, including financial education in Poland (investments for the future, employer branding actions building the image of the Bank as a good employer);
- promoting sport as a local community integration vehicle, active life-style and fair play rules (Bank as a partner for its customers);
- launching projects important to local communities (image building, partnership relations, employee engagement initiatives – employee volunteering).

Given the Bank's rebranding to Santander Bank Polska S.A., the marketing and image building campaigns in 2018, including sponsorship and CSR projects, were designed and launched to additionally increase the new brand's recognition apart from their sales support contribution. Focus was placed on building and emphasising positive emotions attached to the rebranding. This direction brought the expected results and effectively engaged the target groups – the Bank retained its position among banking leaders and most recognised brands in Poland and increased customers' awareness of its global group membership.

Our Bank is concentrated on long-term sponsorship initiatives. Such projects allow the Bank to reach a wider audience and to build positive connotations around the brand. They can also be used in relationship management and communication with employees and customers.

The key sponsoring projects of the Bank in 2018 were:

- Santander Orchestra (4th edition) project based on three initiatives: concerts, music workshops led by the best musicians playing various instruments and music workshops for children;
- UEFA Champions League – sponsor agreement made in November 2017 with Banco Santander as the new UEFA Champions League sponsor from the start of the 2018/2019 season (for three years). To leverage the promotional opportunities offered by the sponsorship of the most popular sporting events in the world, the Bank signed a contract with Polsat TV channel broadcasting the UEFA matches.
- "How's your driving" - driver education program with more than 120,000 followers on Facebook. The page had more than 25 million fans in 2018 and is one of the biggest FB profiles devoted to road safety in Poland. Santander Bank Polska S.A.'s "How's your driving" project was recognised internationally and received the European Excellence Award which has celebrated outstanding performances in the field of PR and communications.

The Foundation of Santander Bank Polska S.A. launches a number of CSR projects with its partners every year. The most important ones are the Foundation's grant programs. In 2018, grants were offered within the following programs: "Bank of Ambitious Youth", "Bank of Children's Smiles", "Here I live, here I make changes" (4th edition) and "Bank of Young Sports Champions" (2nd edition). Overall, 266 grants worth PLN 1,642,000 in total were distributed.

The staff volunteering program coordinated and financially supported by the Foundation covered 145 projects initiated and launched by the Bank's employees. More than 1312 volunteers from the Bank engage in such initiatives each year. 2018 was the first year in many years when the Foundation launched its scholarship program. There were 60 applications and 20 best candidates were offered financial support of PLN 5000 per school year. The short-listed candidates are from various regions of Poland and specialise in various fields.

The Bank's sponsorship and corporate giving initiatives also support the key directions of the Bank's Corporate Social Responsibility and Sustainable Development Policy based on five pillars: support for third-level education; scientific research and entrepreneurship; projects devoted to local communities; environment protection and active dialogue with stakeholders.

In 2018, the Bank issued its fifth CSR Report presenting the organisation's impact on local communities, the economy and the environment. It contains key business highlights and presents major sponsorship projects and community investments in numbers. It was prepared in accordance with the Global Reporting Initiative (GRI) Global Reporting Initiative standards – the Core level.

## 7. SUPERVISORY BOARD'S ASSESSMENT OF THE MANNER OF FULFILLING BY SANTANDER BANK POLSKA S.A. THE DISCLOSURE REQUIREMENTS WITH REGARD TO THE CORPORATE GOVERNANCE RULES SET OUT IN THE WSE RULES AND REGULATIONS PERTAINING TO CURRENT AND PERIODIC INFORMATION PUBLISHED BY ISSUERS OF SECURITIES

In line with rule II.Z.10 of 2016 *Code of Best Practice for WSE Listed Companies* issued by the Warsaw Stock Exchange, adopted by the Annual General Meeting of Shareholders on 20 April 2016, and prior to that by the Management Board and Supervisory Board, the Supervisory Board makes and presents to the AGM the assessment of the manner of fulfilling by Santander Bank Polska S.A. the disclosure requirements with regard to the corporate governance rules set out in the WSE rules and in regulations pertaining to current and periodic information published by issuers of securities.

To discharge its corporate governance information obligations, in 2018 the Corporate Legal Governance Office (in the Legal and Compliance Division) re-assigned individual principles to specific business units and received confirmation that Best Practice was applied.

As a result, no need to report any cases of non-compliance with any of the rules was identified.

In line with the obligation set forth in paragraph 29 (3) of the WSE Rules under the "comply or explain" formula, the non-adherence or incidental non-adherence to a given rule triggers an obligation for a company to immediately report such a situation. The required statement on compliance with the corporate governance rules arising from the Best Practice document is reported through the "Corporate Governance Statement for 2018" included in the annual report. This is treated as a fulfilment of the obligation to provide the WSE with a report on compliance with the corporate governance rules. The statement was included in Chapter XIII of the 2018 Management Board Report on Santander Bank Polska Group's performance published on 22 February 2019.

Given the above, the Bank's fulfilment of disclosure requirements in relation to the adherence to the Corporate Governance Rules in 2018 is positively assessed by the Supervisory Board, whilst the Bank's disclosures are a reliable source of information on its compliance with the corporate governance rules.

## 8. SUMMARY

Based on the assessment whose results are presented above, the Supervisory Board states that the situation of the Santander Bank Polska S.A. and Santander Bank Polska Group is good and stable. The assessment is justified in particular by:

- good financial performance in a challenging economic environment achieved at the same time when progressing strategic projects (including rebranding and acquisition of the organised part of the enterprise of Deutsche Bank Polska S.A.);
- effective risk management;

- strong capital and liquidity position;
- excellent cost management; and
- efficient internal control system.

The Supervisory Board highlights a very good relationship with the Bank's Management Board and extends its congratulations to the Management Board and employees of Santander Bank Polska S.A. and its Group for a rewarding co-operation and overall efforts in building the Bank's strong position on the financial market.

## IV. ASSESSMENT OF COMPLIANCE WITH THE CORPORATE GOVERNANCE RULES FOR SUPERVISED INSTITUTIONS

As of 1 January 2015, Santander Bank Polska S.A. has followed and adhered to the Corporate Governance Rules for Supervised Institutions ("Corporate Governance Rules") implemented under Resolution no. 218/2014 issued by the Polish Financial Supervision Authority (KNF) on 22 July 2014. This is an important document for the Bank's corporate policy as a public trust institution.

The Corporate Governance Rules were approved by way of Resolution no. 29 passed by the Annual General Meeting held on 23 April 2015 and based on the relevant resolutions of the Bank's Management Board and Supervisory Board.

The Rules cover a wide range of issues, including among others internal and external relations of the Bank, also with the shareholders and customers, organisation and functioning of internal supervision and key internal systems and functions, statutory bodies and principles of cooperation, which requires the Bank to comply with top standards and to ensure that the obligations arising from the regulations are adequately fulfilled.

Therefore, the Bank precisely defined organisational units (the so-called business owners) responsible for the adherence to and implementation of the rules assigned to them in line with their area of responsibility in the Bank. Throughout 2018, these units took appropriate measures to ensure compliance with the Corporate Governance Rules.

At the end of 2018, all business owners were asked to report on their unit's compliance with the Corporate Governance Rules. All units fulfilled their obligations on time by providing assurance on the application of the Corporate Governance Rules and indicating the actions that reflected their professionalism, integrity and diligence.

Given the above, the Supervisory Board stated that the process of implementing the Corporate Governance Rules in the Bank in 2018 was carried out adequately. The process was subject to current, in-depth supervision by the business owners. The coordination of the process and collaboration between business owners in joint implementation of certain rules were also effective.

Therefore, the Supervisory Board positively assesses the application of the Corporate Governance Rules in 2018 by the Bank.

## V. ASSESSMENT OF THE REMUNERATION POLICY OF SANTANDER BANK POLSKA S.A.

This assessment was made pursuant to paragraph 28 (3) of the Corporate Governance Rules approved by Resolution No 29 of the Bank's Annual General Meeting issued on 23 April 2015 which states that the supervising body should present the legislative body with a report on the Remuneration Policy of the supervised institution on an annual basis.

The remuneration principles of Santander Bank Polska S.A are defined in the Remuneration Policy of Santander Bank Polska Group. At the same time, the following apply in the Bank:

1. *Remuneration policy for members of the Supervisory Board of Santander Bank Polska S.A. (former: BZ WBK S.A.),*
2. *Remuneration Policy for members of the Management Board of Santander Bank Polska S.A. (former: BZ WBK S.A.),*
3. *Rules for payment of variable remuneration to Identified Employees in 2018 in Santander Bank Polska S.A. (former: BZ WBK S.A.).*

The rules for paying fixed and variable remuneration to the Bank's Management Board members and key employees arise from the above Policies and the bonus regulations based on them as well as from regulations on variable components of remuneration paid to individuals with the status of identified employees. The Remuneration Policy aims at defining the principles of employee remuneration, recognising minimum standards required by the Bank's Group and the law. The Remuneration Policy is the key element of the remuneration strategy and it serves as a reference for designing, reviewing, implementing and overseeing the remuneration practices. The Policy is linked to the strategic objectives of the organisation, its short and long-term goals, long-term interests and performance; the policy also takes into account qualitative and quantitative criteria and solutions aimed at avoiding discrimination for any reason.

Given the applicable 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, the Compensation Department together with the Compliance Area at least once a year review all internal legal documents related to remuneration policy applicable in the Bank. The review also takes account of best practice defined in the Remuneration Policy applicable in Santander Group. As part of the review in 2018, the Remuneration Policy of Santander Bank Polska Group was extended by the provisions on the scope of variable remuneration to include the sales of investment and insurance products and the definition of the conflict of interests. Additionally, the period of the *malus clause* application was defined.

The provisions of the Policies and regulations applicable in the Bank comply with statutory regulations and implementing acts. Moreover, in 2018, the Internal Audit Area carried out a review of the documents on variable components of remuneration paid to material risk takers in Santander Bank Polska S.A. and issued a "satisfactory" global rating.

The IAA indicated that in terms of oversight there was an adequate model in place, the organisational structure and the committees' structures were adequate and provided due oversight of the development and execution of the policy on variable components and that bonuses were approved at the adequate level.

It was established that the Policy on variable components of remuneration ensured compliance with the rules for taking account of the Bank's risk and strategy when defining the variable components whilst the list of the identified employees of the Bank was duly defined in compliance with the KNF's and the EU's regulations.

The Internal Audit Area did not issue any recommendations.

The Bank has a centre of excellence with sufficient knowledge and skills enabling independent update and verification of the list of identified employees holding the status of Material Risk Takers (MRT). Similarly to 2017, the Bank has identified employees whose professional activity has a significant impact on risk profile of the institution based on standards defined in Commission Delegated Regulation (EU) No 604/2014 of 4 March 2014. In 2018, 67 employees of Santander Bank Polska S.A. were covered by that Policy. In 2018, the identification was benchmarked to banking sector practices in Poland and was made in cooperation with a leading consulting company from the market. Each time the identification of MRTs is completed and the list of individuals is approved by resolution of the Supervisory Board, a formal communication process addressed to all identified employees takes place. In Q4 2018, the list of identified employees drafted in H1 2018 was verified (63 identified employees). Following the review of personnel and organisational changes, the list of identified employees was extended by 4 people.

The Supervisory Board performed oversight of the Remuneration Policy, also by verifying whether the criteria and conditions for variable remuneration had been fulfilled prior to the payment of the variable remuneration, either in part or in full.

Bearing in mind the above, the Supervisory Board states that the Policy supports the Bank's growth and security, and in particular sound and effective risk management, and is compatible with its business strategy, objectives, values and long-term interests.