



ANNUAL REPORT 2016
OF BANK ZACHODNI WBK

2016



Bank Zachodni WBK

 Grupa Santander

Dear All,

2016 was a year of seeking growth opportunities amid sustained market and social uncertainty. The European economy had to come to terms with the prospective Brexit whilst the Polish economy was faced with a paradigm shift in development concepts and the slowdown in the GDP growth. The domestic banking sector was confronted with multiple external pressures arising from regulatory and legislative requirements, among other things.

In these conditions, Bank Zachodni WBK consistently pursued its growth strategy, consolidating its position among the top Polish banks. In many business areas our results were not only above the market average, but also ahead of the entire sector.

Macroeconomic environment – relative stabilisation

The key challenges for the European economy in 2016 were centred around the consequences of political developments. The historical decision taken by the British to sever institutional ties with the European Union (Brexit) marks the beginning of building new economic relations between the UK and the entire EU, a process which may take several years. Likewise, two other events: the constitutional referendum in Italy and presidential elections in the United States, have posed important questions about the impact on the European economy. Encouragingly, the turbulence triggered by the above events was short-lived and markets quickly regained stability. According to most estimates, in 2016, GDP of the eurozone was around 1.8%, and in EU-28 it stood at nearly 1.9%. After many years of deflation, inflation is back in the eurozone and the end of the year saw a pronounced improvement in the market climate: the PMI index for the industry sector and the services sector of the eurozone increased to 54.9 points, the lowest level in more than five years. The future potential threats to the European economy may involve geopolitical unrest and increased risk of protectionism that may have unfavourable effect on international trade and economic growth in the long-term.

All in all, the Polish economy in 2016 was characterised by a weaker-than-expected economic growth. According to estimates, for the first time in three years, the domestic GDP, measured for the whole year, did not exceed 3% (it was estimated at 2.5% YoY in Q4). Investments, particularly public ones, were disappointing. Their decrease was associated with a delayed absorption of EU funds as part of the new financial perspective. Exports were stagnant, which reflected the sluggish international trade globally. Like in the most of Western European countries, Poland's economic growth strongly depended on internal demand. However, due to the significant social outlays in 2016 (the start of the "Family 500+" child benefit programme), it was expected that the value of private consumption would exceed 3.9% for the whole year. Nonetheless, it was the economic standing of households that was the most positive feature of our landscape – the number of the employed reached its historical high, the wage growth accelerated and consumer optimism increased to a record level. The financial position of enterprises improved as well.

In 2017, the national economy should see an acceleration of growth, including as a result of a gradual increase in investments, (at least) stable consumption growth and projected recovery of exports.

Banking sector poised to meet the challenges

In 2016 the Polish banking sector successfully resisted both external pressures and the challenges inherent in the process of banks' aligning business models to the changing market conditions. Despite the numerous charges resulting from regulations that had an unfavourable impact on the sector, and the historically lowest interest rates, the total capital ratio of the Polish banking sector increased. Banks also managed to increase their revenues and earnings. The consolidation processes that started several years ago gained momentum with a number of ownership changes in the Polish banking sector. It is worth noting that state-run entities were the most active in sector consolidation in 2016.

A key outstanding issue for the banking sector in Poland is the resolution of the FX mortgage loans problem, announced by the legislative, executive and regulatory authorities. Taking into account the severity of challenges and concerns in the European financial markets (including the crisis in the Italian banking system) and the high volatility in the domestic regulatory landscape, including the requirements set for the sector, the final solutions in this regard should be dealt with properly, taking into account, in a balanced and proportional manner, the interests of the borrowers, security of lenders, stability of the entire banking sector and, consequently, a lack of negative impact on the Polish economy.

Strategic focus on customers

Customers and partnership relations with them are always at the heart of the Bank's strategic development and business transformation. The transformation that has been part of the Bank's business covers many key initiatives designed to bring improvement for customers. One of these is process simplification, which will allow a consistent, transparent and clear offer to be presented to address the needs and expectations of the existing and new customers of Bank Zachodni WBK. In short, our ambition is to be present in those distribution channels that are most convenient for customers, including mobile, internet, phone and branch banking. This is how we define and understand our mission as a Bank, which is Simple, Personal and Fair and helps people and businesses prosper.

Our financial performance in 2016 is evidence that despite the regulatory and legislative pressure and other challenges we remain a stable, a steadily growing institution. In 2016, the profit before tax of Bank Zachodni WBK was more than PLN 2.6 billion.

The value of our assets exceeded PLN 131.4 billion. In the demanding environment of historically lowest interest rates we managed to achieve a year-on-year growth in net interest income and fee income. We remained a leader among our Polish peers in terms of effectiveness measured by ROE.

Bank Zachodni WBK managed its cost base strictly within the budget and duly met all the additional tax charges, mandatory costs of participation in the banking system and in the deposit guarantee scheme. Our capital base is strong and our cost-to-income ratio stands out positively in the sector. In 2016 we demonstrated that in terms of diversification of our business, we were one of the best organised and effective bank in the market. Bank Zachodni WBK confirmed the effectiveness of its strategy and reported robust performance in individual business segments.

Last year was record-breaking for our Bank in terms of the number of retail loans sanctioned. The number of home mortgages increased by more than 20% YoY (30% in terms of value). Also, with regard to consumer finance products we have been much above the market average, with sales of PLN 5.9 billion. Our deposit acquisition efforts yielded an unprecedented result with an increase of 22% in personal and savings account balances. Bank Zachodni WBK opened more than 346 thousand new personal accounts, including nearly 261 thousand Accounts Worth Recommending. We have been very successful in online sales of personal accounts, the number of accounts opened being twice as high as in 2015.

The portfolio of credit cards was nearly 7% higher YoY with nearly 800 thousand cards at the end of 2016. Furthermore, 2016 saw a major growth (by 25%) in demand for non-related insurance products. More than 1.2 million customers have already taken out insurance via the Bank. The sales of cancer insurance (Onkopolisa) were particularly high. By the end of the year, it was sold to more than ten thousand customers. Bank Zachodni WBK finished the year as a leader among banking distributors of mutual funds as measured by net sales.

In the SME segment we are making consistent efforts to become a preferred banker for Polish firms. In 2016 we put together a new business account offer (Account Worth Recommending and Account Worth Recommending Premium). Thanks to improved standardisation and streamlining of many procedures, the number of new, active customers increased by 50%. In 2016 the Business and Corporate Banking Division continued its strategy focused on increasing its share in the corporate customers market. As a result, the performing loans portfolio increased by 5% YoY in the corporate segment and the deposit balance rose by 9%. The Bank successfully developed its business activity in the food & agri sector, which resulted in a 23% YoY increase in customer assets. Also, the Exports Development Programme was continued to ensure that customers could reach new business partners in the markets where Santander Group is present. This was reflected in the rapid growth in export finance, which increased by 8% YoY.

The Global Corporate Banking Division successfully developed its proposition, using the international know-how of Santander Group, e.g. by joining the innovative FX platform and becoming a leader in the global trade in Polish government bonds. The division finalised a number of financing transactions with customers from the food, telecommunication, property and financial sectors, including capital raising for a financial institution as part of the largest public offering on the WSE since 2013 and the largest issue of shares with pre-emptive rights since 2009.

The multichannel transformation of Bank Zachodni WBK results in an increased activity of our customers in online and mobile banking segments, as well as higher value of facilities sold in both channels (increase by nearly 45% YoY). Bank Zachodni WBK was one of the mobile banking pioneers in Poland and we aim at constant improvement of our market position. Last year, we introduced mobile HCE payments, BLIK transfers via phones and Android Pay. With our payments strategy we want to focus first of all on building the value added based on mobile application that will be the customer's payment management hub, i.e. their "wallet" of the future. Our strength is best proven by the fact that in 2016 the number of our mobile banking users increased by more than 30% YoY. The mobile solution of Bank Zachodni WBK was also recognised by international experts. We were ranked 1st in Poland and 3rd in Europe in the prestigious ranking European Mobile Banking, Functionality Benchmark.

Transformation of the Bank

Bank Zachodni WBK is among the leaders of digital revolution that is changing the face of the banking sector in Poland. To develop this trend, a Transformation Programme has been set up at the Bank, which is focused both on optimisation of the product offering and on improvement of processes for our customers. Our overarching objective is to remain the first-choice bank for our existing and new customers. The work undertaken under the Transformation Programme is focused on improving the quality of service, further development of innovative products and services, increasing sales effectiveness and keeping costs down. The key initiatives include digitisation and automation of processes, creating an optimum model of distribution channels, further development of CRM and remote channels. All these measures are expected to improve customer experience, encourage referrals and to strengthen satisfaction with the level of service among the Bank's new and existing customers and business partners. The transformation covers not only retail banking, but also SME and corporate banking.

Corporate Social Responsibility

Bank Zachodni WBK is a proud promoter of Corporate Social Responsibility projects. In 2016, as part of Poland's largest programme of cooperation between the world of science and business – Santander Universidades, comprising already 64 Polish universities, we extended support to 1026 scholarship holders. We issued and activated 1023 Student IDs with a payment function (smartcards).

We also do the Barrier-Free Banking programme and have implemented a number of features, in all service channels, to assist movement, hearing and vision impaired persons, including video calls with advisors who speak the sign language, the “talking ATMs” or electronic banking adapted to the needs of the visually impaired.

2016 was also very special for us in terms of our marketing activity. We put together a unique social media campaign “12th Player”, telling about the emotions associated with supporting our national football team and emphasising the feeling of togetherness among Poles. We were one of the most visible institutions in the traditional, electronic and social media.

Our campaigns endorsed by Łukasz Fabiański, among others, resulted in record loan sales for the Bank.

Our social activities have been assisted by the Foundation of Bank Zachodni WBK, which has been actively operating for more than 20 years. Only in 2016 the foundation provided social organisations with 227 grants totalling PLN 1.2 million (e.g. as part of the Bank of Children’s Smiles or the Bank of Ambitious Youth programmes). The number of active volunteers have been increasing year over year (with more than 600 at present). In the social area, our intention is to help as many beneficiaries as possible. Under the projects carried out by the Bank and our foundation, we extended aid to more than 115,000 beneficiaries in 2016.

Last year, Bank Zachodni WBK issued the third CSR Report, describing its social activities in 2015. In the “Social Reports” competition, the Bank was awarded by journalists for reporting essential data from the key stakeholders’ perspective. The report was also voted the best by internet users.

Bank Zachodni WBK may also boast the title of the Best Bank in Poland awarded by Euromoney Awards for Excellence 2016 in recognition of its outstanding effectiveness and excellent financial performance. We received the statuette and title of the Banking Quality Leader 2016 in the Busies Friendly Bank Competition. The competition jury recognised Bank Zachodni WBK for our exceptionally active approach towards SMEs, extensive offer, and high service quality.

Simple, Personal and Fair

The satisfactory results generated by Bank Zachodni WBK in 2016 are an effect of the trust that customers have for our development strategy. Moreover, and let me emphasise this, it reflects the skills, experience and engagement of all the Bank’s employees, features that are evident in their daily efforts to strengthen our market position. Our main shareholder, Santander Group, helps us build best practice and provides us with valuable inspiration for our key banking projects.

In 2016 changes took place in the Bank’s Management Board. Artur Chodacki joined the Board as Head of Small and Medium Enterprise Banking Division, while Feliks Szyszkowiak became responsible for the Digital Transformation Division. In addition, Dorota Strojewska was appointed a new member of the Management Board. In turn, Beata Daszyńska – Muzyczka and Paweł Wieczorek resigned as Board members.

I joined the Management Board of Bank Zachodni WBK on 29 November 2016. I would like to thank Gerry Byrne, the Supervisory Board Chairman, and the entire Supervisory Board for their trust and assure you that this is an utmost honour and privilege for me to be part of the Bank’s team.

Michał Gajewski

CEO of Bank Zachodni WBK Management Board

FINANCIAL HIGHLIGHTS		PLN k		EUR k		
		for reporting period ended:		31.12.2016	31.12.2015	31.12.2016
Stand alone financial statement						
I	Net interest income		3 480 440	3 134 852	795 402	749 104
II	Net fee and commission income		1 604 735	1 613 244	366 738	385 501
III	Operating profit		3 005 326	2 176 553	686 822	520 109
IV	Profit before tax		2 649 248	2 176 553	605 446	520 109
V	Profit for the period		2 081 720	1 756 210	475 746	419 664
VI	Total net cash flows		(175 348)	(383 623)	(40 073)	(91 671)
VII	Total assets		131 417 988	125 477 589	29 705 693	29 444 465
VIII	Deposits from banks		1 212 765	548 558	274 133	128 724
IX	Deposits from customers		103 381 249	94 021 282	23 368 275	22 062 955
X	Total liabilities		112 388 468	106 768 460	25 404 265	25 054 197
XI	Total equity		19 029 520	18 709 129	4 301 429	4 390 268
XII	Number of shares		99 234 534	99 234 534		
XIII	Net book value per share in PLN/EUR		191.76	188.53	43.35	44.24
XIV	Capital ratio		16.52%	15.80%		
XV	Profit per share in PLN/EUR		20.98	17.70	4.79	4.23
XVI	Diluted earnings per share in PLN/EUR		20.94	17.67	4.79	4.22
XVII	Declared or paid dividend per share in PLN/EUR*		*	13,00	*	3,05

*As of the date of publication of this report, the Management Board of Bank Zachodni WBK has not finalised its analysis in respect of recommendation on dividend payout for 2016.

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

- for balance sheet items – average NBP exchange rate as at 30.12.2016: EUR 1 = PLN 4.4240 and as at 31.12.2015: EUR 1 = PLN 4.2615
- for profit and loss items – as at 31.12.2016 - the rate is calculated as the average of NBP exchange rates prevailing as at the last day of each month in 2016: EUR 1 = PLN 4.3757; as at 31.12.2015 - the rate is calculated as the average of NBP exchange rates prevailing as at the last day of each month in 2015: EUR 1 = PLN 4.1848

As at 31.12.2016, FX denominated balance sheet positions were converted into PLN in line with the NBP FX table no. 252/A/NBP/2016 dd. 30.12.2016.



**FINANCIAL STATEMENT
OF BANK ZACHODNI WBK
FOR 2016**

2016



Bank Zachodni WBK

 Grupa Santander

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in thousands of PLN

Income statement of Bank Zachodni WBK

	for reporting period:	01.01.2016- 31.12.2016	01.01.2015- 31.12.2015
Interest income		4 469 917	4 243 768
Interest expenses		(989 477)	(1 108 916)
Net interest income	Note 5	3 480 440	3 134 852
Fee and commission income		1 904 106	1 887 844
Fee and commission expenses		(299 371)	(274 600)
Net fee and commission income	Note 6	1 604 735	1 613 244
Dividend income	Note 7	439 288	156 365
Net gains/(losses) on subordinated entities		-	234 391
Net trading income and revaluation	Note 8	266 371	193 495
Gains (losses) from other financial securities	Note 9	401 189	273 717
Other operating income	Note 10	119 465	119 649
Impairment losses on loans and advances	Note 11	(583 479)	(667 895)
Operating expenses incl.:		(2 722 683)	(2 881 265)
<i>Bank's staff, operating expenses and management costs</i>	<i>Notes 12,13</i>	<i>(2 360 209)</i>	<i>(2 589 034)</i>
<i>Depreciation/amortisation</i>		<i>(234 117)</i>	<i>(206 104)</i>
<i>Other operating expenses</i>	Note 14	<i>(128 357)</i>	<i>(86 127)</i>
Operating profit		3 005 326	2 176 553
Tax on financial institutions		(356 078)	-
Profit before tax		2 649 248	2 176 553
Corporate income tax	Note 15	(567 528)	(420 343)
Profit for the period		2 081 720	1 756 210
Net earnings per share (PLN/share)	Note 16		
Basic earnings per share		20,98	17,70
Diluted earnings per share		20,94	17,67

Statement of comprehensive income of Bank Zachodni WBK

	for reporting period:	01.01.2016- 31.12.2016	01.01.2015- 31.12.2015
Profit for the period		2 081 720	1 756 210
Other comprehensive income which can be transferred to the profit and loss account:		(492 701)	(185 890)
Available-for sale financial assets valuation, gross		(713 041)	(119 113)
Deferred tax		135 478	22 632
Cash flow hedges valuation, gross		104 768	(110 382)
Deferred tax		(19 906)	20 973
Other comprehensive income which can't be transferred to the profit and loss account		5 208	8 042
Provision for retirement allowances – actuarial gains/losses, gross		6 430	9 929
Deferred tax		(1 222)	(1 887)
Other comprehensive income for the period, net of income tax		(487 493)	(177 848)
TOTAL COMPREHENSIVE INCOME FOR THE PERIOD		1 594 227	1 578 362

Notes presented on pages 8 - 88 constitute an integral part of this Financial Statement.

in thousands of PLN

Statement of financial position of Bank Zachodni WBK

		as at:	31.12.2016	31.12.2015
ASSETS				
Cash and balances with central banks	Note 17		4 696 634	6 129 543
Loans and advances to banks	Note 18		3 308 802	4 484 202
Financial assets held for trading	Note 19		3 198 187	4 174 634
Hedging derivatives	Note 20		66 787	162 823
Loans and advances to customers	Note 21		87 102 390	81 125 350
Buy-sell-back transactions	Note 40		-	289 260
Financial assets available for sale	Note 22		26 322 361	22 576 246
Investments in subsidiaries and associates	Note 23		2 377 325	2 377 325
Intangible assets	Note 24		464 308	443 603
Goodwill	Note 25		1 688 516	1 688 516
Property, plant and equipment	Note 26		779 866	742 245
Net deferred tax assets	Note 27		950 307	842 763
Assets classified as held for sale	Note 28		608	637
Other assets	Note 29		461 897	440 442
Total assets			131 417 988	125 477 589
LIABILITIES AND EQUITY				
Deposits from banks	Note 30		1 212 765	548 558
Hedging derivatives	Note 20		1 961 828	2 024 012
Financial liabilities held for trading	Note 19		1 809 969	2 535 708
Deposits from customers	Note 31		103 381 249	94 021 282
Sell-buy-back transactions	Note 40		-	4 007 525
Subordinated liabilities	Note 32		440 457	426 507
Debt securities in issue	Note 33		1 783 303	1 698 619
Current income tax liabilities			12 999	165 537
Provisions	Note 34		66 345	82 649
Other liabilities	Note 35		1 719 553	1 258 063
Total liabilities			112 388 468	106 768 460
Equity				
Share capital	Note 36		992 345	992 345
Other reserve capital	Note 37		15 132 993	14 238 675
Revaluation reserve	Note 38		281 754	769 247
Retained earnings			540 708	952 652
Profit for the current period			2 081 720	1 756 210
Total equity			19 029 520	18 709 129
Total liabilities and equity			131 417 988	125 477 589

Notes presented on pages 8 - 88 constitute an integral part of this Financial Statement.

in thousands of PLN

Statement of changes in equity

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

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

Statement of changes in equity	Share capital	Other reserve capital	Revaluation reserve	Retained earnings and profit for the period	Total
Note	36	37	38		
Opening balance as at 31.12.2014	992 345	13 177 940	947 095	1 994 632	17 112 012
Total comprehensive income	-	-	(177 848)	1 756 210	1 578 362
Profit for the period	-	-	-	1 756 210	1 756 210
Other comprehensive income	-	-	(177 848)	-	(177 848)
Distribution of profits and losses	-	1 041 980	-	(1 041 980)	-
Share scheme charge	-	18 755	-	-	18 755
As at 31.12.2015	992 345	14 238 675	769 247	2 708 862	18 709 129

The revaluation reserve of PLN 769,247k comprises valuation of debt securities of PLN 181,310k, equity shares of PLN 781,761k, cash flow hedges of PLN (196,442)k and the provision for retirement allowances with cumulative actuarial gains of PLN 2,618k.

Notes presented on pages 8 - 88 constitute an integral part of this Financial Statement.

in thousands of PLN

Statement of cash flows of Bank Zachodni WBK

	for reporting period:	01.01.2016- 31.12.2016	01.01.2015- 31.12.2015
Profit before tax		2 649 248	2 176 553
Total adjustments:			
Depreciation/amortisation		234 117	206 104
Profit (loss) from investing activities		(407 305)	(531 489)
Impairment losses		13 767	322
		2 489 827	1 851 490
Changes in:			
Provisions		(16 304)	(27 867)
Trading portfolio financial instruments		950 591	800 422
Hedging derivatives		33 852	866 152
Loans and advances to banks		1 005 145	121 331
Loans and advances to customers		(5 977 040)	(6 479 470)
Deposits from banks		225 942	(143 276)
Deposits from customers		9 079 395	4 081 973
Buy-sell/ Sell-buy-back transactions		(3 990 565)	(1 831 263)
Other assets and liabilities		460 547	449 873
		1 771 563	(2 162 125)
Interest accrued excluded from operating activities		(508 586)	(473 784)
Dividend		(438 757)	(154 986)
Paid income tax		(713 260)	(737 207)
Net cash flows from operating activities		2 600 787	(1 676 612)
Inflows		6 237 656	6 498 340
Sale of investments in subsidiaries		-	244 316
Sale/maturity of financial assets available for sale		5 179 272	5 378 212
Sale of intangible assets and property, plant and equipment		19 534	77 002
Dividend received		438 609	154 986
Interest received		600 241	643 824
Outflows		(8 451 780)	(4 823 050)
Purchase of financial assets available for sale		(8 155 389)	(4 516 952)
Purchase of intangible assets and property, plant and equipment		(296 391)	(306 098)
Net cash flows from investing activities		(2 214 124)	1 675 290
Inflows		2 454 500	1 327 019
Debt securities in issue		1 065 880	715 000
Drawing of loans		1 388 620	612 019
Outflows		(3 016 511)	(1 709 320)
Debt securities buy out		(980 000)	-
Repayment of loans		(670 906)	(1 618 109)
Dividends and other payments to shareholders		(1 290 049)	-
Interest paid		(75 556)	(91 211)
Net cash flows from financing activities		(562 011)	(382 301)
Total net cash flows		(175 348)	(383 623)
Cash at the beginning of the accounting period		11 729 903	12 113 526
Cash at the end of the accounting period		11 554 555	11 729 903

*Cash components are presented in Note 45.

Notes presented on pages 8 - 88 constitute an integral part of this Financial Statement.

in thousands of PLN

Additional notes to financial statement of Bank Zachodni WBK

1. General information about issuer

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

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

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

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

2. Basis of preparation of financial statement

Statement of compliance

This financial statement of Bank Zachodni WBK was prepared in accordance with the International Financial Reporting Standards (IFRS) adopted by the European Union, which are applied on a consistent basis, as at 31.12.2016 and, in the case of matters not governed by the above Standards, in accordance with the provisions of the Accounting Act of 29.09.1994 (consolidated text: Journal of Law of 30.01.2013, item 330, as amended) and related implementing acts as well as the requirements imposed on issuers whose securities are admitted to trading on regulated markets or issuers who have applied to have securities admitted to trading on regulated markets.

Thi financial statements have been approved for publication by the Bank's Management Board on 14.02.2017.

In addition, please note that Consolidated financial statements of BZ WBK Group for 2016 were published on 17.02.2017.

in thousands of PLN

New standards and interpretations or changes to existing standards or interpretations which can be applicable to the Bank and are not yet effective or have neither been implemented earlier

IFRS	Nature of changes	Effective from	Influence on Bank
Amendments to IAS 7 Statement of Cash Flows *	Amendments to IAS 7 introduce the requirements to disclose changes in liabilities arising from financing activities in statement of cash flows, including both changes arising from cash flows and non-cash changes.	1 January 2017	The amendments will not have any material impact on the financial statement.
Amendment to IAS 12 Income Taxes *	The amendment clarifies the application of the standard for the recognition of a deferred tax asset in the case of losses on measurement of financial instruments classified as available for sale, among other things debt instruments.	1 January 2017	The amendments will not have any material impact on the financial statement.
IFRS 9 Financial Instruments	<p>The changes refer to the following areas:</p> <ul style="list-style-type: none"> • Classification and measurement – introduction of three classification categories for debt instruments, i.e. measured at: amortised cost, fair value through other comprehensive income and fair value through profit or loss. Changes were made in the measurement of equity instruments by limiting the possibility of measurement at historical cost; • Expected credit losses – introduction of a new model for recognition of impairment (ECL): impairment charge is required to be measured as lifetime expected credit losses rather than 12-month expected credit losses; • Hedge effectiveness testing and eligibility for hedge accounting – replacement of the precise effectiveness range (80-125%) with a requirement that there is an economic relationship between the hedged item and the hedging instrument and that the hedge ratio is the same as the one used for risk management purposes. Ineffective hedges continue to be taken to a profit and loss account; • Hedged items – new requirements allow appointment of new hedged items in relation to certain economically viable hedging strategies, which, to date, were not eligible under IAS 39; • Hedging instruments – relaxation of requirements pertaining to certain hedging instruments listed in IAS 39. The standard allow recognition of the time value of options purchased and implementing non-derivative financial instruments as hedging instruments; • Recognition of change in the fair value of financial liability arising from changes in the liability's credit risk in other comprehensive income (in principle). 	1 January 2018	IFRS 9 implementation progress is described below.
IFRS 15 - Revenue from Contracts with Customers	<p>Changes relate to the following areas:</p> <ul style="list-style-type: none"> • Transfer of control – recognition of revenue only when the customer gains control over a good or service. The amendment makes the definition of the transfer of control more precise. Introducing regulations allowing to define the legitimacy of recognising the revenue over time or at a point in time; • Variable consideration - the amendment takes into account variable consideration in prices of goods or services arising, for example, as a result of penalties or performance bonus; • Allocation of the transaction price on the basis of an adequate sales price per unit - introduction of the requirement to allocate the payment for goods or services in the case of sale under a single contract; • Licences - introduction of the requirement for entities to define the time for which a licence is transferred and specifying more precisely the revenue calculation in the case of transferring a licence at a point in time or over time; • Time value of money – the transaction price is adjusted for the time value of money. The entity may choose not to account for the time value of money when the interval between transfer of the promised goods or services and payment by the customer is expected to be less than 12 months; • Costs of obtaining a contract - introducing the conditions which determine if the given costs of obtaining a contract are subject to capitalization and can be amortised parallel to revenue recognition; • Disclosures - introduction of a requirement to disclose qualitative and quantitative information relating to judgements and changes in the judgements related with revenue recognition. 	1 January 2018	The Bank does not expect significant impact on revenue recognition model.

in thousands of PLN

IFRS 16 Leases *	<p>Changes relate to the following areas:</p> <ul style="list-style-type: none"> • Introduction of a new definition of lease as an agreement or part of an agreement; • Recognition by lessee - the change will influence balance-sheet measurements; • Recognition by lessor - in the case of book recognition of sales and leaseback and additional disclosures. 	1 January 2019	The total obligations under irrevocable operating lease agreements concluded by the Bank are presented in disclosure number 44.
Amendments to IFRS 2: Classification and measurement share-based payment transactions *	<p>Changes relate to the following areas:</p> <ul style="list-style-type: none"> • Guideliness on fair value measurement of liability due to cash-settled share-based payment transaction; • Guideliness on classification modification from cash-based to equity-settled payment transactions and also • Guideliness on employees tax liabilities recognition relating to share-based payment transactions. 	1 January 2018	The Bank has not completed the analysis of changes.

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

IFRS 9 “Financial instruments”

Classification and measurement

IFRS 9 removes currently existing under IAS 39 categories, in particular held-to-maturity investments and available-for-sale financial assets. Financial assets' classification under IFRS 9 depends from financial assets' business model management and contractual cash flow characteristics. According to the standard financial instruments are classified to one of the two groups:

- financial assets measured at fair value or
- financial assets measured at amortized cost.

In 2016, the Bank has preliminarily identified business models which are not contrary to the segments determined for the management purposes. It is only for the ALM and Centre segment that the Bank analyses the merits of the distinguishing of the following two business models: a hold-to-collect business model and a hold-to-collect-and-sell business model.

Based on current contractual cash flow analysis and the business model assessment, the Bank assumes that there will be no significant changes with respect to the classification:

- financial assets classified as Loans and Advances under IAS 39 will generally be classified into amortized cost under the condition that instrument passes SPPI test,
- available for sale debt instruments will generally continue to be classified into fair value with changes in other comprehensive income,
- available for sale equity instruments shall be classified into fair value, and depending on the nature of the investment, their variations will be recorded in the income statement or in other comprehensive income,
- Financial instruments currently classified into fair value through profit or loss will generally continue to be classified into fair value through profit or loss.

The Bank is currently implementing an analysis of its portfolios given contractual cash flow characteristics test and business model assessment outcomes in order to identify and classify the financial instruments into their corresponding portfolio under IFRS 9.

Hedge accounting

IFRS 9 includes new hedge accounting requirements which have a twofold objective: to simplify current requirements, and to bring hedge accounting in line with risk management, so allowing there to be a greater variety of derivative financial instruments which may be considered to be hedging instruments.

Furthermore, additional breakdowns are required providing useful information regarding the effect which hedge accounting has on financial statements and also on the entity's risk management strategy.

Once the analysis of the advantages and disadvantages of the proposal is completed, the Bank shall make its decision for hedge accounting under IFRS 9. According to the best estimates hedging relations will be continued.

in thousands of PLN

Impairment of credit exposures

IFRS 9 introduces a new approach to estimating impairment charges for assets measured at amortised cost. The new approach will be based on expected credit loss instead of the incurred loss model that is used currently under IAS 39.

In accordance with IFRS 9, the measurement of expected losses will depend on changes in credit risk after recognition of the exposure. The standard introduces three main stages for recognising estimated credit losses:

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

One of the aspects of implementation of IFRS 9 is to work out a definition of a significant increase in credit risk that determines the classification of an exposure as Stage 2. In 2016, the Bank started work on systematisation of the definition of a significant increase in risk. The definition will use the key criteria laid down in IFRS 9, such as delay in repayment exceeding 30 days and the Bank's PD/rating models as well as additional elements of a qualitative risk assessment used in the process of exposure monitoring. To identify a significant increase in risk it is also necessary to compare the risk assessment at the time of initial recognition with the current assessment at the reporting date, which entails major technological changes in impairment allowance calculation.

Another key feature introduced by IFRS 9 is the approach to the estimation of risk parameters. For the purpose of estimating impairment allowances, the bank plans to continue using own estimates of risk parameters (PD, LGD, CCF) that are based on internal models. However, in the context of IFRS 9 requirements, the process of models calibration will change significantly. As a result of transition from the incurred loss to expected loss model, the emergence period/ loss identification period (LIP) parameter will no longer be used for provision calculation on the IBNR portfolio. On average for the whole portfolio of the Bank, emergence period/LIP was shorter than 12 months, so as a result of transition to IFRS 9, the provision estimation horizon will increase (Stage 1 - 12 months, Stage 2 - lifelong). In addition, to ensure proper estimation of parameters over the life of an exposure, it is necessary to consider several options of future macroeconomic conditions and to estimate the expected future life of the exposure. Finally, in accordance with the standard, parameters will be calibrated using several scenarios, and the final impairment allowance will be estimated as a weighted average of expected losses in each scenario. The above changes cause a significant increase in the range of parameters used for the calculations. They also introduce new elements to the models of impairment parameters resulting from the use of calibration in several macroeconomic scenarios. In 2016, the Bank worked on preparation of the final methodological concept for the model parameters and on implementation of the new allowance calculation method, a process that will become much complex after IFRS 9 is adopted.

Status of implementation

As described above, the Bank is currently in process of business models identification and contractual cash flows analysis generated by individual portfolios of assets. Also works connected with impairment losses are in progress. In late 2016, the Bank has launched a phase relating to tax aspects, hedge accounting and disclosures required by the Standard.

Due to the ongoing process of IFRS 9 "Financial instruments" implementation and the lack of reliable impact estimation, the Bank has not disclosed quantitative implications of the IFRS 9 implementation.

in thousands of PLN

Standards and interpretations or changes to existing standards or interpretations which were applied for the first time in 2016

IFRS	Nature of changes	Effective from	Influence on Bank
IFRS 14 Regulatory Deferral Accounts	The standard permits an entity which is a first-time adopter of International Financial Reporting Standards to continue to recognize amounts related to rate regulation in accordance with their previous accounting rules. To improve the comparability with entities that have already adopted IFRS and do not recognise such amounts, in line with the published IFRS 14 amounts from the rate-regulated activities are presented separately in the statement of financial position and income statement and statement of other comprehensive income.	1 January 2016	The change had no significant effect on financial statement.
IAS 19 "Employee benefits"	Change in determining the discount rate - it is applicable to post-employment obligations, in the currency of the obligation rather than the country of origin of the obligation.	1 February 2016	The change had no significant effect on financial statement.
Annual improvements to IFRS cycle 2010-2012	Improvements concern: <ul style="list-style-type: none"> • IFRS 2 definition of "vesting condition"; • IFRS 3 Contingent consideration in a business combination; • IFRS 8 Aggregation of operating segments, reconciliation of the total of the reportable segments' assets to the entity's assets; • IFRS 13 Short-term receivables and payables; • IAS16/IAS 38 Update – proportionate method; • IAS 24 Key management personnel. 	1 February 2015	The change had no significant effect on financial statement.
Amendment to IAS 27 Equity method in separate financial statements	Change in accounting for investments in subsidiaries in an entity's separate financial statements. <ul style="list-style-type: none"> • At purchase price; • In line with IFRS 9; • In line with IAS 28 guidelines (ownership rights); Refinement of the definition of separate financial statements.	1 January 2016	The change had no significant effect on financial statement.
Annual improvements to IFRS cycle 2012-2014	Improvements relate to: <ul style="list-style-type: none"> • IFRS 5 Changes of disposal method; • IFRS 7 Servicing contracts; • IAS 19 Discount rate: regional market issue; • IAS 34 Disclosure of information "elsewhere in the interim financial report." 	1 January 2016	The change had no significant effect on financial statement.
Amendments to IFRS 11 Joint arrangements	During acquisition of an interest in a joint operation by an investor (in line with the IFRS3: "an investment") the requirement for the investor to apply the accounting rules for joint operations and to perform a number of actions: <ul style="list-style-type: none"> • to remeasure the identifiable assets and liabilities to fair value, • to relate the acquisition cost to the financial results, • to recognised deferred income tax, • to recognise residual value as goodwill. 	1 January 2016	The change had no significant effect on financial statement.
Amendment to IAS 16 and IAS 38	In line with the amendment to IAS 16, the method of depreciation of fixed tangible assets based on revenues under this measure is not considered to be appropriate. In line with the amendment to IAS 38, the method of amortization and depreciation of intangible assets based on revenues under this measure is not considered to be appropriate.	1 January 2016	The change had no significant effect on financial statement.
Amendments to IAS 1	The change regards the presentation of the financial statements, taking into consideration their materiality and disaggregation. The amendment introduces changes on drawing up notes to the financial statement, disclosing accounting principles and grouping of items presented in other comprehensive income from the investment.	1 January 2016	The Bank implemented Standard's provisions. Influence's description is disclosed in section "Comparability with results of previous periods"
Amendments to IFRS 10, IFRS 12 and IAS 28 Investment Entities: Applying the Consolidation	The amendments to IFRS 10, IFRS 12 and IAS 28 exempt to the requirement of presenting consolidated financial statements by an entity that is a parent if its ultimate or any intermediate parent produces financial statements that are available for public use and comply with IFRSs, in which subsidiaries are consolidated or are measured at fair value through profit or loss. Additionally, the requirement to consolidation was limited to the situation when an investment entity has a subsidiary that is not itself an investment entity and whose main purpose and activities are providing services that relate to the investment entity's investment activities. Moreover, when applying the equity method in an associate or joint venture that is an investment entity, an investor retain the fair value measurement applied by that investment entity associate or joint venture to the investment entity associate's or joint venture's interests in subsidiaries.	22 September 2016	The change had no significant effect on financial statement

in thousands of PLN

Accounting policies

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

Changes in accounting policies

No major changes were introduced in accounting policies.

Comparability with results of previous periods

Due to the entry into force of amendments to IAS 1, Bank Zachodni WBK decided to adjust the comparative data to provide more transparent information about its financial position.

Starting from 30.06.2016, Bank Zachodni WBK changed the presentation of buy-sell-back transactions and sell-buy-back transactions. They used to be disclosed under the following line items: Loans and advances to customers, Loans and advances to banks and Deposits from banks and Deposits from customers, respectively. Now, buy-sell-back transactions and sell-buy-back transactions are reported under separate line items of the statement of financial position.

Starting from 31.12.2016, Bank Zachodni WBK changed the presentation of provisions. They used to be disclosed under Other liabilities, now they are reported under a separate line item of the statement of financial position.

The tables below present the impact of changes in range of presentation for comparative data.

	31.12.2015 before conversion	Change in recognition of Buy-sell-back and Sell-buy-back transactions	31.12.2015 converted
Loans and advances to banks	4 756 502	(272 300)	4 484 202
Loans and advances to customers	81 142 310	(16 960)	81 125 350
Buy-sell-back transactions	-	289 260	289 260
Deposits from banks	3 935 893	(3 387 335)	548 558
Deposits from customers	94 641 472	(620 190)	94 021 282
Sell-buy-back transactions	-	4 007 525	4 007 525

	31.12.2015 before conversion	Change in recognition of provisions	31.12.2015 converted
Provisions	-	82 649	82 649
Other liabilities	1 340 712	(82 649)	1 258 063

The above changes are for presentation purposes only

The tax imposed under the act on tax on certain financial institutions that became effective on 1.02.2016 was disclosed in a separate item in the income statement as "Tax on financial institutions".

Basis of preparation

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

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

Use of estimates and judgments

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

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

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

in thousands of PLN

Main estimates and judgments made by the Bank

Loan impairment

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

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

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

The analysis of impairment is carried out:

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

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

Impairment loss on non-financial assets

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

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

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

Assets held for sale are measured at the lower of their carrying amount or estimated fair value less estimated costs to sell.

Fair value of financial instruments

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

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

Revenues arising from insurance mediation

In 2016, the Bank has changed estimation of the parameters of the relative-fair-value model. The model is applied by the Bank to allocate the amount of intermediation remuneration services arising from insurance sale offered in conjunction with a financial instrument between components: one-off recognised immediately in income statement on the time of origination, part of fee amortized as part of the loan and as provisions for reimbursement in proportion accordingly to fair value of financial instrument and fair value of intermediation services in relation to the sum of the two above amounts. Based on the parameters review, the following elements have been changed: a portion of remuneration arising from the offered financial instrument, remuneration for insurance mediation services and remuneration for additional activities carried out during the term of the insurance contract.

in thousands of PLN

Other accounting estimates and judgments

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

See Note 48 for details about provisions for staff benefits.

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

Provisions for legal claims have been estimated considering the expected loss arising on individual cases.

Changes in judgments and estimates

In 2016, the scope of data covered by estimates did not change in comparison with the unconsolidated financial statements of Bank Zachodni WBK for 2015 with the exception of those listed above.

Foreign currency

Foreign currency transactions

The functional and presentation currency of the Bank are the Polish zloty (PLN).

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

Financial assets and financial liabilities

Classification

The Bank classifies its financial instruments into the following categories:

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

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

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

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

Held-to-maturity investments

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

in thousands of PLN

Loans and receivables

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

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

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

Available-for-sale financial assets

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

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

Other financial liabilities

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

Recognition

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

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

Derecognition

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

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

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

Measurement

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

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

- (a) loans and receivables which shall be measured at amortised cost using the effective interest rate method;
- (b) held-to-maturity investments, which are measured at amortised cost using the effective interest rate;

in thousands of PLN

- (c) investments in equity instruments that do not have a quoted market price in an active market and whose fair value cannot be reliably measured.

The fair values of quoted financial instruments in active markets are based on current bid prices. If the market for a financial asset is not active (and for unlisted securities) the Bank establishes fair value by using valuation techniques which include recent arm's length market transactions, discounted cash flow analysis, option pricing models and other valuation techniques commonly used by market participants. Where a fair value cannot be reliably estimated, unquoted instruments that do not have a quoted market price in an active market are measured at cost and periodically reviewed for impairment.

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

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

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

Gains and losses on subsequent measurement

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

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

Offsetting financial instruments

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

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

Subsidiaries, associates and joint ventures

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

Repurchase and reverse repurchase transactions

The bank also generates/ invests funds by selling/purchasing financial instruments under repurchase/reverse repurchase agreements whereby the instruments must be repurchased/resold at the previously agreed price.

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

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

Derivative financial instruments

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

in thousands of PLN

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

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

Hedge accounting

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

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

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

The Bank discontinues hedge accounting when:

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

Fair value hedge

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

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

Cash flow hedge

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

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

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

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

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

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

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

in thousands of PLN

Impairment of financial assets

Assets carried at amortised cost – loans and receivables

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

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

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

The calculation of the present value of the estimated future cash flows of a collateralised financial asset reflects the cash flows that may result from foreclosure less costs in obtaining and selling the collateral, whether or not foreclosure is probable.

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

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

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

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

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

in thousands of PLN

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

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

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

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

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

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

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

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

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

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

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

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

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

The amount of the reversal is recognised in income statement.

in thousands of PLN

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

Available-for-sale financial assets

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

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

Contingent liabilities

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

Property, plant and equipment

Owned fixed assets

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

Leased assets

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

Subsequent expenditure

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

Depreciation

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

- | | |
|-----------------------|--------------|
| • buildings | 40 years |
| • structures | 22 years |
| • plant and equipment | 3 – 14 years |
| • vehicles | 4 years |

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

Fixed assets held for sale

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

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

in thousands of PLN

Goodwill and Intangible assets

Goodwill

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

Licences, patents, licences and similar assets

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

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

Other intangible assets

Other intangible assets that are acquired by the Bank are stated at cost less accumulated amortisation and impairment losses.

Expenditure on intangible assets

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

Amortisation

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

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

Other items of statement of financial position

Other trade and other receivables

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

Other liabilities

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

Equity

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

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

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

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

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

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

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

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

in thousands of PLN

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

Custody services

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

Capital payments (Dividends)

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

Employee benefits

Short-term employee benefits

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

Long-term employee benefits

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

Equity-settled share-based payment transactions

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

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

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

Cash-settled share-based payment transactions

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

Provisions

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

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

in thousands of PLN

Net interest income

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

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

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

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

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

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

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

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

Net commission income

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

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

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

Net income on bancassurance

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

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

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

The Bank verifies the accuracy of the assumed allocation of different types of income at least annually.

Net trading income and revaluation

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

in thousands of PLN

Dividend income

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

Profit on disposal of subsidiaries, associates and joint ventures

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

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

Other operating income and costs

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

Impairment losses on loans and advances

In line „Impairment losses on loans and advances” are presented loan receivables impairment losses and the result on loan receivables’ sale. The result on loan receivables’ sale is computed at the assets’ derecognition date in the difference between balance sheet amount and remuneration received.

Operating lease payments

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

Finance lease payments

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

Corporate income tax

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

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

Deferred tax assets and liabilities are provided, using the balance sheet method, on temporary differences between the tax bases of assets and liabilities and their values arising from the statement of financial position. Deferred income tax is determined using tax rates based on legislation enacted or substantively enacted at the end of the reporting period and expected to apply when the deferred tax asset is realised or the deferred tax liability is settled. Deferred tax assets are recognised at realizable amount – it is to the extent that it is probable that the Bank generates taxable profit allowing partial or wholly realisation of deferred tax assets.

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

3. Risk management

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

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

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

in thousands of PLN

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

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

Audit and Compliance Committee of the Supervisory Board supports the Supervisory Board in its supervisory activities. The Committee annually reviews the internal controls in financial reporting, accepts the reports from the independent internal audit unit and compliance units. The Committee receives the regular quarterly reports on the status of the implementation of audit recommendations as the basis of the assessment of the quality of management actions. The Audit Committee assesses the efficiency of the internal control system and the risk management system.

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

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

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

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

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

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

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

- **Credit Risk Panel;**
- **Market Risk Panel;**
- **Models and Methodology Panel;**
- **Equity Investment and Underwriting Panel;**

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

Provisions Committee decides on the amount of impairment losses on credit exposures and the legal provisions. The Committee approves the methodology and the parameters used for the calculation of impairment on a portfolio level for the Bank.

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

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

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

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

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

in thousands of PLN

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

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

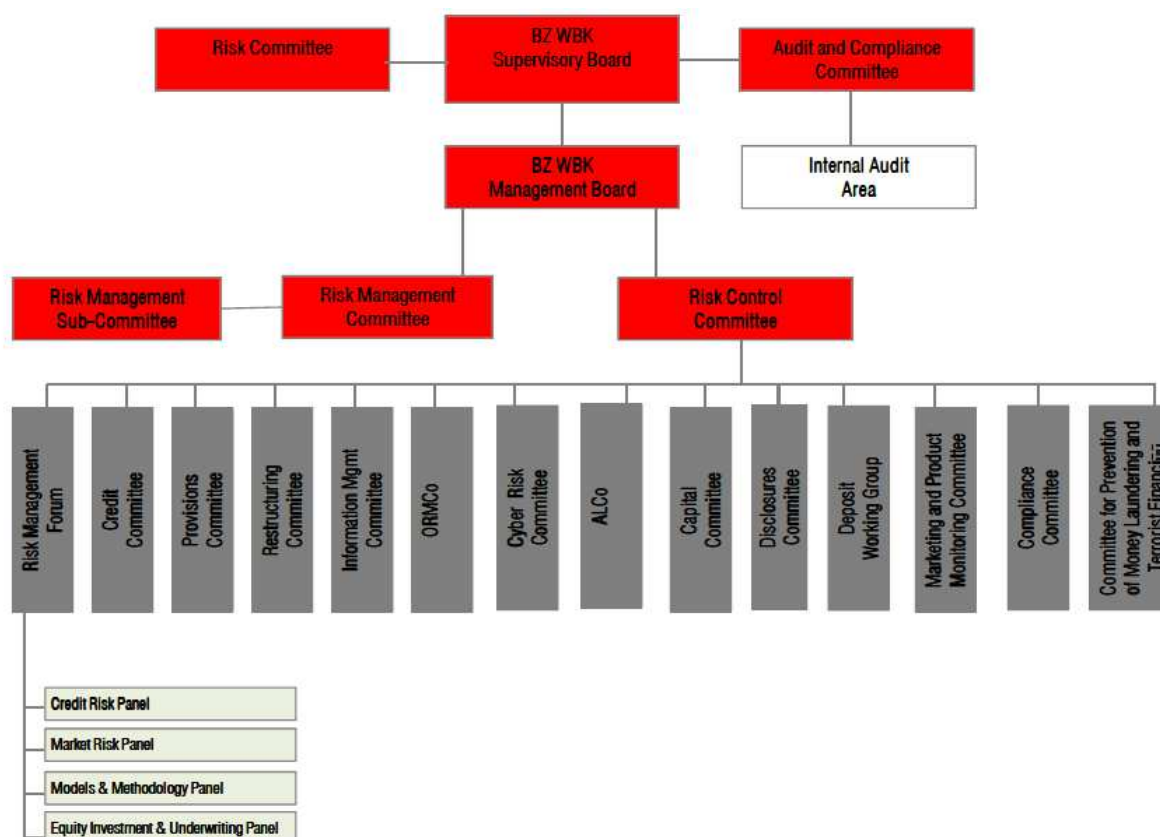
Product Marketing and Monitoring Committee approves new products and services to be implemented in the market, taking into account the reputation risk analysis.

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

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

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

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



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

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

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

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

in thousands of PLN

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

Credit risk

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

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

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

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

The Bank is closely looking at the macroeconomic environment and analysing its credit exposure to particular customer segments and economic sectors to respond with an adequate and prompt action and adjust its credit policy parameters accordingly. The year 2016 in this respect was fairly stable and the introduced changes only modified Bank's policy.

One of the Bank's priorities in 2016 was close monitoring of foreign currency housing loan portfolio. In response to the numerous legislative proposals Bank conducted multivariate analyzes and actively participated in the consultation processes. The Bank pays particular attention to credit risk on these portfolios and assesses them as low.

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

Risk Management Forum

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

Risk Management Division

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

Credit Policies

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

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

Credit Decision Making Process

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

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

in thousands of PLN

Credit Grading

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

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

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

Credit Reviews

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

Collateral

In the Bank's security model, the Collateral and Credit Agreements Department is the central unit responsible for creation and maintenance of collateral.

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

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

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

Retail customers

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

Business customers

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

in thousands of PLN

Collateral management process

Before a credit decision is approved, the Collateral and Credit Agreements Department assesses the collateral quality, a process that includes:

- verification of the valuation reports – assessment of the security value;
- assessment of the legal status of the security;
- assessment of the investment process for the properties;
- seeking legal advice on the securities offered.

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

- drafting credit documentation;
- verification and assessment of the signed credit documentation;
- verification of data in the IT systems;
- collateral monitoring and reporting;
- releasing the collateral.

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

Credit risk stress testing

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

Calculation of impairment

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

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

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

in thousands of PLN

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

31.12.2016	Provision cover	Loans and advances to customers	Loans and advances to banks	Available for sale- debt securities	Financial assets held for trading*
Impaired portfolio					
Individually impaired					
	up to 50%	1 500 928	-	-	-
	50% - 70%	270 519	-	-	-
	70% - 85%	259 884	-	-	-
	over 85%	470 047	-	-	-
Gross amount		2 501 378	-	-	-
Impairment		(1 196 414)	-	-	-
Net amount		1 304 964	-	-	-
Collectively impaired					
	up to 50%	1 271 446	-	-	-
	50% - 70%	574 080	-	-	-
	70% - 85%	549 588	-	-	-
	over 85%	488 484	-	-	-
Gross amount		2 883 598	-	-	-
Impairment		(1 544 447)	-	-	-
Net amount		1 339 151	-	-	-
IBNR portfolio					
	up to 0,10%	55 018 192	3 308 802	25 467 070	3 189 152
	0,10% - 0,30%	15 178 908	-	-	-
	0,30% - 0,65%	7 853 208	-	-	-
	over 0,65%	6 447 565	-	-	-
Gross amount		84 497 873	3 308 802	25 467 070	3 189 152
IBNR		(341 566)	-	-	-
Net amount		84 156 307	3 308 802	25 467 070	3 189 152
Other receivables		301 968	-	-	-
Off-balance sheet exposures					
Financing granted		21 445 091	-	-	-
Guarantees		4 248 934	-	-	-
Nominal value of derivatives - purchased		-	-	-	233 442 959
Allowance for off-balance sheet exposures		(28 706)	-	-	-
Off-balance sheet exposures - total		25 665 319	-	-	233 442 959

*the value of financial assets held for trading includes adjustment of the fair value as described in Note 19

in thousands of PLN

31.12.2015	Provision cover	Loans and advances to customers	Loans and advances to banks	Available for sale- debt securities	Financial assets held for trading*
Impaired portfolio					
Individually impaired					
	up to 50%	1 815 677	-	-	-
	50% - 70%	556 773	-	-	-
	70% - 85%	203 814	-	-	-
	over 85%	623 506	-	-	-
Gross amount		3 199 770	-	-	-
Impairment		(1 424 661)	-	-	-
Net amount		1 775 109	-	-	-
Collectively impaired					
	up to 50%	748 789	-	-	-
	50% - 70%	496 116	-	-	-
	70% - 85%	554 485	-	-	-
	over 85%	687 035	-	-	-
Gross amount		2 486 425	-	-	-
Impairment		(1 659 504)	-	-	-
Net amount		826 921	-	-	-
IBNR portfolio					
	up to 0,10%	42 125 337	4 484 203	21 471 774	4 149 710
	0,10% - 0,30%	21 369 336	-	-	-
	0,30% - 0,65%	8 439 085	-	-	-
	over 0,65%	6 817 449	-	-	-
Gross amount		78 751 207	4 484 203	21 471 774	4 149 710
IBNR		(340 429)	(1)	-	-
Net amount		78 410 778	4 484 202	21 471 774	4 149 710
Other receivables					
		112 542	-	-	-
Off-balance sheet exposures					
Financing granted		20 863 916	-	-	-
Guarantees		4 488 628	-	-	-
Nominal value of derivatives - purchased		-	-	-	202 173 420
Allowance for off-balance sheet exposures		(55 276)	-	-	-
Off-balance sheet exposures - total		25 297 268	-	-	202 173 420

*the value of financial assets held for trading includes adjustment of the fair value as described in Note 19

IBNR portfolio

	Loans and advances to customers	
	31.12.2016	31.12.2015
Non-past due	80 792 439	76 104 329
Past-due	3 705 434	2 646 878
1-30 days	3 069 721	2 085 816
31-60 days	437 594	388 363
61-90 days	186 593	159 739
> 90 days	11 526	12 960
Gross amount	84 497 873	78 751 207

in thousands of PLN

	IBNR	
	31.12.2016	31.12.2015
Loans and advances to enterprises	151 480	148 344
Loans and advances to individuals	189 982	191 870
Loans and advances to public sector	104	215
	341 566	340 429

Allowances for impairment by classes

Provision cover	Loans and advances to customers		Loans and advances to banks	
	31.12.2016	31.12.2015	31.12.2016	31.12.2015
Individual allowance for impairment				
up to 50%	(384 215)	(351 186)	-	-
50% - 70%	(156 840)	(334 924)	-	-
70% - 85%	(194 368)	(149 758)	-	-
over 85%	(460 991)	(588 793)	-	-
Total individual allowance for impairment	(1 196 414)	(1 424 661)	-	-
Collective allowance for impairment				
up to 50%	(248 359)	(261 893)	-	-
50% - 70%	(388 687)	(303 493)	-	-
70% - 85%	(429 886)	(433 774)	-	-
over 85%	(477 515)	(660 344)	-	-
Total collective allowance for impairment	(1 544 447)	(1 659 504)	-	-
IBNR				
up to 0,10%	(17 554)	(11 899)	-	(1)
0,10%-0,30%	(22 817)	(40 699)	-	-
0,30%-0,65%	(38 273)	(40 347)	-	-
over 0,65%	(262 922)	(247 484)	-	-
Total IBNR	(341 566)	(340 429)	-	(1)
Total allowance for impairment	(3 082 427)	(3 424 594)	-	(1)

Credit risk concentration

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

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

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

As at 31.12.2015, pursuant to art. 71 of the Banking Law Act, the maximum limits for the bank totalled:

- PLN 3,510,684 k (25% of Bank's own funds).

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

The analysis of the Bank's exposures in terms of sector concentrations proved that the Bank does not have any exposures in excess of the limits imposed by the regulator in 2016.

in thousands of PLN

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

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

A list of the 20 largest borrowers (or group of capital-related borrowers) of Bank Zachodni WBK (performing loans) as at 31.12.2015.

Industry code (PKD)	Industry description	Total credit exposure	Balance sheet exposure	Committed credit lines, guarantees, treasury limits and capital investments
64	OTHER FINANCIAL SERVICES	4 103 499	999 599	3 103 900
64	OTHER FINANCIAL SERVICES	3 719 204	3 238 626	480 578
64	OTHER FINANCIAL SERVICES	2 860 000	2 774 551	85 449
64	OTHER FINANCIAL SERVICES	2 224 574	1 341 986	882 588
61	TELECOMMUNICATION	1 419 999	1 129 054	290 945
06	MINING	1 250 988	72 206	1 178 782
35	POWER INDUSTRY	968 984	183 984	785 000
19	RAFINERY	761 910	404 167	357 743
07	MINING	757 601	140 436	617 165
19	RAFINERY	656 709	174 858	481 851
35	POWER INDUSTRY	560 329	507 363	52 966
35	POWER INDUSTRY	529 168	480 168	49 000
41	CONSTRUCTION	429 001	1	429 000
20	CHEMICAL INDUSTRY	410 000	143 389	266 611
68	REAL ESTATE SERVICES	407 369	285 831	121 538
61	TELECOMMUNICATION	403 409	-	403 409
33	MACHINE INDUSTRY	399 986	42 601	357 385
68	REAL ESTATE SERVICES	389 978	224 679	165 299
68	REAL ESTATE SERVICES	387 244	385 235	2 009
68	REAL ESTATE SERVICES	379 217	379 217	-
Total gross exposure		23 019 169	12 907 951	10 111 218

in thousands of PLN

Industry concentration

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

As at 31.12.2016, the highest concentration level was recorded in the “distribution” sector (11% of the Bank Zachodni WBK exposure), “financial sector” (10%) and “property” (10%).

Groups of PKD by industries:

Industry	Gross exposure		
	31.12.2016	31.12.2015	
Distribution	10 068 097	9 309 131	
Financial sector	8 840 305	9 095 528	
Property	8 594 381	9 646 258	
Manufacturing	8 001 053	8 362 864	
Energy	2 224 262	1 633 540	
Transportation	1 199 147	1 186 794	
Agriculture	1 061 495	1 089 473	
Construction	899 540	870 331	
Other industries	5 706 034	4 408 734	
A	Total Business Loans	46 594 314	45 602 653
B	Retail (including mortgage loans)	43 288 535	38 834 749
A+B	BZ WBK portfolio	89 882 849	84 437 402
C	Other receivables (commercial bonds)	301 968	112 542
A+B+C	Total BZ WBK	90 184 817	84 549 944

Forbearance Policy

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

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

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

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

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

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

in thousands of PLN

		Book value	
		31.12.2016	31.12.2015
Loans and advances to customers- gross amount			
under forbearance measure:		3 620 780	3 916 577
	corporate exposures	2 554 629	3 050 425
	mortgage exposures	936 319	779 432
	individuals exposures	129 832	86 720
Allowance for impairment - forbearance clients		(733 395)	(1 128 786)
	of which: individually impaired	(502 349)	(929 512)
Loans and advances to forbearance clients- net amount		2 887 385	2 787 791

Analysis of credit quality of financial assets subject to forbearance:

Loans and advances to customers under forbearance	Gross exposure		Collateral value		Allowance for impairment	
	31.12.2016	31.12.2015	31.12.2016	31.12.2015	31.12.2016	31.12.2015
Loans and advances -impaired	1 889 974	2 647 104	6 692 669	4 338 467	(679 872)	(1 087 399)
Loans and advances -unimpaired	1 730 806	1 269 473	5 073 632	3 131 955	(53 523)	(41 387)
non-overdue	1 053 988	988 021	2 667 597	2 177 952	(32 380)	(29 774)
from 1 to 30 days overdue	567 030	204 106	2 203 805	782 207	(17 253)	(8 111)
from 31 to 60 days overdue	74 744	57 216	91 641	143 369	(2 324)	(2 798)
from 61 to 90 days overdue	35 044	20 130	110 589	28 427	(1 566)	(704)
Total gross amount	3 620 780	3 916 577	11 766 301	7 470 422	(733 395)	(1 128 786)

Interest income on assets subject to forbearance was PLN 96,331 k as at 31.12.2016 and PLN 107,202 k as at 31.12.2015.

Loans and advances to customers under forbearance by geographical region (gross amount)	31.12.2016	31.12.2015
Dolnośląskie	298 385	258 702
Kujawsko-Pomorskie	43 725	43 945
Lubelskie	27 591	27 198
Lubuskie	38 656	43 560
Mazowieckie	1 871 206	1 814 027
Małopolskie	92 461	279 646
Opolskie	20 615	18 249
Podkarpackie	21 312	15 890
Podlaskie	30 312	18 320
Pomorskie	163 983	124 562
Warmińsko-Mazurskie	25 760	26 328
Wielkopolskie	155 547	259 228
Zachodniopomorskie	55 622	56 832
Śląskie	520 326	575 507
Świętokrzyskie	188 408	268 602
Łódzkie	66 871	85 981
Total	3 620 780	3 916 577

in thousands of PLN

Loans and advances to customers under forbearance by industry (gross amount)	31.12.2016	31.12.2015
Construction	274 516	364 526
Distribution	74 408	265 767
Energy	399 368	588 969
Financial sector	341	5 418
Other industries	176 376	564 151
Property	1 360 369	912 205
Manufacturing	227 267	303 185
Agriculture	8 410	8 409
Transportation	33 574	37 795
Individuals	1 066 151	866 152
Total	3 620 780	3 916 577

	31.12.2016	31.12.2015
Net carrying amount as at 31.12.2015	2 787 791	2 586 574
Allowance for impairment	395 391	(28 662)
Loans and advances derecognised during the period	(758 110)	(33 356)
Loans and advances recognised during the period	1 260 732	1 301 381
Other changes/repayments	(798 419)	(1 038 146)
Net carrying amount as at 31.12.2016	2 887 385	2 787 791

Market risk

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

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

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

General principles of market risk management

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

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

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

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

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

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

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

in thousands of PLN

Assessment methods

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

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

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

Interest rate risk in the banking book

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

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

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

The sensitivity measures for 2016 and 2015 are presented in the table below.

1 day holding period	NII Sensitivity		MVE Sensitivity	
	31.12.2016	31.12.2015	31.12.2016	31.12.2015
Maximum	218	118	250	215
Average	184	97	198	186
as at the end of the period	218	116	218	215
Limit	280	170	340	220

In 2016, the global NII and MVE limits for the banking book were not exceeded.

Interest rate risk in the trading book

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

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

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

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

in thousands of PLN

The table below shows risk measures at the end of 2016 and 2015 for 1-day position holding period.

Interest rate risk 1 day holding period	VAR	
	31.12.2016	31.12.2015
Average	1 706	1 643
Maximum	3 681	5 534
Minimum	659	375
as at the end of the period	1 509	837
Limit	7 523	5 852

In 2016, the VAR limit for interest rate risk has not been exceeded.

FX risk

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

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

The table below illustrates the risk measures at the end of December 2016 and 2015.

FX risk 1 day holding period	VAR	
	31.12.2016	31.12.2015
Average	393	636
Maximum	3 096	3 411
Minimum	30	52
as at the end of the period	319	846
Limit	3 134	1 951

In 2016, the VAR limit for fx risk has not been exceeded.

FX Balance Sheet

In 2016, the share of assets in foreign currencies in the bank's balance sheet decreased compared to the level observed in 2015. A slight decrease fall in amounts receivable in EUR and in amounts receivable in CHF were observed as a result of continued amortisation of mortgage loans.

As a result of increased funding from the wholesale market, the mismatch between EUR assets and liabilities became less pronounced. The resulting funding gap was closed by entering into a swap transaction in the FX market.

in thousands of PLN

The tables below show the Bank's main FX items – as at 31.12.2016 and 31.12.2015.

31.12.2016	PLN	EUR	CHF	USD	Other	Total
ASSETS						
Cash and balances with central banks	4 341 719	221 874	18 083	48 073	66 885	4 696 634
Loans and advances to banks	323 153	2 656 552	23 120	207 867	98 110	3 308 802
Loans and advances to customers	59 372 866	16 392 857	10 509 567	675 502	151 598	87 102 390
Investment securities	24 887 081	995 504	-	439 776	-	26 322 361
Selected assets	88 924 819	20 266 787	10 550 770	1 371 218	316 593	121 430 187
LIABILITIES						
Deposits from banks	366 840	790 952	23 652	30 357	964	1 212 765
Deposits from customers	87 041 211	12 207 824	288 917	2 947 761	895 536	103 381 249
Subordinated liabilities	-	440 457	-	-	-	440 457
Selected liabilities	87 408 051	13 439 233	312 569	2 978 118	896 500	105 034 471

31.12.2015	PLN	EUR	CHF	USD	Other	Total
ASSETS						
Cash and balances with central banks	5 800 253	202 996	16 367	64 028	45 899	6 129 543
Loans and advances to banks	463 992	2 848 811	804 658	170 653	196 088	4 484 202
Loans and advances to customers	52 577 302	16 628 470	10 827 800	921 084	170 694	81 125 350
Financial assets available for sale	21 349 674	1 017 716	-	208 856	-	22 576 246
Selected assets	80 191 221	20 697 993	11 648 825	1 364 621	412 681	114 315 341
LIABILITIES						
Deposits from banks	179 047	170 212	730	197 489	1 080	548 558
Deposits from customers	80 840 335	9 451 537	676 231	2 444 533	608 646	94 021 282
Subordinated liabilities	-	426 507	-	-	-	426 507
Selected liabilities	81 019 382	10 048 256	676 961	2 642 022	609 726	94 996 347

Equity investment risk

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

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

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

The table below presents the risk measures in 2016 and 2015:

Equity risk	VAR Brokerage Office	
	31.12.2016	31.12.2015
1 day holding period		
Average	301	429
Maximum	742	1 057
Minimum	50	90
as at end of the period	77	230
Limit	4 346	4 057

In 2016, the VAR limit for equity risk has not been exceeded.

Liquidity risk

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

Liquidity Risk Management

The BZ WBK Liquidity Management Policy is designed to:

- ensure the ability to finance assets and satisfy claims, both current and future, in a timely manner and at an economic price;
- manage the maturity mismatch between assets and liabilities;
- set a scale of the liquidity risk in the form of various internal limits;

in thousands of PLN

- ensure proper organization of the liquidity management process in Bank Zachodni WBK;
- prepare the organization for emergence of adverse factors, either external or internal;
- ensure compliance with regulatory requirements, both qualitative and quantitative.

The general principle adopted by the Bank in its liquidity management process is that all expected outflows occurring within 1 month in respect of deposits, current funds, loan drawdowns, guarantee payments and transaction settlements should be at least fully covered by the anticipated inflows or Qualified Liquid Assets (QLA) assuming normal or predictable conditions for the Bank's operations. The QLA category includes: cash on hand, cash deposited with NBP (National Bank of Poland), securities which may be sold or pledged under repo transactions or NBP lombard loans.

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

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

As at 31 December 2016, LCR ratio was at 144.6% and NSFR ratio was at 115.0%.

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

Management Process

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

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

Risk Measurement and Reporting

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

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

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

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

Concurrently, liquidity is measured in accordance with KNF Resolution no. 386/2008 on setting liquidity standards for banks, and with the requirements laid down in CRD IV / CRR.

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

Stress tests and the contingency plan

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

in thousands of PLN

- Baseline scenario, which assumes non-renewability of wholesale funding;
- Idiosyncratic liquidity crisis scenarios (specific to the bank);
- Local systemic liquidity crisis scenario;
- Global systemic liquidity crisis scenario;
- Combined liquidity crisis scenario (idiosyncratic crisis and local systemic crisis);
- Deposit outflows in a one-month horizon.

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

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

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

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

In 2016, as in 2015, the Bank focused on keeping its loan-to-deposit ratio at a comfortable level (which totaled 84% as at 31 December 2016) and controlling key short- and long-term liquidity measures.

In 2016 and in the comparable period, all key supervisory measures applicable to the Bank were maintained at the required levels.

Economic liquidity gap analysis as at 31.12.2016 and in comparable period:

31.12.2016	A'vista	up to 1 month	from 1 to 3	from 3 to 6	from 6 to 12	from 1 to 2 years	from 2 to 5 years	over 5 years
Economic liquidity gap	12 681 182	6 267 741	(8 945 412)	(4 763 837)	931 488	3 890 399	3 959 170	(14 020 732)
Cumulative economic liquidity gap	12 681 182	18 948 923	10 003 511	5 239 674	6 171 162	10 061 561	14 020 731	(1)

31.12.2015	A'vista	up to 1 month	from 1 to 3	from 3 to 6	from 6 to 12	from 1 to 2 years	from 2 to 5 years	over 5 years
Economic liquidity gap	15 325 329	(1 489 742)	(9 045 449)	(4 486 001)	2 506 687	4 401 822	4 172 754	(11 385 400)
Cumulative economic liquidity gap	15 325 329	13 835 587	4 790 138	304 137	2 810 824	7 212 646	11 385 400	-

Liquidity Policy Report – Modified Liquidity Gap:

Liquidity risk	<1W	<1M	>1M
31.12.2016			
Qualifying Liquid Assets	25 208 949	185 000	5 749 534
Treasury inflows	3 544 628	2 926	-
Other inflows	10 556 297	7 260 699	147 026 492
Treasury outflows	(638 164)	(27 000)	(178 662)
Other outflows	(11 433 127)	(16 161 516)	(166 408 418)
GAP	27 238 583	(8 739 891)	(13 811 054)
Cumulative GAP	27 238 583	18 498 692	4 687 638

Liquidity risk	<1W	<1M	>1M
31.12.2015			
Qualifying Liquid Assets	21 728 281	441 227	6 124 214
Treasury inflows	3 663 745	-	942 880
Other inflows	10 904 761	7 270 239	142 518 779
Treasury outflows	(3 954 473)	(473 625)	(629 791)
Other outflows	(11 001 957)	(15 145 062)	(157 330 479)
GAP	21 340 357	(7 907 221)	(8 374 397)
Cumulative GAP	21 340 357	13 433 136	5 058 739

Operating Risk

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

in thousands of PLN

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

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

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

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

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

Bank Zachodni WBK uses the following tools:

- Identification and estimation of operational risk

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

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

- Reporting on operational incidents and lessons learned

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

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

- Analysis of risk indicators

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

- Business continuity management (BCM)

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

- Insurance

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

in thousands of PLN

- Regular reporting to the Risk Management Committee and Supervisory Board

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

The Bank's Information Security Management System has a certificate of compliance with ISO 27001:2005 standard.

Legal and Compliance Risk

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

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

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

In Bank Zachodni WBK, individual processes for the legal and compliance risk are managed by relevant units.

Responsibilities of the Legal and Compliance Division relate to the "conduct of business" compliance obligations, in particular with regard to: protection of consumer rights, implementation and sale of new products, prevention of money laundering, ethical issues, protection of sensitive information and protection of personal data, conflict of interests management.

The identification, interpretation and communication roles relating to other legal and regulatory obligations for the bank as a legal entity (non-conduct of business) have been assigned to functions with specialist knowledge in those areas:

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

The bank's Management Board adopted a policy statement on compliance with legal and regulatory obligations, which was approved by the Supervisory Board. The policy provides the Compliance Area operating within the Legal and Compliance Division, with the relevant mandate to support senior managers in effective management of the compliance risk. The Compliance Area escalates all issues to the Risk Management Committee and Audit and Compliance Committee of the Supervisory Board which ensure the fulfilment of regulatory obligations and approve the internal control principles and compliance policy framework, so that the Compliance Area may operate independently from business units and has relevant resources to perform its tasks.

The Audit and Compliance Committee regularly reviews key compliance issues identified by the Compliance Area and Anti-Money Laundering Department:

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

in thousands of PLN

The major responsibilities of the Compliance Area and Anti-Money Laundering Department include: prevention of legal and compliance risk, maintenance of appropriate relations with business units and market regulators, providing support to the Bank management in the strategic decision-making process regarding compliance, coordination (under the applicable laws) of the implementation of compliance management standards by compliance units operating in the Bank. These tasks are delivered through:

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

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

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

Reputation Risk Management

Reputation risk is defined as the risk arising from negative perception of the Bank by customers, counterparties, shareholders or investors.

The potential sources of the risk are internal and external operational incidents, such as adverse publicity, dissemination of negative feedback from customers e.g. on the Internet, in social media and other mass media. They may refer directly to the Bank and its products as well as the Bank's shareholders and the entire banking and financial sectors (domestic and international ones).

The elements of the reputation risk include customer complaints and claims related to the process of offering banking products, including complaints about sufficient (i.e. complete, true, reliable and non-misleading) information about products and related risks, complexity of products, improper sales practices or loss of capital.

The owner of the reputation risk is the Corporate Communication and Marketing Area (CC&MA) and Compliance Area (CA).

The objective of the reputation risk management process is to protect the image of Bank Zachodni WBK and to limit and eliminate negative events which affect the image and financial results of the Bank.

Key risk mitigation measures:

- BZ WBK Information Policy;
- Daily, constant monitoring of local, nationwide and certain international mass media sources (Corporate Communication and Marketing Area);

in thousands of PLN

- Daily monitoring of social media sources (in particular: Facebook, Twitter) in the context of references to BZ WBK (Corporate Communication and Marketing Area);
- Collection and analysis of image-sensitive information by the Press Office (Corporate Communication and Marketing Area);
- Response to information which poses a threat to public perception of the Bank's image (Corporate Communication and Marketing Area);
- Keeping the representatives of nationwide and local media up to date about new products and changes to the regulations regarding the existing products;
- Customer satisfaction index (Corporate Communication and Marketing Area);
- Preparation and control by relevant Bank Zachodni WBK units of all important communiqués and reports for the shareholders, the Polish Financial Supervision Authority (KNF) and the Warsaw Stock Exchange and timely publication of such communiqués and reports;
- Evaluation of new products or their modifications, procedures, commercial materials, processes and other bank initiatives (promotions, contests), training materials for sales staff - in respect of their compliance with the regulations and the regulatory guidelines (Compliance Area);
- Participation in the process of handling customer complaints, especially those addressed to the regulators (Compliance Area);
- Supervision of the after-sales control of investment products (Compliance Area);
- Mystery shopping surveys for investment products (Compliance Area);
- Regular monitoring of the reputation risk associated with the products offered by Bank Zachodni WBK through the analysis of customer complaints, sales volumes, number of customers and rate of return (Compliance Area).

4. Capital Management

Introduction

It is the policy of the Bank Zachodni WBK to maintain the level of capital adequate to the type and scale of operations and the level of risk. The level of own funds required to ensure safe operations of Bank Zachodni WBK and capital requirements estimated for the unexpected loss is determined in accordance with the CRD IV / CRR package implemented on 01.01.2014 by the European Parliament and European Banking Authority (EBA), plus KNF recommendations regarding national options.

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

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

Pursuant to the bank's information strategy, details about the level of own funds and capital requirements are presented in the annual report entitled "Information on capital adequacy of the bank and BZ WBK Group as at 31.12.2016".

In 2016, Bank Zachodni WBK met all regulatory requirements regarding capital management.

Capital Policy

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

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

As at 31.12.2016, the minimum capital ratios of the Bank satisfying the regulatory recommendations and additional own fund requirements under Pillar 2 were as follows:

in thousands of PLN

- a Tier 1 capital ratio of 11.22%;
- a total capital ratio of Bank Zachodni WBK of 14.37%;

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

Pursuant to the KNF decision of 14.10.2016, Bank Zachodni WBK maintain own funds at the level sufficient to cover an additional capital requirement for risk attaching to foreign currency home mortgages (0.62 p.p. above the total capital ratio). The capital buffer should be composed of at least 75% of the Tier 1 capital (which corresponds to the capital requirement of 0.47 p.p. above the Tier 1 capital ratio) and at least 56% of the Common Equity Tier 1 capital (which corresponds to the capital requirement of 0.35 p.p. above the Common Equity Tier 1 capital).

The Act of 5.08.2015 on macroprudential oversight of the financial system and crisis management in the financial sector transposes CRD IV into the Polish law with regard to, among other things, additional capital buffers to be maintained by banks. As of 01.01.2016, the minimum capital ratios for the banking sector in Poland will be increased by 1.25 p.p. due to introduction of a conservation buffer.

On 4.10.2016, KNF identified Bank Zachodni WBK as other systemically important institution and imposed an additional capital buffer of 0.5 p.p.

Regulatory Capital

The capital requirement for Bank Zachodni WBK Group is determined in accordance with Part 3 of Regulation (EU) no. 575/2013 of the European Parliament and of the Council of 26.06.2013 on prudential requirements for credit institutions and investment firms and amending Regulation (EU) no. 648/2012 (CRR), which formed a legal basis as at 31.12.2016.

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

The tables below show capital requirement for the Bank as of 31.12.2016 and 31.12.2015.

	31.12.2016	31.12.2015
I Total Capital requirement (Ia + Ib + Ic + Id), of which:	7 068 621	7 108 755
Ia - due to credit risk & counterparty credit risk	6 183 425	6 086 323
Ib - due to market risk	103 644	162 249
Ic - due to credit valuation adjustment risk	41 192	118 860
Id - due to operational risk	740 360	741 323
II Total own funds*	18 078 713	17 869 121
III Reductions	3 481 785	3 826 387
IV Own funds after reductions (II-III)	14 596 928	14 042 734
V CAD [IV/(I*12.5)]	16,52%	15,80%
VI Tier I ratio	16,08%	15,40%

* On 30.09.2016, the bank included current year profit of PLN 688,513k for the period between 1.01.2016 and 30.06.2016 to own funds as permitted by KNF.

Internal Capital

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

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

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

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

in thousands of PLN

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

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

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

Subordinated liabilities

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

Furthermore, on 2.12.2016, the bank issued EUR 120m worth of bonds as part of the strategy aimed at increasing the Tier 2 capital. On 5.12.2016, the bank requested a consent from KNF to allocate the above bonds to the Tier 2 capital.

Detailed information on subordinated liabilities is presented in Note 32.

5. Net interest income

	01.01.2016- 31.12.2016	01.01.2015- 31.12.2015
Interest income		
Loans and advances to enterprises	1 607 575	1 535 361
Loans and advances to individuals, of which:	1 922 895	1 733 407
<i>Home mortgage loans</i>	842 497	735 011
Debt securities incl.:	576 044	596 287
<i>Investment portfolio available for sale</i>	543 738	563 946
<i>Trading portfolio</i>	32 306	32 341
Loans and advances to banks	63 020	75 340
Public sector	6 881	7 817
Reverse repo transactions	9 149	9 578
Interest recorded on hedging IRS	284 353	285 978
Total	4 469 917	4 243 768
	01.01.2016- 31.12.2016	01.01.2015- 31.12.2015
Interest expenses		
Deposits from individuals	(495 924)	(587 815)
Deposits from enterprises	(337 316)	(328 565)
Repo transactions	(30 571)	(45 070)
Deposits from public sector	(41 627)	(56 171)
Deposits from banks	(18 999)	(10 104)
Subordinated liabilities and issue of securities	(65 040)	(81 191)
Total	(989 477)	(1 108 916)
Net interest income	3 480 440	3 134 852

As at 31.12.2016 net interest income includes interest on impaired loans of PLN 192,462 k (as at 31.12.2015 - PLN 245,206 k).

in thousands of PLN

6. Net fee and commission income

	01.01.2016- 31.12.2016	01.01.2015- 31.12.2015
Fee and commission income		
eBusiness & payments	579 525	542 171
Current accounts and money transfer	329 318	329 161
Asset management fees	4 268	6 454
Foreign exchange commissions	320 003	312 906
Credit commissions	205 485	219 939
Insurance commissions	93 301	123 032
Brokerage activities	71 627	71 347
Credit cards	85 036	82 199
Off-balance sheet guarantee commissions	65 579	42 732
Issue arrangement fees	15 212	15 028
Distribution fees	129 582	132 210
Other commissions	5 170	10 665
Total	1 904 106	1 887 844
Fee and commission expenses		
eBusiness & payments	(201 328)	(173 807)
Credit cards	(17 868)	(20 393)
Brokerage activities	(10 368)	(11 579)
Finance lease commissions	(66)	(127)
Commissions paid to credit agents	(12 471)	(20 088)
Insurance commissions	(8 280)	(8 876)
Other	(48 990)	(39 730)
Total	(299 371)	(274 600)
Net fee and commission income	1 604 735	1 613 244

Included above is fee and commission income on credits, credit cards and off-balance sheet guarantee commissions of PLN 356,100 k (2015: PLN 344,870 k) and fee and commission expenses on credits cards and paid to credit agents of PLN (30,339) k (2015: PLN (40,481) k) (other than fees included in determining the effective interest rate), relating to financial assets and liabilities not carried at fair value through profit or loss.

7. Dividend income

	01.01.2016- 31.12.2016	01.01.2015- 31.12.2015
Dividend income		
Dividends from subsidiaries and associates	343 770	51 680
Dividends from equity financial assets available for sale	94 987	103 306
Dividends income from equity financial assets at fair value through profit or loss	531	1 379
Total	439 288	156 365

in thousands of PLN

8. Net trading income and revaluation

	01.01.2016- 31.12.2016	01.01.2015- 31.12.2015
Net trading income and revaluation		
Derivative instruments and interbank fx transactions	248 025	204 662
Other FX related income	12 176	15 648
Profit on equity instruments	(1 710)	(10 273)
Profit on debt instruments	7 880	(16 542)
Total	266 371	193 495

Net trading income and revaluation includes the change of the value of derivative instruments in the amount of PLN (5,952) k for 2016 and the write-back of change in the amount of PLN 7,057 k for 2015. The amounts included CVA and DVA adjustments which in 2016 and 2015 totaled PLN (2 748) k and PLN 6 584 k respectively.

9. Gains (losses) from other financial securities

	01.01.2016- 31.12.2016	01.01.2015- 31.12.2015
Gains (losses) from other financial securities		
Profit on sale of equity shares available for sale	307 666	2 215
Profit on sale of debt securities available for sale	92 772	276 368
Charge due to impairment losses	(1 408)	(323)
Total profit (losses) on financial instruments	399 030	278 260
Change in fair value of hedging instruments	57 503	46 294
Change in fair value of underlying hedged positions	(55 344)	(50 837)
Total profit (losses) on hedging and hedged instruments	2 159	(4 543)
Total	401 189	273 717

10. Other operating income

	01.01.2016- 31.12.2016	01.01.2015- 31.12.2015
Other operating income		
Income on sale of services	19 428	17 183
Insurance indemnity received	2 210	1 305
Reimbursements of BGF charges	54 215	39 683
Release of provision for legal cases and other assets	12 788	21 831
Settlements of leasing agreements	2 907	1 341
Recovery of other receivables	6 876	5 758
Profit on sales or liquidation of fixed assets, intangible assets and assets for disposal	7 026	18 515
Received compensations, penalties and fines	1 047	474
Other	12 968	13 559
Total	119 465	119 649

in thousands of PLN

11. Impairment losses on loans and advances

	01.01.2016- 31.12.2016	01.01.2015- 31.12.2015
Impairment losses on loans and advances		
Collective and individual impairment charge	(609 608)	(694 394)
Incurred but not reported losses charge	(143)	6 103
Recoveries of loans previously written off	(1 133)	4 370
Off-balance sheet credit related facilities	27 405	16 026
Total	(583 479)	(667 895)

12. Employee costs

	01.01.2016- 31.12.2016	01.01.2015- 31.12.2015
Employee costs		
Salaries and bonuses	(1 010 647)	(1 032 141)
Salary related costs	(165 456)	(173 051)
Staff benefits costs	(28 431)	(30 055)
Professional trainings	(15 163)	(16 428)
Retirement fund, holiday provisions and other employee costs	(1 073)	(3 646)
Total	(1 220 770)	(1 255 321)

13. General and administrative expenses

	01.01.2016- 31.12.2016	01.01.2015- 31.12.2015
General and administrative expenses		
Maintenance and rentals of premises	(299 118)	(320 683)
Marketing and representation	(86 624)	(117 758)
IT systems costs	(148 335)	(145 509)
Bank Guarantee Fund, Polish Financial Supervision Authority and National Depository for Securities	(246 326)	(408 150)
Postal and telecommunication costs	(32 642)	(37 534)
Consulting fees	(46 943)	(32 738)
Cars, transport expenses, carriage of cash	(60 089)	(59 614)
Other external services	(75 771)	(74 347)
Stationery, cards, cheques etc.	(20 708)	(18 425)
Sundry taxes	(26 661)	(29 080)
Data transmission	(12 378)	(16 508)
KIR, SWIFT settlements	(25 106)	(24 963)
Security costs	(24 375)	(19 147)
Costs of repairs	(15 942)	(8 770)
Other	(18 421)	(20 487)
Total	(1 139 439)	(1 333 713)

in thousands of PLN

14. Other operating expenses

	01.01.2016- 31.12.2016	01.01.2015- 31.12.2015
Other operating expenses		
Charge of provisions for legal cases and other assets	(93 813)	(67 866)
Impairment loss on property, plant, equipment and intangible assets	(12 359)	-
Costs of purchased services	(2 775)	(1 672)
Other membership fees	(675)	(722)
Paid compensations, penalties and fines	(1 932)	(3 111)
Donations paid	(4 260)	(5 542)
Other	(12 543)	(7 214)
Total	(128 357)	(86 127)

15. Corporate income tax

	01.01.2016- 31.12.2016	01.01.2015- 31.12.2015
Corporate income tax		
Current tax charge	(560 722)	(427 380)
Deferred tax	(6 806)	7 037
Total	(567 528)	(420 343)

	01.01.2016- 31.12.2016	01.01.2015- 31.12.2015
Corporate total tax charge information		
Profit before tax	2 649 248	2 176 553
Tax rate	19%	19%
Tax calculated at the tax rate	(503 357)	(413 545)
Non-tax-deductible expenses	(33 889)	(13 762)
Tax on financial institutions	(67 654)	-
Sale of receivables	(43 223)	(29 110)
Non-taxable income (dividends)	83 439	29 705
Non-tax deductible bad debt provisions	(8 023)	(4 859)
Adjustment of prior year tax	8 385	10 431
Other	(3 206)	797
Total income tax expense	(567 528)	(420 343)

	01.01.2016- 31.12.2016	01.01.2015- 31.12.2015
Deferred tax recognised directly in equity		
Relating to equity securities available-for-sale	(124 073)	(183 376)
Relating to debt securities available-for-sale	33 645	(42 530)
Relating to cash flow hedging activity	26 173	46 079
Relating to valuation of defined benefit plans	(1 835)	(614)
Total	(66 090)	(180 441)

in thousands of PLN

16. Earnings per share

	01.01.2016- 31.12.2016	01.01.2015- 31.12.2015
Earnings per share (PLN/share)		
Profit attributable to ordinary shares	2 081 720	1 756 210
Weighted average number of ordinary shares	99 234 534	99 234 534
Earnings per share (PLN)	20,98	17,70
Profit attributable to ordinary shares	2 081 720	1 756 210
Weighted average number of ordinary shares	99 234 534	99 234 534
Weighted average number of potential ordinary shares *	155 947	167 928
Diluted earnings per share (PLN)	20,94	17,67

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

17. Cash and balances with central banks

	31.12.2016	31.12.2015
Cash and balances with central banks		
Cash	2 114 542	2 003 444
Current accounts in central banks	2 535 091	4 126 099
Term deposits	47 001	-
Total	4 696 634	6 129 543

Bank Zachodni WBK holds an obligatory reserve on a current account in the National Bank of Poland. The figure is calculated at a fixed percentage of the monthly average balance of the customers' deposits, which was 3.5% as at 31.12.2016 and 31.12.2015.

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

18. Loans and advances to banks

	31.12.2016	31.12.2015
Loans and advances to banks		
Loans and advances	798 068	1 753 992
Current accounts, other	2 510 734	2 730 211
Gross receivables	3 308 802	4 484 203
Allowance for impairment	-	(1)
Total	3 308 802	4 484 202

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

in thousands of PLN

19. Financial assets and liabilities held for trading

Financial assets and liabilities held for trading	31.12.2016		31.12.2015	
	Assets	Liabilities	Assets	Liabilities
Trading derivatives	1 876 563	1 729 840	2 074 811	2 011 510
Interest rate operations	971 978	899 009	1 297 769	1 261 946
Forward	6	20	-	-
Options	17 744	17 743	9 638	9 639
IRS	947 336	874 150	1 284 493	1 247 064
FRA	6 892	7 096	3 638	5 243
Transactions on equity instruments	12 032	12 032	13 099	13 099
Options	12 032	12 032	13 099	13 099
FX operations	892 553	818 799	763 943	736 465
CIRS	226 334	245 130	123 878	171 575
Forward	69 838	61 693	35 472	36 408
FX Swap	429 196	352 967	394 037	324 068
Spot	1 561	2 041	1 913	1 729
Options	156 718	156 718	202 503	202 503
Other	8 906	250	6 140	182
Debt and equity securities	1 321 624	-	2 099 823	-
Debt securities	1 312 589	-	2 074 899	-
Government securities:	612 233	-	2 073 995	-
- bonds	612 233	-	2 073 995	-
Central Bank securities:	699 883	-	-	-
- bills	699 883	-	-	-
Commercial securities:	473	-	904	-
- bonds	473	-	904	-
Equity securities:	9 035	-	24 924	-
- listed	9 035	-	24 924	-
Short sale	-	80 129	-	524 198
Total financial assets/liabilities	3 198 187	1 809 969	4 174 634	2 535 708

Financial assets and liabilities held for trading - trading derivatives include the change in the value of counterparty risk in the amount of PLN 9,373 k as at 31.12.2016 and PLN 14,197 k as at 31.12.2015.

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

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

All financial assets measured at fair value through profit and loss are assigned to this category due to the trading character of the transactions. As at 31.12.2016 and in comparable period there were no cases of instruments designated to financial assets measured at fair value through profit and loss at initial recognition.

Offsetting financial assets and financial liabilities

The Bank does not set off or present financial assets and financial liabilities as a net amount. Consequently, in accordance with IFRS 7, the information below refers only to financial assets and financial liabilities arising from forward and derivative transactions effected under master agreements such as ISDA Master Agreement or other master agreements providing for the possibility to terminate and settle the transaction with a counterparty in the event of default on the basis of a net amount of mutual receivables and payables.

The table below presents fair value amounts of derivative instruments (both held for trading and designated as hedging instruments under hedge accounting) and cash collateral covered by mandate agreements providing for the right of set-off under specific circumstances.

in thousands of PLN

Offsetting financial assets and financial liabilities	31.12.2016		31.12.2015	
	Financial assets	Financial liabilities	Financial assets	Financial liabilities
Fair value measurements of derivative instruments	1 934 442	3 691 420	2 231 495	4 035 340
Value of collateral accepted/provided	(249 791)	(2 131 485)	(207 534)	(2 293 837)
Assets and liabilities subject to set-offs under a mandate agreement	1 684 651	1 559 935	2 023 961	1 741 503
Maximum amount of potential set-off	(924 984)	(924 984)	(1 492 632)	(1 492 632)
Assets and liabilities subject to set-offs under a mandate agreement, taking into account the maximum amount of potential set-off	759 667	634 951	531 329	248 871

The table below presents derivatives' nominal values.

Derivatives' nominal values	31.12.2016	31.12.2015
1. Term derivatives (hedging)	30 178 193	35 681 069
a) Single-currency interest rate swap	2 282 240	2 115 615
b) Macro cash flow hedge -purchased (IRS)	2 242 000	3 498 747
c) Macro cash flow hedge -purchased (CIRS)	12 013 523	14 281 838
d) Macro cash flow hedge -sold (CIRS)	13 640 430	15 784 869
2. Term derivatives (trading)	291 909 465	251 524 712
a) Interest rate operations	172 058 392	148 248 296
Single-currency interest rate swap	148 034 909	131 201 753
FRA - purchased amounts	16 680 000	13 375 000
Options	7 314 133	3 671 543
Forward- purchased amounts	27 090	-
Forward- sold amounts	2 260	-
b) FX operations	119 851 073	103 276 416
FX swap – purchased amounts	30 143 163	23 112 618
FX swap – sold amounts	30 025 420	23 042 788
Forward- purchased amounts	5 580 260	4 872 628
Forward- sold amounts	5 620 242	4 899 101
Cross-currency interest rate swap – purchased amounts	13 205 081	9 336 831
Cross-currency interest rate swap – sold amounts	13 232 885	9 389 486
FX options -purchased CALL	5 398 974	6 972 190
FX options -purchased PUT	5 623 037	7 339 292
FX options -sold CALL	5 398 974	6 972 190
FX options -sold PUT	5 623 037	7 339 292
3. Currency transactions- spot	1 540 212	3 119 168
Spot-purchased	769 621	1 559 682
Spot-sold	770 591	1 559 486
4. Transactions on equity financial instruments	1 335 679	1 485 063
Derivatives contract- purchased	664 431	731 883
Derivatives contract - sold	671 248	753 180
Total	324 963 549	291 810 012

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

20. Hedging derivatives

Hedging derivatives	31.12.2016		31.12.2015	
	Assets	Liabilities	Assets	Liabilities
Derivatives hedging fair value	3 232	139 973	116	192 392
Derivatives hedging cash flow	63 555	1 821 855	162 707	1 831 620
Total hedging derivatives	66 787	1 961 828	162 823	2 024 012

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

in thousands of PLN

For the valuation of hedging transactions, Bank uses a valuation model classified to the Level II of fair value, in which data used for valuation are based on observable market parameters (directly or indirectly). Bank treats differences that arise in the initial valuation it as the Day 1 profit or loss and amortises it in time and indicates the valuation effect in the profit and loss account. Amortisation of adjustment to the valuation of day 1 is recognized in Net trading income and revaluation.

21. Loans and advances to customers

Loans and advances to customers	31.12.2016	31.12.2015
Loans and advances to enterprises	46 811 514	45 442 685
Loans and advances to individuals, of which:	42 995 955	38 865 950
<i>Home mortgage loans</i>	32 711 667	29 195 051
Loans and advances to public sector	195 752	234 917
Other	181 596	6 392
Gross receivables	90 184 817	84 549 944
Allowance for impairment	(3 082 427)	(3 424 594)
Total	87 102 390	81 125 350

As at 31.12.2016 the fair value adjustment due to hedged risk on individual loans was PLN 2,948 k.

In December 2015, Bank Zachodni WBK stopped applying fair value macro hedge accounting for a hedge of interest rate risk on fixed interest rate cash loans in PLN (6 relationships in total). By the time the Bank stopped using the hedge accounting, the accumulated fair value adjustment for the hedged position recognized in the balance sheet was PLN 7,148 k. This amount is amortized against the profit & loss account according to the tenors originally agreed for individual hedging relationships. PLN 5,687k was recognised in the income statement for 2016 and PLN 1,461k will be reflected in the income statement by the end of 2018.

Detailed currency analysis of mortgage loans is presented in the consolidated financial statements of Bank Zachodni WBK Group for 2016 released on 17.02.2017.

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

Movements on impairment losses on loans and advances to customers	31.12.2016	31.12.2015
Individual and collective impairment		
As at the beginning of the period	(3 084 165)	(3 079 999)
Charge/write back of current period	(609 609)	(694 394)
Write off/Sale of receivables	938 201	661 948
Transfer	26 892	35 920
F/X differences	(12 180)	(7 640)
Balance at the end of the period	(2 740 861)	(3 084 165)
IBNR		
As at the beginning of the period	(340 429)	(342 520)
Charge/write back of current period	(143)	6 059
Sale of receivables	3 182	-
Transfer	-	-
F/X differences	(4 176)	(3 968)
Balance at the end of the period	(341 566)	(340 429)
Allowance for impairment	(3 082 427)	(3 424 594)

in thousands of PLN

22. Financial assets available for sale

Financial assets available for sale	31.12.2016	31.12.2015
Available for sale investments - measured at fair value		
Debt securities	25 467 070	21 471 774
Government securities:	20 472 331	17 379 677
- bonds	20 472 331	17 379 677
Central Bank securities:	2 849 694	1 849 461
- bills	2 849 694	1 849 461
Commercial securities:	2 145 045	2 242 636
- bonds	2 145 045	2 242 636
Equity securities	855 291	1 095 923
- listed	12 644	18 271
- unlisted	842 647	1 077 652
Investment certificates	-	8 549
Total	26 322 361	22 576 246

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

As at 31.12.2015 fixed interest rate debt securities measured at fair value amount to PLN 16,399,457 k, variable interest rate securities amount to PLN 5,072,317 k.

As at 31.12.2016 fair value adjustment resulting from fair value hedge on available for sale debt securities totaled PLN 132,512 k (as at 31.12.2015 PLN 177,761 k).

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

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

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

Movements on financial assets available for sale	Financial instruments representing equity rights		Total
	Debt securities		
As at 1 January 2015	23 612 492	852 956	24 465 448
Additions	95 257 414	6 805	95 264 219
Disposals (sale and maturity)	(96 982 076)	(15 193)	(96 997 269)
Fair value adjustment	(417 785)	260 227	(157 558)
Movements on interest accrued	(32 928)	-	(32 928)
Allowances for impairment	-	(323)	(323)
F/X differences	34 657	-	34 657
As at 31 December 2015	21 471 774	1 104 472	22 576 246

in thousands of PLN

23. Investments in subsidiaries and associates

Investments in subsidiaries and associates	31.12.2016	31.12.2015
Subsidiaries	2 340 719	2 340 719
Associates	36 606	36 606
Total	2 377 325	2 377 325

Fair value of "Investment in subsidiaries and associates" is presented in Note 41.
There was no impairment of investments in subsidiaries and associates.

in thousands of PLN

Investments in subsidiaries and associates as at 31.12.2016 *

Name of entity	BZ WBK	BZ WBK	Gieldokracja Sp.	BZ WBK	BZ WBK	Santander	Total
	Inwestycje	WBK Finanse	z o.o.	Nieruchomości	Towarzystwo Funduszy Inwestycyjnych	Consumer Bank	
	Sp. z o.o.	Sp. z o.o.	z o.o.	S.A.	S.A.	S.A.	
Registered office	Poznań	Poznań	Poznań	Zakrzewo	Poznań	Wrocław	
Type of connection	Subsidiary	Subsidiary	Subsidiary	Subsidiary	Subsidiary	Subsidiary	
% of holding	100.00	100.00	100.00	99.99	50.00	60.00	
Balance sheet value	46 600	130 097	100	753	6 755	2 156 414	2 340 719
Total assets	44 842	212 953	152	564	117 934	17 382 269	17 758 714
Own funds of entity, of which:	44 807	208 399	152	505	93 603	2 705 034	3 052 500
Share capital	100	1 165	334	750	13 500	520 000	535 849
Other own funds, of which:	44 707	207 234	(182)	(245)	80 103	2 185 034	2 516 651
<i>from previous years</i>	-	-	-	(215)	26 751	-	26 536
<i>net profit (loss)</i>	(6 232)	23 441	(182)	(30)	49 267	451 408	517 672
Liabilities of entity	35	4 554	-	59	24 331	14 677 235	14 706 214
Revenue	(7 805)	32 365	38	117	258 932	1 735 893	2 019 540

* unaudited data

Name of entity	Business
BZ WBK Inwestycje Sp. z o.o.	trading in shares of commercial companies as well as other securities; seeking investors for companies
BZ WBK Finanse Sp. z o.o.	centralised management of the bank's subsidiaries: BZ WBK Leasing S.A., BZ WBK Lease S.A and BZ WBK Faktor Sp. z o.o.
Gieldokracja Sp. z o.o.	advertising services, educational services related to the capital market, maintenance of internet portals and communication services
BZ WBK Nieruchomości S.A.	organisation of various events, catering and hotel services, agency services
BZ WBK Towarzystwo Funduszy Inwestycyjnych S.A.	activities related to the management of funds
Santander Consumer Bank S.A.	accepting savings and term deposits, granting and taking out loans and advances

Name of associate	Country of incorporation and place of business	The Group's share in capital / voting power		Valuation method	Scope of business
		2016	2015		
BZ WBK - Aviva Towarzystwo Ubezpieczeń na Życie S.A.	Poland	49,00	49,00	Equity method	life insurance
BZ WBK - Aviva Towarzystwo Ubezpieczeń Ogólnych S.A.	Poland	49,00	49,00	Equity method	property and personal insurance

in thousands of PLN

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

	BZ WBK - Aviva Towarzystwo Ubezpieczeń na Życie S.A.		BZ WBK - Aviva Towarzystwo Ubezpieczeń Ogólnych S.A.	
	2016 *	2015 *	2016 *	2015 *
Loans and advances to banks	29 667	57 595	10 137	3 827
Financial assets held for trading	18 166	22 024	1 273	2 601
Financial assets available for sale	240 673	147 801	327 600	261 350
Deferred tax assets	750	95	1 060	(961)
Net life insurance assets where the deposit (investment) risk is incurred by the insuring party	538 517	615 798	-	-
Other settlements	66 013	12 359	81 129	18 825
Prepayments	129 269	79 536	12 875	28 929
Other items	1 119	688	924	441
Total assets	1 024 174	935 896	434 998	315 012
Technical insurance provisions	839 675	854 252	175 593	190 194
Reinsurers' share in provisions	(6 059)	(6 502)	(114 575)	(74 642)
Estimated recourses and recoveries (negative value)	-	-	(724)	(436)
Other liabilities	93 858	6 859	103 240	17 093
Prepayments and accruals	1 453	2 340	68 202	44 732
Special funds	15	18	31	38
Total liabilities	928 942	856 967	231 767	176 979
INCOME	191 223	239 430	153 558	164 415
Profit (loss) for the period	40 727	30 688	71 573	40 312
Dividends paid to BZ WBK	10 827	5 721	-	-

* data are based on estimates of companies

in thousands of PLN

Investments in subsidiaries and associates as at 31.12.2015

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

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

in thousands of PLN

24. Intangible assets

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

in thousands of PLN

Intangible assets Year 2015	Licences, patents etc.	Other	Expenditure on intangible assets	Total
Gross value - beginning of the period	1 156 509	213 775	157 644	1 527 928
Additions from:				
- purchases	-	-	156 595	156 595
- donation	-	-	-	-
- intangible assets taken for use	146 813	15 595	-	162 408
- transfers	-	-	3 941	3 941
Disposals from:				
- liquidation, sale	(45 540)	-	(17)	(45 557)
- intangible assets taken for use	-	-	(162 408)	(162 408)
- transfers	-	-	-	-
Gross value - end of the period	1 257 782	229 370	155 755	1 642 907
Accumulated depreciation - beginning of the period	(1 043 619)	(91 044)	-	(1 134 663)
Additions/disposals from:				
- current year amortisation	(78 903)	(31 182)	-	(110 085)
- liquidation, sale	45 444	-	-	45 444
- transfers	-	-	-	-
Write down/Reversal of impairment write down	-	-	-	-
Accumulated depreciation- end of the period	(1 077 078)	(122 226)	-	(1 199 304)
Balance sheet value				
Purchase value	1 257 782	229 370	155 755	1 642 907
Accumulated depreciation	(1 077 078)	(122 226)	-	(1 199 304)
As at 31 December 2015	180 704	107 144	155 755	443 603

25. Goodwill

As at 31.12.2016 and in the corresponding period, the goodwill covered the following item:

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

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

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

In 2016 and in the corresponding period, the Bank conducted tests for impairment of goodwill arising from the merger with Kredyt Bank on 4.01.2013. The carrying amount as at 31.12.2016 was PLN 1,688,516 (the same as at 31.12.2015).

Recoverable amount based on value in use

The recoverable amount of cash-generating units is the higher of fair value less costs of disposal and value in use. Value in use which is higher than the fair value less costs of disposal is measured on the basis of a discounted cash flow model relevant for banks and other financial institutions. The future expected cash flows generated by business segments of Bank Zachodni WBK are in line with the 3-year financial projections of the Bank's management for 2017-2019.

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

in thousands of PLN

Key assumptions for measuring value in use

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

	Business and Global Banking and				ALM and Centre	Total
	Retail Banking	Corporate Banking	Banking	Markets		
Goodwill	764 135	578 808	222 621	122 952	1 688 516	

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

Financial projection

The financial projection for 2017-2019 was prepared taking into account strategic and operational plans for 2017-2019 and available macroeconomic and market forecasts. According to the macroeconomic forecasts for 2017-2019 underlying the goodwill impairment test, the average GDP growth is projected at 2.5%. Interest rates are expected to continue at the low level at least until the end of 2017 and grow thereafter. The financial projection assumes the continued expansion of products and services, with a special focus on an increase in the main product lines and on services to retail and SME customers who use financing and savings products and transactional banking services.

Discount rate

The discount rate in the dividend discount model, depending on the time horizon, is 9.9% - 10.8%. The discount rate equal to the rate of return was calculated on the basis of the Capital Assets Pricing Model, taking into account: risk-free rate, beta coefficient for the banking sector and equity risk premium. The risk-free rate ranges from 3.60% to 4.53% and is based on the yield on treasury securities commensurate with the discount period. Cash flows beyond the 3-year financial projection are discounted using yield on 10-year treasury securities. At the end of 2016, the equity risk premium was estimated at 5.5%.

Growth rate in the period beyond the financial projections

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

Minimum solvency ratio imposed by the regulator

An increase in the required capital amount results in a decrease in the amount of capital available for distribution as part of the test. In Q4 2015, higher capital requirements became effective pursuant to the applicable Polish laws: additional capital requirements for risk associated with FX mortgage loans (0.62 pp), an additional conservation buffer of 1.25 pp and an increase of 3.0 pp in the additional capital requirement enabling dividend payment. All the above factors have a negative impact on the capital available for distribution and, consequently, on the results of the goodwill impairment test.

In view of the above, the minimum solvency ratio assumed in the 3-year projection period is 14.37% and is equal to the minimum ratio imposed by KNF.

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

in thousands of PLN

26. Property, plant and equipment

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

in thousands of PLN

Property, plant & equipment Year 2015	Land and buildings	Financial leaseback - land and buildings	Equipment	Transportation means	Other fixed assets	Financial leaseback - expenditure	Capital expenditures	Total
Gross value - beginning of the period	975 589	-	699 789	61 273	292 514	-	92 137	2 121 302
Additions from:								
- purchases	-	-	-	-	-	3 067	146 436	149 503
- leasing	-	39 480	-	39 740	-	-	-	79 220
- fixed assets taken for use	22 548	-	73 812	-	8 640	-	-	105 000
- transfers	1 319	-	-	-	23 911	-	-	25 230
Disposals from:								
- sale, liquidation, donation	(134 136)	-	(193 856)	(429)	(48 219)	-	(1 837)	(378 477)
- fixed assets taken for use	-	-	-	-	-	-	(105 000)	(105 000)
- transfers	-	-	(23 911)	(15 080)	-	-	(3 941)	(42 932)
Gross value - end of the period	865 320	39 480	555 834	85 504	276 846	3 067	127 795	1 953 846
Accumulated depreciation - beginning of the period	(615 928)	-	(552 037)	(23 652)	(253 473)	-	-	(1 445 090)
Additions/disposals from:								
- current year amortisation	(25 898)	(660)	(47 099)	(10 743)	(11 618)	-	-	(96 018)
- sale, liquidation, donation	80 567	-	193 715	429	45 426	-	-	320 137
- transfers	(210)	-	19 087	9 580	(19 087)	-	-	9 370
Accumulated depreciation- end of the period	(561 469)	(660)	(386 334)	(24 386)	(238 752)	-	-	(1 211 601)
Balance sheet value								
Purchase value	865 320	39 480	555 834	85 504	276 846	3 067	127 795	1 953 846
Accumulated depreciation	(561 469)	(660)	(386 334)	(24 386)	(238 752)	-	-	(1 211 601)
As at 31 December 2015	303 851	38 820	169 500	61 118	38 094	3 067	127 795	742 245

in thousands of PLN

27. Net deferred tax assets

	31.12.2016	Changes to equity	Changes to financial result	Changes in temporary differences	31.12.2015
Deferred tax assets					
Provisions for impairment of loans and advances	440 134	-	11 645	11 645	428 489
Valuation of derivative financial instruments	718 212	-	(49 632)	(49 632)	767 844
Cash flow hedges valuation	26 173	(19 906)	-	(19 906)	46 079
Other provisions	106 521	-	(3 810)	(3 810)	110 331
Deferred income	263 974	-	10 073	10 073	253 901
Unrealized interest on credits, loans and securities	18 688	-	(22 164)	(22 164)	40 852
Other negative temporary differences	8 377	-	604	604	7 773
Total assets of deferred tax	1 582 079	(19 906)	(53 284)	(73 190)	1 655 269
Deferred tax liabilities					
Revaluation of financial instruments available for sale	(90 428)	135 478	-	135 478	(225 906)
Provisions for retirement allowances	(1 836)	(1 222)	-	(1 222)	(614)
Valuation of derivative financial instruments	(367 427)	-	56 063	56 063	(423 490)
Unrealised interest income on loans, securities and interbank deposits	(173 492)	-	(13 613)	(13 613)	(159 879)
Prepayments regarding amortization of applied investment relief	(1 876)	-	327	327	(2 203)
Difference between balance sheet and taxable value of non-financial assets	5 260	-	3 169	3 169	2 091
Other positive temporary differences	(1 973)	-	532	532	(2 505)
Total liabilities deferred tax	(631 772)	134 256	46 478	180 734	(812 506)
Net deferred tax assets	950 307	114 350	(6 806)	107 544	842 763

As at 31.12.2016 the assets in the calculation of deferred tax assets do not include purchased receivables in the amount of gross PLN 8,500 k and provisions for loans that do not become tax expense in the amount of gross PLN 52,896 k.

	31.12.2015	Changes to equity	Changes to financial result	Changes in temporary differences	31.12.2014
Deferred tax assets					
Provisions for impairment of loans and advances	428 489	-	(15 641)	(15 641)	444 130
Valuation of derivative financial instruments	767 844	-	86 638	86 638	681 206
Cash flow hedges valuation	46 079	20 972	-	20 972	25 107
Other provisions	110 331	-	12 166	12 166	98 165
Deferred income	253 901	-	20 206	20 206	233 695
Unrealized interest on credits, loans and securities	40 852	-	(94 584)	(94 584)	135 436
Other negative temporary differences	7 773	-	1 172	1 172	6 601
Total assets of deferred tax	1 655 269	20 972	9 957	30 929	1 624 340
Deferred tax liabilities					
Revaluation of financial instruments available for sale	(225 906)	22 631	-	22 631	(248 537)
Provisions for retirement allowances	(614)	(1 886)	-	(1 886)	1 272
Valuation of derivative financial instruments	(423 490)	-	(11 733)	(11 733)	(411 757)
Unrealised interests from loans, securities and interbank deposits	(159 879)	-	3 651	3 651	(163 530)
Prepayments regarding amortization of applied investment relief	(2 203)	-	1 024	1 024	(3 227)
Difference between balance sheet and taxable value of non-financial assets	2 091	-	3 262	3 262	(1 171)
Other positive temporary differences	(2 505)	-	877	877	(3 382)
Total liabilities deferred tax	(812 506)	20 745	(2 919)	17 826	(830 332)
Net deferred tax assets	842 763	41 717	7 038	48 755	794 008

As at 31.12.2015 the assets in the calculation of deferred tax assets do not include purchased receivables in the amount of gross PLN 11,893 k and provisions for loans that do not become tax expense in the amount of gross PLN 91,615 k.

in thousands of PLN

Movements on net deferred tax	31.12.2016	31.12.2015
As at the beginning of the period	842 763	794 008
Changes recognised in income statement	(6 806)	7 037
Changes recognised in other comprehensive income	114 350	41 718
Balance at the end of the period	950 307	842 763

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

Temporary differences recognised in the income statement comprise provision for impairment of loans and receivables and assets in the course of business.

28. Assets classified as held for sale

Assets classified as held for sale	31.12.2016	31.12.2015
Land and buildings	608	637
Total	608	637

29. Other assets

Other assets	31.12.2016	31.12.2015
Interbank and interbranch settlements	106 835	120 406
Sundry debtors	277 447	227 847
Prepayments	31 715	31 265
Repossessed assets	24 463	37 364
Settlements of stock exchange transactions	21 385	23 508
Other	52	52
Total	461 897	440 442
of which financial assets*	405 667	371 761

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

30. Deposits from banks

Deposits from banks	31.12.2016	31.12.2015
Term deposits	28 522	29 050
Loans from other banks	664 188	195 247
Current accounts	520 055	324 261
Total	1 212 765	548 558

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

in thousands of PLN

31. Deposits from customers

Deposits from customers	31.12.2016	31.12.2015
Deposits from individuals	57 845 383	54 219 574
Term deposits	18 086 495	22 061 992
Current accounts	39 650 731	32 087 122
Other	108 157	70 460
Deposits from enterprises	42 540 494	36 729 117
Term deposits	20 453 339	18 424 576
Current accounts	18 519 563	14 972 460
Credits	3 020 931	2 638 739
Other	546 661	693 342
Deposits from public sector	2 995 372	3 072 591
Term deposits	1 234 058	1 292 043
Current accounts	1 747 709	1 668 272
Other	13 605	112 276
Total	103 381 249	94 021 282

As at 31.12.2016 deposits held as collateral totalled PLN 277,959 k (as at 31.12.2015 - PLN 492,717 k).

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

32. Subordinated liabilities

Subordinated liabilities	Redemption date	Currency	Nominal value
Tranche 1	05.08.2025	EUR	100 000

Movements in subordinated liabilities	31.12.2016	31.12.2015
As at the beginning of the period	426 507	1 439 835
Increase (due to):	29 231	166 216
- interest on subordinated loan	16 479	42 564
- FX differences	12 752	123 652
Decrease (due to):	(15 281)	(1 179 544)
- subordinated loans repayment	-	(1 138 338)
- interest repayment	(15 281)	(41 206)
As at the end of the period	440 457	426 507
Short-term	1 604	2 158
Long-term (over 1 year)	438 853	424 349

Subordinated loans in the amount of PLN 1,138,338 k were repaid to KBC Bank in June 2015 as they no longer qualified to be treated as Tier II capital under CRD IV/CRR rules.

Other details on these liabilities are disclosed in Note 4.

in thousands of PLN

33. Debt securities in issue

Debt securities in issue	ISIN	Nominal value	Currency	Redemption date	31.12.2016
Series C bank securities	PLBZ00000218	100 000	PLN	17.02.2017	
Series D	PLBZ00000200	185 000	PLN	26.02.2017	
Series B	PLBZ00000168	475 000	PLN	17.07.2017	
Series C	PLBZ00000176	485 000	PLN	25.06.2018	
Series E	PLBZ00000226	120 000	EUR	03.12.2026	
Debt securities in issue					
- as at the end of the period					1 783 303

Debt securities in issue	ISIN	Nominal value	Currency	Redemption date	31.12.2015
Series A bank securities	PLBZ00000184	230 000	PLN	17.02.2016	
Series A	PLBZ00000150	500 000	PLN	19.12.2016	
Series B	PLBZ00000168	475 000	PLN	17.07.2017	
Series C	PLBZ00000176	485 000	PLN	25.06.2018	
Debt securities in issue					
- as at the end of the period					1 698 619

Movements in debt securities in issue	31.12.2016	31.12.2015
As at the beginning of the period	1 698 619	983 646
Increase (due to):	1 111 318	753 484
- debt securities in issue	1 065 880	715 000
- interest on debt securities in issue	45 438	38 484
Decrease (due to):	(1 026 634)	(38 511)
- debt securities buy out	(980 000)	-
- interest repayment	(46 634)	(38 511)
As at the end of the period	1 783 303	1 698 619

34. Provisions

Provisions	31.12.2016	31.12.2015
Provisions for legal claims	37 639	27 373
Provisions for off-balance sheet credit facilities	28 706	55 276
Total	66 345	82 649

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

in thousands of PLN

Change in provisions 31.12.2015	Provisions for legal claims	Provisions for off balance sheet credit facilities	Total
As at the beginning of the period	39 466	71 050	110 516
Provision charge	4 299	86 730	91 029
Utilization	(7 628)	252	(7 376)
Write back	(8 764)	(102 756)	(111 520)
Other changes	-	-	-
Balance at the end of the period	27 373	55 276	82 649
Short-term	27 373	40 880	68 253
Long-term	-	14 396	14 396

35. Other liabilities

Other liabilities	31.12.2016	31.12.2015
Employee provisions	311 687	319 000
Other provisions	3 300	3 306
Interbank and interbranch settlements	578 741	202 215
Other deferred and suspended income	171 320	157 560
Sundry creditors	413 579	353 179
Accrued liabilities	137 364	152 191
Public and law settlements	78 248	45 236
Settlements of stock exchange transactions	25 314	25 376
Total	1 719 553	1 258 063
of which financial liabilities *	1 469 985	1 055 267

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

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

Change in provisions 31.12.2015	Employee provisions*	Other provisions	Total
As at the beginning of the period	306 503	3 300	309 803
Provision charge	249 212	6	249 218
Utilization	(227 870)	-	(227 870)
Write back	(8 845)	-	(8 845)
Other changes	-	-	-
Balance at the end of the period	319 000	3 306	322 306
Short-term	259 678	3 306	262 984
Long-term	59 322	-	59 322

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

in thousands of PLN

36. Share capital

31.12.2016

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

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

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

31.12.2015

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

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

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

in thousands of PLN

37. Other reserve capital

Other reserve capital	31.12.2016	31.12.2015
General banking risk fund	649 810	649 810
Share premium	7 035 424	7 035 424
Other reserves of which:	7 447 759	6 553 441
<i>Reserve capital</i>	7 277 010	6 382 692
<i>Supplementary capital</i>	170 749	170 749
Total	15 132 993	14 238 675

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

Reserve capital as at 31.12.2016 includes share scheme charge of PLN 120 750 k, as at 31.12.2015 of PLN 104,537 k.

Other movements of other reserve capital are presented in "movements on equity" for 2016 and 2015.

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

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

38. Revaluation reserve

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

in thousands of PLN

Revaluation reserve 31.12.2015	Total gross	Deferred tax adjustment	Total nett
Opening balance, of which:	1 169 253	(222 158)	947 095
Debt and equity securities	1 308 090	(248 537)	1 059 553
Valuation related to cash flow hedge	(132 140)	25 107	(107 033)
Actuarial gains/losses on retirement allowances	(6 697)	1 272	(5 425)
Change in valuation of debt and equity securities available for sale investments	(118 351)	22 487	(95 864)
Decrease in revaluation reserve related to sale of investments	(763)	145	(618)
Change of cash flow hedges valuations	(102 672)	19 508	(83 164)
Change in available for sale cash flow hedges valuations	(7 710)	1 465	(6 245)
Change of actuarial gains/losses on retirement allowances	9 930	(1 887)	8 043
Closing balance, of which:	949 687	(180 440)	769 247
Debt and equity securities	1 188 976	(225 905)	963 071
Valuation related to cash flow hedge	(242 522)	46 080	(196 442)
Actuarial gains/losses on retirement allowances	3 233	(615)	2 618

39. Hedge accounting

The Bank applies hedge accounting in line with the risk management assumptions described in Note 3 of the annual financial statements.

Fair value hedges

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

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

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

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

The tables below contain details about individual groups of hedge transactions for 2016 and the comparative period:

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

31.12.2015	Bonds
Nominal value of hedging position	2 115 615
Measurement to fair value of hedging instrument	(181 935)
Fair value adjustment of hedged instrument due to hedged risk	177 761
Hedged risk	Interest rate risk
Period over which the instruments have an impact on the Bank's results	up to 2023

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

in thousands of PLN

In December 2015, Bank Zachodni WBK stopped applying fair value macro hedge accounting for a hedge of interest rate risk on fixed interest rate cash loans in PLN (6 relationships in total). By the time the Bank stopped using the hedge accounting, the accumulated fair value adjustment for the hedged position recognized in the balance sheet was PLN 7,148 k. This amount is amortized against the profit & loss account according to the tenors originally agreed for individual hedging relationships. PLN 5,687k was recognised in the income statement for 2016 and PLN 1,461k will be reflected in the income statement by the end of 2018.

Cash flow hedging

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

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

As of 31.12.2016, the nominal value of the hedging item was PLN 15,882,430 k (31.12.2015 – PLN 19,283,616) k. Measurement to fair value of the hedging instrument was PLN (137,755) k (31.12.2015 – PLN (242,522) k); the same amount, less deferred tax, is recognised in comprehensive income and accumulated in the Bank's equity under revaluation reserve. Hedging instruments have been concluded for a period of time until 2028.

The non-effective portion of fair value of the cash flow hedge was PLN (7,235) k as of 31.12.2016 and PLN 11,123 k as of 31.12.2015. It was taken to the 'Net trading income and revaluation' line of the profit and loss account.

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

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

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

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

	31.12.2016	31.12.2015
	Balance sheet value	Balance sheet value
Liabilities valued at amortised cost (contains sell-buy-back)	-	4 007 525
Fair value of securities held as collateral for sell-buy-back/repo transactions	-	3 945 269
Buy-sell-back transactions	-	289 260
Fair value of securities held for buy-sell-back/reverse repo transactions	-	289 260

Buy-sell-back transactions	31.12.2016	31.12.2015
Buy-sell-back transactions to banks	-	272 300
Buy-sell-back transactions to customers	-	16 960
Total	-	289 260

Sell-buy-back transactions	31.12.2016	31.12.2015
Sell-buy-back transactions from banks	-	3 387 335
Sell-buy-back transactions from customers	-	620 190
Total	-	4 007 525

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

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

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

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

in thousands of PLN

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

As at 31.12.2016 and 31.12.2015 statements of financial position contained no financial instruments serving as collateral to repo transactions maturing within a period shorter or equal to that of the main transaction.

41. Fair value

Fair value is the amount for which an asset could be exchanged, or a liability settled, between knowledgeable, willing parties in an arm's length transaction other than in a forced or liquidation sale, and is best reflected by the market price, if available.

Below is a summary of the book values and fair values of the individual groups of assets and liabilities.

Assets	31.12.2016		31.12.2015	
	Book Value	Fair Value	Book Value	Fair Value
Cash and balances with central banks	4 696 634	4 696 634	6 129 543	6 129 543
Loans and advances to banks	3 308 802	3 308 802	4 484 202	4 484 202
Financial assets held for trading	3 198 187	3 198 187	4 174 634	4 174 634
Hedging derivatives	66 787	66 787	162 823	162 823
Loans and advances to customers	87 102 390	87 014 565	81 125 350	81 773 676
Financial assets available for sale	26 322 361	26 322 361	22 576 246	22 576 246
Liabilities				
Deposits from banks	1 212 765	1 212 765	548 558	548 558
Hedging derivatives	1 961 828	1 961 828	2 024 012	2 024 012
Financial liabilities held for trading	1 809 969	1 809 969	2 535 708	2 535 708
Subordinated liabilities	440 457	564 402	426 507	503 582
Deposits from customers	103 381 249	103 390 563	94 021 282	94 020 221

Below is a summary of the key methods and assumptions used in the estimation of fair values of the financial instruments shown in the table above.

Financial assets and liabilities not carried at fair value in the statement of financial position

The Bank has financial instruments which in accordance with the IFRS are not carried at fair value in the accounts. The fair value of such instruments is measured using the following methods and assumptions.

Apart from assets that are not measured at fair value, all the other fair values fulfil conditions for classification to Level II of fair value.

Loans and advances to banks: The fair value of deposits and placements is measured using discounted cash flows at the current money market interest rates for receivables of similar credit risk, maturity and currency. In the case of demand deposits without a fixed maturity date or with maturity up to 6 months, it is assumed that their fair value is not significantly different than their book value. The process of fair value estimation for these instruments is not affected by the long-term nature of the business with depositors.

Loans and advances to customers: Carried at net value after impairment charges. Fair value is calculated as the discounted value of the expected future cash flows in respect of principal and interest payments. It is assumed that loans and advances will be repaid at their contractual maturity date. The estimated fair value of the loans and advances reflects changes in the credit risk from the moment of sanction (margins) and changes in interest rates.

Financial assets not carried at fair value: The Bank does not use fair valuation for equity securities of unlisted companies for which the fair value cannot be reliably established. In the statement of financial position, equity instruments are presented at cost less impairment. Debt instruments are measured at amortised cost.

Deposits from banks and deposits from customers: Fair value of the deposits with maturity exceeding 6 months was estimated based on the cash flows discounted by the current market rates for the deposits with similar maturity dates. In the case of demand deposits without a fixed maturity date or with maturity up to 6 months, it is assumed that their fair value is not significantly different than their book value. The process of fair value estimation for these instruments is not affected by the long-term nature of the business with depositors.

Debt securities in issue and subordinated liabilities: The Bank has made an assumption that fair value of those securities is based on discounted cash flows methods incorporating adequate interest rates.

in thousands of PLN

Financial assets and liabilities carried at fair value in the statement of financial position

As at 31.12.2016 and in the comparable periods the Bank made the following classification of its financial instruments measured at fair value in the statement of financial position:

Level I (active market quotations): debt, equity and derivative financial instruments which at the balance sheet date were measured using the prices quoted in the active market. The Bank allocates to this level fixed-rate State Treasury bonds, treasury bills, Eurobonds of the German government, Eurobonds of the American government, shares of listed companies and WIG 20 futures.

Level II (the measurement methods based on market-derived parameters): This level includes derivative instruments and variable-rate State Treasury bonds. These bonds were measured using discounted cash flow models based on the discount curve derived from the market of fixed-rate treasury bonds. Derivative instruments are measured using discounted cash flow models based on the discount curve derived from the inter-bank market.

Level III (measurement methods using material non-market parameters): The level includes equity securities that are not quoted in the active market, measured using the expert valuation model; investment certificates measured at the balance sheet date at the price announced by the mutual fund.

The objective of using a valuation technique is to determine the fair value, i.e., prices, which were obtained by the sale of an asset in an orderly transaction between market participants carried out under current market conditions between market participants at the measurement date.

Valuation of major capital investments classified to Level III:

- a) AVIVA Towarzystwo Ubezpieczeń na Życie SA (AVIVA TUŻ),
- b) AVIVA Powszechne Towarzystwo Emerytalne SA (AVIVA PTE),
- c) AVIVA Towarzystwo Ubezpieczeń Ogólnych SA (AVIVA TUO)

are made semi-annually by specialized units of the Bank using income methods based on discounted cash flows, where the most important variables of the model are the level of forecasted dividends and the risk free rate. During the reporting period revaluation of above equity investments has been made in the total amount of (57.8 million PLN). This write-off, net of tax, was recognized in the revaluation reserve.

As at 31.12.2016 and in the comparable period the Bank classified its financial instruments to the following fair value levels.

31.12.2016	Level I	Level II	Level III	Total
Financial assets				
Financial assets held for trading	282 769	2 915 167	251	3 198 187
Hedging derivatives	-	66 787	-	66 787
Financial investment assets - debt securities	15 062 259	10 366 571	38 240	25 467 070
Financial investment assets - equity securities	12 644	-	842 647	855 291
Total	15 357 672	13 348 525	881 138	29 587 335
Financial liabilities				
Financial liabilities held for trading	80 129	1 729 840	-	1 809 969
Hedging derivatives	-	1 961 828	-	1 961 828
Total	80 129	3 691 668	-	3 771 797

31.12.2015	Level I	Level II	Level III	Total
Financial assets				
Financial assets held for trading	1 743 073	2 429 722	1 839	4 174 634
Hedging derivatives	-	162 823	-	162 823
Financial investment assets - debt securities	14 549 997	6 921 777	-	21 471 774
Financial investment assets - equity securities	18 271	-	1 086 201	1 104 472
Total	16 311 341	9 514 322	1 088 040	26 913 703
Financial liabilities				
Financial liabilities held for trading	524 198	2 011 510	-	2 535 708
Hedging derivatives	-	2 024 012	-	2 024 012
Total	524 198	4 035 522	-	4 559 720

in thousands of PLN

The tables below show reconciliation of changes in the balance of financial instruments whose fair value is established by means of the valuation methods using material non-market parameters.

Level III	Financial assets			Financial liabilities
	Financial assets held for trading	Financial investment assets - debt securities	Financial investment assets - equity securities	Financial liabilities held for trading
31.12.2016				
Beginning of the period	1 839	-	1 086 201	-
Profit or losses				
<i>recognised in income statement</i>	81	-	68 506	-
<i>recognised in equity</i>	-	-	(52 028)	-
Purchase	340	-	4 900	-
Sale	(2 009)	-	(264 932)	-
Matured	-	-	-	-
Impairment	-	-	-	-
Other	-	38 240	-	-
At the period end	251	38 240	842 647	-

Level III	Financial assets			Financial liabilities
	Financial assets held for trading	Financial investment assets - debt securities	Financial investment assets - equity securities	Financial liabilities held for trading
31.12.2015				
Beginning of the period	1 390	-	832 488	-
Profit or losses				
<i>recognised in income statement</i>	23	-	-	-
<i>recognised in equity</i>	-	-	258 175	-
Purchase	1 278	-	6 805	-
Sale	(852)	-	(11 267)	-
Matured	-	-	-	-
Impairment	-	-	-	-
Transfer between levels	-	-	-	-
At the period end	1 839	-	1 086 201	-

42. Contingent liabilities

Significant court proceedings conducted by Bank Zachodni WBK

As at 31.12.2016, no proceedings were instituted by court or by state administration agencies with relation to any claims made by or against the Bank amounting to a minimum of 10% of the Bank's equity.

The value of all litigation amounts to PLN 437,175 k, which is ca. 2.30% of the Bank's equity. This amount includes PLN 247,406 k claimed by the Bank, PLN 189,769 k in claims against the Bank. In 2016, there was a significant year-on-year increase in the amount claimed by the Bank (from PLN 93,305 k to PLN 247,406 k) which results from the abrogation of the laws pertaining to the banking writs of execution and the need to refer to the court any unpaid receivables of the bank under ordinary proceedings or proceedings by writ of payment. There were no litigations for bankruptcy or arrangement.

In 2016 the amount of significant court proceedings which had been completed amounted to PLN 246,789 k.

As at 31.12.2016, the value of provisions for legal risks, for court cases against the Bank was PLN 37,639 k. In 8 cases against the Bank, where the claim value was high, a provision of PLN 34,778 k was raised.

As at 31.12.2015, no proceedings were instituted by court or by state administration agencies with relation to any claims made by or against the Bank amounting to a minimum of 10% of the Bank's equity.

in thousands of PLN

The value of all litigation amounts to PLN 305,012 k, which is ca. 1.63% of the Bank's equity. This amount includes PLN 93,305 k claimed by the Bank, PLN 198,060 k in claims against the Bank and PLN 13,647 k are Bank's receivables due to bankruptcy or arrangement cases.

In 2015 the amount of significant court proceedings which had been completed amounted to PLN 16,128 k.

As at 31.12.2015, the value of provisions for legal risks, for court cases against the Bank was PLN 27,373 k. In 8 cases against the Bank, where the claim value was high, a provision of PLN 25,000 k was raised.

The Bank raises provisions for legal risk where an internal risk assessment for a particular case indicates a possible outflow of cash. Provisions for cases disputed in court are presented in Note 34.

Off-balance sheet liabilities

The break-down of contingent liabilities and off-balance transactions into categories are presented below. The values of guarantees and letters of credit as set out in the table below represent the maximum possible loss that would be disclosed as at the balance sheet day if the customers did not meet any of their obligations towards third parties.

Contingent liabilities - sanctioned	31.12.2016	31.12.2015
Liabilities sanctioned		
- financial	21 445 091	20 863 915
- credit lines	17 945 726	17 948 232
- credit cards debits	2 809 662	2 474 536
- import letters of credit	655 655	438 346
- term deposits with future commencement term	34 048	2 801
- guarantees	4 248 934	4 488 629
Allowance for impairment	(28 706)	(55 276)
Total	25 694 025	25 352 544

43. Assets and liabilities pledged as collateral

Assets securing funds to cover the BGF are debt securities.

In order to calculate the contribution to the deposit protection fund, Bank Zachodni WBK applied 0.55% (i.e. the same rate as in 2015) of funds deposited in all accounts with the bank, being the basis for calculating the obligatory reserve.

As at 31.12.2016, assets allocated to that end totalled PLN 554,489k compared with PLN 507,992k a year before.

In 2016, deposits opened with financial institutions to secure the value of transactions totalled PLN 2 131 120k (PLN 2,293,716k as at 31.12.2015).

In 2016, the BZ WBK accepted PLN 249,871k worth of deposits securing transactions (vs. PLN 207,623k in 2015).

Other assets pledged and liabilities accepted as collateral are disclosed in Notes 31 and 40.

44. Finance and operating leases

Finance leases

Bank Zachodni WBK acts as a lessee in finance lease agreements where the lessor side is represented by BZ WBK leasing subsidiaries. The leasing contracts finance purchase of cars and furniture.

Finance leases gross liabilities - maturity	31.12.2016	31.12.2015
less than 1 year	13 340	16 236
between 1 and 5 years	46 913	36 105
over 5 years	422	-
Total	60 675	52 341

in thousands of PLN

Present value of minimum lease payments - maturity	31.12.2016	31.12.2015
less than 1 year	13 332	16 082
between 1 and 5 years	43 254	33 500
over 5 years	374	-
Total	56 960	49 582

Reconciliation between the gross investment and the present value of minimum lease payments	31.12.2016	31.12.2015
Finance leases gross liabilities	60 675	52 341
Unrealised financial costs	(3 715)	(2 759)
Present value of minimum lease payments	56 960	49 582

Financial leaseback

On 16.04.2015, an agreement was signed between BZ WBK and its subsidiary BZ WBK Leasing providing for a financial leaseback of properties (freehold of a building and land and perpetual usufruct of land) and a lease of a planned project (an office building to be developed during the next three years) located in Wrocław.

The final total value of the assets arising from the lease of the building and land, which was estimated at the time of initiation of the transaction, was PLN 156,278 k.

Current value of the fixed assets obtained under the financial leaseback agreement was PLN 38,976 k as at 31.12.2016, the initial value of fixed assets under construction was PLN 20,328 k.

In accordance with the agreement, the basic lease term was defined as 153 months.

The purchase of assets by BZ WBK Leasing and development of the office building is financed with a loan provided by BZ WBK.

The lease agreement requires that only interest should be paid on the lease and the loan during the term of the respective agreements, while the principal sums will be paid as part of the last tranche, with the pre-financing costs relating to the building and the site where the building is developed are to be capitalised by BZ WBK Leasing, and the bank is to pay them along with the principal payment at the end of contractual period. Both agreements are to be based on 1M WIBOR + margin, and the parties reportedly plan to offset their mutual obligations.

Finance leaseback gross liabilities - maturity	31.12.2016	31.12.2015
less than 1 year	421	427
between 1 and 5 years	1 686	1 706
over 5 years	30 614	31 416
Total	32 721	33 549

Present value of minimum lease payments - maturity	31.12.2016	31.12.2015
less than 1 year	418	423
between 1 and 5 years	1 611	1 631
over 5 years	26 056	26 347
Total	28 085	28 401

Reconciliation between the gross investment and the present value of minimum lease payments	31.12.2016	31.12.2015
Finance leaseback gross liabilities	32 721	33 549
Unrealised financial costs	(4 636)	(5 148)
Present value of minimum lease payments	28 085	28 401

Operating leases

The BZ WBK leases offices in compliance with operational leasing agreements. As a standard, agreements are concluded for 5-10 years. A small part of the offices is subleased outside the Bank. In 2016 and 2015 rentals totalled PLN 192,596 k and PLN 218,270 k, respectively. These payments are presented in the profit and loss account under "operating expenses".

The table below shows the total obligations under irrevocable operating lease agreements concluded by the Bank (including the value of perpetual usufruct of land).

in thousands of PLN

Payments - maturity	31.12.2016	31.12.2015
less than 1 year	197 670	217 432
between 1 and 5 years	462 982	439 575
over 5 years	467 632	421 770
Total	1 128 284	1 078 777

45. Statement of cash flows- additional information

Table below specifies components of cash balances of Bank Zachodni WBK.

Cash components	31.12.2016	31.12.2015
Cash and balances with central banks	4 696 634	6 129 543
Receivables from interbank deposits*	3 308 344	3 750 899
Debt securities held for trading*	699 883	-
Debt securities available for sale*	2 849 694	1 849 461
Total	11 554 555	11 729 903
The impact of changes in currency exchange rates during the financial year on cash and cash equivalents	85 118	12 980

* financial assets with initial maturity below three months

Bank Zachodni WBK holds restricted cash, which are the funds accumulated on obligatory reserve account in the Central Bank.

In the periods presented in the financial statement Bank Zachodni WBK has received and made interest payments in the following amounts:

Interests received and interests paid	01.01.2016- 31.12.2016	01.01.2015- 31.12.2015
Interests received, including:	4 636 840	4 305 174
- operating activities	4 036 599	3 661 350
- investing activities	600 241	643 824
Interests paid, including:	(958 223)	(923 489)
- operating activities	(882 667)	(832 278)
- financing activities	(75 556)	(91 211)

46. Related parties

The tables below present intercompany transactions. Most of the transactions are banking transactions made as part of ordinary business activities and mainly include loans, deposits, guarantees, leases. In the case of internal transactions, a transfer pricing documentation is prepared.

in thousands of PLN

Transactions with subsidiaries	31.12.2016	31.12.2015
ASSETS	7 986 464	8 528 758
Loans and advances to banks	3 312	1 151 017
Financial assets held for trading	17 820	9 123
Loans and advances to customers	7 952 284	7 356 993
Other assets	13 048	11 625
LIABILITIES	322 073	272 243
Deposits from banks	51 406	12 867
Financial liabilities held for trading	911	43
Deposits from customers	152 939	166 793
Other liabilities	116 817	92 540
INCOME	276 217	342 419
Interest income	147 114	142 294
Fee and commission income	133 083	143 557
Other operating income	8 183	7 689
Net trading income and revaluation	(12 163)	48 879
Gains (losses) from other financial securities	-	-
EXPENSES	9 442	15 121
Interest expenses	5 035	9 383
Fee and commission expenses	4 384	5 067
Operating expenses incl.:	23	671
<i>Bank's staff, operating expenses and management costs</i>	-	647
<i>Other</i>	23	24
CONTINGENT LIABILITIES	1 837 552	2 292 336
Sanctioned:	1 837 552	2 292 336
- <i>financial</i>	1 770 561	2 227 705
- <i>guarantees</i>	66 991	64 631
DERIVATIVES' NOMINAL VALUES	1 868 845	1 553 216
Spot-purchased	-	51 120
Spot-sold	-	51 138
FX swap – purchased amounts	-	162 779
FX swap – sold amounts	-	161 541
Cross-currency interest rate swap – purchased amounts	288 211	275 758
Cross-currency interest rate swap – sold amounts	270 900	270 900
Single-currency interest rate swap	1 309 734	579 980

Transactions with associates	31.12.2016	31.12.2015
LIABILITIES	78 414	60 075
Deposits from customers	78 414	60 075
INCOME	17 755	49 028
Fee and commission income	17 755	49 028
EXPENSES	7 783	4 412
Interest expenses	1 313	1 237
Fee and commission expenses	89	203
Operating expenses incl.:	6 381	2 972
<i>contingent liabilities</i>	6 381	2 972
CONTINGENT LIABILITIES	-	407
Sanctioned:	-	407
- <i>guarantees</i>	-	407

in thousands of PLN

Transactions with Santander Group	with the parent company		with other entities	
	31.12.2016	31.12.2015	31.12.2016	31.12.2015
ASSETS	981 961	684 477	3 674	13 376
Loans and advances to banks, incl:	594 042	337 099	274	1 391
<i>deposits</i>	353 911	252 132	-	-
<i>current accounts</i>	240 131	84 967	274	1 391
Financial assets held for trading	387 727	343 790	3 371	11 982
Hedging derivatives	-	1 529	-	-
Other assets	192	2 059	29	3
LIABILITIES	633 941	401 482	90 859	124 986
Deposits from banks incl.:	271 312	102 590	3 683	9 193
<i>current accounts</i>	271 312	102 590	3 683	9 193
Hedging derivatives	54 503	22 065	-	-
Financial liabilities held for trading	308 126	276 696	7 365	7 220
Deposits from customers	-	-	71 079	105 202
Other liabilities	-	131	8 732	3 371
INCOME	2 265 606	736 899	(2 146)	473
Interest income	14 268	13 035	28	11
Fee and commission income	2 096	2 220	239	63
Other operating income	-	-	7	614
Net trading income and revaluation	2 249 242	721 644	(2 420)	(215)
EXPENSES	1 721	1 083	23 681	15 314
Interest expenses	446	116	1 276	1 034
Fee and commission expenses	1 106	967	5	3
Operating expenses incl.:	169	-	22 400	14 277
<i>Bank's staff, operating expenses and management costs</i>	-	-	22 400	14 277
<i>Other operating expenses</i>	169	-	-	-
CONTINGENT LIABILITIES	10 706	280	-	-
Sanctioned:	10 706	280	-	-
- <i>financial</i>	10 706	280	-	-
- <i>guarantees</i>	-	-	-	-
DERIVATIVES' NOMINAL VALUES	57 761 351	48 521 643	634 312	2 059 430
Cross-currency interest rate swap – purchased amounts	5 645 125	3 704 776	-	-
Cross-currency interest rate swap – sold amounts	5 424 101	3 586 042	-	-
Single-currency interest rate swap	16 517 900	11 991 876	633 412	1 591 418
FRA	-	1 600 000	-	-
Options	7 285 846	3 626 907	-	-
FX swap – purchased amounts	5 363 317	4 412 806	-	-
FX swap – sold amounts	5 344 715	4 401 243	-	-
FX options -purchased CALL	2 643 269	3 563 906	-	-
FX options -purchased PUT	2 798 804	3 751 086	-	-
FX options -sold CALL	2 755 705	3 408 284	-	-
FX options -sold PUT	2 824 233	3 588 205	-	-
Spot-purchased	162 456	144 011	-	-
Spot-sold	162 876	143 917	-	-
Forward- purchased amounts	101 365	165 120	-	-
Forward- sold amounts	74 665	169 671	900	-
Capital derivatives contract - purchased	656 974	263 793	-	468 012

in thousands of PLN

Transactions with key management personnel

Remuneration of Bank Zachodni WBK Management Board Members, Supervisory Board Members and key management. Loans and advances made by the Bank to the key management personnel

As at 31.12.2016 and 31.12.2015 members of the Management Board were bound by the non-compete agreements which remain in force after they step down from their function. If a Member of the Management Board is removed from their function or not appointed for another term, he/she is entitled to a once-off severance pay. The severance pay does not apply if the person accepts another function in the Bank.

Loans and advances have been sanctioned on regular terms and conditions.

Remuneration of Management Board Members and Key Management	Management Board Members		Key Management	
	2016	2015	2016	2015
Remuneration	10 162	11 743	20 601	19 693
Additional benefits (e.g among others, life insurance cover without pension option, medical cover, accommodation, travel expenses and school fees)	894	973	877	1 462
The awards paid in 2016 and 2015 *	6 910	6 475	6 224	4 760
Equivalent paid for unused annual leave	199	1 056	108	209
Additional compensation for termination of the contract and the non-competition clause	1 092	1 108	-	-
Loans and advances made by the Bank to the Members of the Management Board/Key Management and to their relatives	7 158	5 160	25 694	21 898
Deposits from The Management Board and their relatives/Key management	13 312	16 091	14 199	17 654
Provisions for retirement benefits and provision for unused holidays in the amount	584	868	1 181	1 488
The number of conditional rights to shares	17 671	17 918	28 615	27 550

* included part of the award for 2015, 2014, 2013 and 2012 which was conditional and deferred in time

The category of key management personnel includes the persons covered by the principles laid down in the "Policy on variable components of remuneration paid to the individuals holding managerial positions at Bank Zachodni WBK".

BZ WBK Group applies the Policy on variable components of remuneration for individuals holding managerial positions in BZ WBK Group. The Policy has been approved by the bank's Management Board and Supervisory Board and is reviewed annually or each time significant organisational changes are made.

Persons holding managerial positions are paid variable remuneration once a year following the end of the settlement period and release of the bank's results. Variable remuneration is awarded in accordance with applicable bonus regulations and paid in cash and phantom stock. The latter shall represent min. 50% of the total amount of variable remuneration. Payment of min. 40% of variable remuneration referred to above is conditional and deferred for the period of three years (13.3% per annum). Variable remuneration is paid in arrears in equal annual instalments depending on individual performance in the period subject to assessment and the value of the phantom stock.

In 2016, the total remuneration paid to the Supervisory Board Members of Bank Zachodni WBK totalled PLN 1,712 k. Mr John Power received remuneration of PLN 35 k from subsidiaries for his membership in their Supervisory Boards.

In 2015, the total remuneration paid to the Supervisory Board Members of Bank Zachodni WBK totalled PLN 1,535 k. In addition, Mr John Power received remuneration for the supervision of the merger process of BZ WBK and Kredyt Bank on behalf of the Supervisory Board in the amount of PLN 1,050 k. Mr John Power received remuneration of PLN 31 k from subsidiaries for his membership in their Supervisory Boards.

47. Acquisitions and disposals of investments in subsidiaries

Acquisitions and disposals of investments in subsidiaries 2016 and 2015

Controlling stake at the companies PSA Finance sp. z o.o. and indirectly, PSA Consumer Finance sp. z o.o.

On 30.09.2016, Santander Consumer Bank (SCB), a subsidiary of Bank Zachodni WBK, and Banque PSA Finance entered into an agreement establishing strategic cooperation with regard to financing in Poland the vehicles manufactured by PSA Peugeot Citroen (PSA), financing the working capital requirements of the Polish PSA network and joint distribution of financial and banking products to the Polish customers of PSA. Under the above agreement, as of 1.10.2016 ("Change of Control Date"),

in thousands of PLN

Santander Consumer Finance (a subsidiary of SCB) purchased 50% shares of PSA Finance and, indirectly, PSA Consumer Finance for PLN 61,352,500. The price paid, which is a preliminary price, represents 50% of the reference book value of the acquired companies as agreed by the parties. The final price will be determined by the end of Q1 2017 and will depend on the outcome of the review of the acquired assets and liabilities carried out by the acquiring entity.

Registration of SC Poland Consumer 16-1 sp. z o.o.

On 17.05.2016, a subsidiary of Santander Consumer Bank trading as SC Poland Consumer 16-1 sp. z o.o. was registered. This is a special-purpose vehicle formed for the purpose of securitisation of a part of the credit portfolio, its shareholder being a Polish legal person that is not associated with the Group. As the control criteria set out in IFRS 10.7 are met, the company is considered as an entity controlled by Santander Consumer Bank.

A merger of BZ WBK Towarzystwo Funduszy Inwestycyjnych S.A. and BZ WBK Asset Management S.A. was completed, as a result of which BZ WBK TFI has acquired AM.

On 31.03.2016, a merger of BZ WBK Towarzystwo Funduszy Inwestycyjnych S.A. (BZ WBK TFI) and BZ WBK Asset Management S.A. (BZ WBK AM) was completed, as a result of which BZ WBK TFI has acquired AM.

The merger was executed by way of transfer of all assets of AM (the acquired company) to BZ WBK TFI (the acquiring company) in return for shares which BZ WBK TFI has allotted to the shareholders of the acquired company. The merger of the companies took effect on the date of entry of the merger into the register of businesses. Upon recording of the merger, AM has been deleted from the register of businesses. As of the merger date BZ WBK TFI has taken over all rights and obligations of its legal predecessor, i.e. AM. Business combinations under common control have no material impact on the financial statements.

Metrohouse Franchise S.A. shares sale transaction

On 22.01.2016, BZ WBK Inwestycje Sp. z o.o. sold all its shares of Metrohouse Franchise S.A. and ceased to be a shareholder of Metrohouse Franchise S.A.

Disposal of a shareholding in Lizar Sp. z o.o.

On 29.10.2015, BZ WBK Lease entered into an agreement with Poland Media Properties S.A. whereby it sold all its shares of Lizar Sp. z o.o. As a result, the company ceased to be a member of Bank Zachodni WBK Group.

Registration of SC Poland Consumer 15-1 sp. z o.o.

On 07.07.2015, a subsidiary of Santander Consumer Bank trading as SC Poland Consumer 15-1 sp. z o.o. was registered. This is a special-purpose vehicle formed for the purpose of securitisation of a part of the credit portfolio, its shareholder being a foreign legal person that is not associated with the Group. As the control criteria set out in IFRS 10.7 are met, the company is considered as an entity controlled by Santander Consumer Bank.

48. Employee benefits

Staff benefits include the following categories:

- Short-term benefits (remuneration, social security contributions, paid leaves, profit distributions and bonuses and non-cash benefits). Value of short-term employee benefits are undiscounted,
- Post-employment benefits (retirement benefits and similar payments, life insurance or medical care provided after the term of employment).

Within these categories, the Bank Zachodni WBK creates the following types of provisions:

Provisions for unused holidays

Liabilities related to unused holidays are stated in the expected amount (based on current salaries) without discounting.

Provisions for employee bonuses

Liabilities related to bonuses system are stated in the amount of the probable payment without discounting.

Provisions for retirement allowances

Based on internal regulations in respect to remuneration, the employees of the Bank are entitled to defined benefits other than remuneration:

in thousands of PLN

- a) retirement benefits,
- b) retirement pension.

The present value of such obligations is measured by an independent actuary using the projected unit credit method.

The amount of the retirement benefits and death-in-service benefits is dependent on length of service and amount of remuneration. The expected present value of the benefits is calculated, taking into account the financial discount rate and the probability of an individual get to the retirement age or die while working respectively. The financial discount rate is determined by reference to up-to-date market yields of government bonds. The probability of an individual get to the retirement age or die while working is determined using the multiple decrement model, taking into consideration the following risks: possibility of dismissal from service, risk of total disability to work and risk of death.

These defined benefit plans expose the Bank to actuarial risk, such as:

- interest rate risk – the decrease in market yields on government bonds would increase the defined benefit plans obligations,
- remuneration risk – the increase in remuneration of the Bank's employees would increase the defined benefit plans obligations,
- mobility risk – changes in the staff rotation ratio,
- longevity risk – the increase in life expectancy of the Bank's employees would increase the defined benefit plans obligations.

The principal actuarial assumptions as at 31.12. 2016 are as follows:

- the discount rate at the level of 3.6% (3.1% as at 31.12.2015),
- the future salary growth rate at the level of 2.0% (2.0% as at 31.12.2015),
- the probable number of leaving employees calculated on the basis of historical data concerning personnel rotation in the Bank,
- the mortality adopted in accordance with Life Expectancy Tables for men and women, published the Central Statistical Office, adequately adjusted on the basis of historical data of the Bank.

Reconciliation of the present value of defined benefit plans obligations

The following table presents a reconciliation from the opening balances to closing balances for the present value of defined benefit plans obligations.

	31.12.2016	31.12.2015
Balance as at 1 January	59 322	65 825
Current service cost	1 073	1 769
Interest expense	1 772	1 657
Actuarial (gains) and losses	(6 430)	(9 929)
Balance as at 31 December	55 737	59 322

Sensitivity analysis

The following table presents how the impact on the defined benefits obligations would have increased (decreased) as a result of a change in the respective actuarial assumptions by one percent as at 31.12.2016.

Defined benefit plan obligations	1 percent increase	1 percent decrease
Discount rate	10,86%	-11,94%
Future salary growth rate	-12,10%	9,51%

The following table presents how the impact on the defined benefits obligations would have increased (decreased) as a result of a change in the respective actuarial assumptions by one percent as at 31.12.2015

Defined benefit plan obligations	1 percent increase	1 percent decrease
Discount rate	12,26%	-13,51%
Future salary growth rate	-13,57%	12,42%

Other staff-related provisions

These are provisions for the National Fund of Rehabilitation of the Disabled, redundancies, overtime and staff training. These liabilities are stated at the amounts of expected payment without discounting.

The balances of the respective provisions are shown in the table below:

in thousands of PLN

Provisions	31.12.2016	31.12.2015
Provisions for unused holidays	51 700	51 700
Provisions for employee bonuses	195 663	200 014
Provisions for retirement allowances	55 737	59 322
Other staff-related provisions	8 587	7 964
Total	311 687	319 000

Detailed information about movements on staff-related provisions is available in Note 35.

49. Share based incentive scheme

On the 30th of June 2014, Annual General Meeting of the Shareholders of Bank Zachodni WBK S.A. implemented three-year Incentive Scheme no. V which participants are employees of the Bank Zachodni WBK Group (including Members of the Management Board), however not more than 500 individuals.

Vesting condition will be considered from two perspectives, separately for every year of operation of the scheme and on a cumulative basis after 3 years.

In every single year annual award not exceeding one third on total award will be considered. Shares will vest on a linear pattern between 25% and 100% contingent on profit after tax (PAT) growth. The range of the scale requires PAT growth between 7% and 11% in first year and between 17% and 26% in second and third year of duration of scheme.

Additionally, after 3 years cumulative award will be considered. Shares will vest on a linear pattern between 25% and 100% contingent on PAT compound annual growth rate in 3 years' time between 13.6% and 20.8%. If number of shares resulting from cumulative assessment will be higher than sum of annual awards vested to date, additional shares will be allocated to individuals up to the amount resulting from cumulative assessment.

Persons who are covered by the EU's regulations on variable remuneration components and have a significant impact on the risk profile of the Group are additionally required to achieve a stated RoRWA ratio in the respective years of the programme.

The Black Scholes model has been used to value awards granted at the grant date. The expected volatility of the values of shares is based on an analysis of historical volatility of share prices based on 160 sessions preceding the grant date. The following table details the assumptions used, and the resulting fair value.

Share based payments granted in 2014:

	2014
Number of share	177 336
Share price in PLN	363,30
Exercise price PLN	10
Vesting period	2,8 years
Expected volatility of share prices	26,40%
Award life	3 lata
Discount risk free rate	2,29%
Fair value per award	PLN 322,39
Dividend yield	2,75%

The following table summarizes the share based payments activity:

	12 months of 2016 based payments	12 months of 2015 based payments
Outstanding at 1 January	168 784	177 336
Granted	-	-
Exercised	-	-
Forfeited	(11 530)	(8 552)
Expired	-	-
Outstanding at 31 December	157 254	168 784
Exercisable at 31 December	-	-

Exercise price for all share based payments amounts to PLN 10.

For the share based payments outstanding as at 31.12.2016 and 31.12.2015 the average remaining contractual life is approximately 0.5 years and 1.5 year respectively.

in thousands of PLN

The total expense is recognized in profit and loss account for 12 months of 2016, 2015 increase of equity amounted to PLN 15,842 k, PLN 18,411 k respectively.

The table below presents information about the number of conditional rights to shares vested in BZ WBK Management Board members under the 5th Incentive Scheme. The rights may be exercised only in part depending on the future performance of the Group. Information about the rights exercised in full or in part will be provided in the future reports.

No. of awards	2016	2015
Outstanding at 1 January	17 918	24 073
Awarded before assumption of the duties of Management Board Member	1 253	2 500
Termination of appointment	(1 500)	(4 798)
Resignation from the Management Board President function	-	(3 857)
As at 31 December	17 671	17 918

The table below presents information about the number of conditional rights to shares vested in BZ WBK Key Management.

No. of awards	2016	2015
Outstanding at 1 January	27 550	25 293
Change due to inclusion in key management personnel	1 065	9 545
Change due to exclusion from key management personnel	-	(7 288)
As at 31 December	28 615	27 550

50. Dividend per share

As of the date of publication of this report, the Management Board of Bank Zachodni WBK has not finalised its analysis in respect of recommendation on dividend payout for 2016.

On 20.04.2016, the Annual General Meeting of Bank Zachodni WBK adopted a resolution to distribute the net profit of PLN 1,756,210 k in respect of 2015 as follows: PLN 702,484 k to be allocated to the dividend for shareholders, PLN 878,105 k to be allocated to the reserve capital and the remainder of PLN 175,621 k to be left undistributed and the Annual General Meeting of Bank Zachodni WBK allocated to the dividend for shareholders, the amount PLN 587,565 k from retained profit in the amount of PLN 952,652k generated by the Bank in the accounting year commenced on 01.01.2014 and ended on 31.12.2014. The remaining part PLN 365,087 k to be left undivided.

Dividend per share is PLN 13.

51. Operating segments reporting

Operating segments reporting were presented in "Consolidated Financial Statement of Bank Zachodni WBK Group for 2016" released on 17.02.2017.

52. Events which occurred subsequently to the end of the period

There were no major events subsequent to the end of the interim period.

**Signatures of Members of the Management Board**

Date	Name	Function	Signature
14.02.2017	Michał Gajewski	President	
14.02.2017	Andrzej Burliga	Member	
14.02.2017	Artur Chodacki	Member	
14.02.2017	Eamonn Crowley	Member	
14.02.2017	Michael McCarthy	Member	
14.02.2017	Carlos Polaino Izquierdo	Member	
14.02.2017	Juan de Porras Aguirre	Member	
14.02.2017	Marcin Prell	Member	
14.02.2017	Miroslaw Skiba	Member	
14.02.2017	Feliks Szyszkowiak	Member	

Signature of a person who is responsible for maintaining the book of account

Date	Name	Function	Signature
14.02.2017	Wojciech Skalski	Financial Accounting Area Director	