



ANNUAL REPORT 2017 **OF BANK ZACHODNI WBK GROUP**

2017



Bank Zachodni WBK

 Grupa Santander

Dear All,

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

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

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

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

Macroeconomic environment - we are on the rise

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

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

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

Banking sector ready for new challenges

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

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

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

Bank As You Want It

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

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

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

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

Through the “Bank As You Want It” strategy we want to be not only the best bank for the customers but also an innovator whose primary goal is to increase customers satisfaction with services and their loyalty as well as business partners of Bank Zachodni WBK Group.

Business effectiveness

Our financial performance confirms the effectiveness of our development strategy. In 2017, the gross profit of Bank Zachodni WBK Group totalled PLN 3,3bn, the underlying profit increased and the value of our assets exceeded PLN 152bn.

We enjoy a strong capital position, compliant with regulatory requirements. We have continued strict control over costs whose level has not changed yoy, despite investments in the future and development of the Group, and the C/I ratio for 2017 was 43.4%.

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

Positive performance is accompanied by growth in our customers’ trust and satisfaction. They have recognised and appreciated the Group’s digital transformation policy. This is evidenced by a 4,5% growth yoy in the number of active users in digital channel. In 2017, customers made over 23.5m transactions using the mobile banking channel which represents a 10.2m growth yoy (+76%). The number of credit products sold via remote channels (mobile, Internet, contact centre) surged by 36%.

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

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

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

Santander Consumer Bank Group, a part of Bank Zachodni WBK Group, also generated excellent results - its net profit was higher by 36% than a year ago and the sale of products financing the purchase of passenger cars increased considerably.

The Bank's subsidiaries are also in good condition. BZ WBK Leasing financed assets totalling PLN 4.2bn, of which financing machines and equipment accounted for nearly PLN 2bn, i.e. 18,8% up on last year. At the same time, the number of customers increased by 14%. BZ WBK Faktor was ranked second on the factoring market with a 12.6% share. Its turnover went up by 23% yoy while the loan portfolio increased by 25% yoy. BZ WBK TFI, thanks to excellent management and sales performance, assets under management rose in 2017 by PLN 2.6bn to PLN 16bn which translated into a growth in the retail market share to 10.38%.

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

In Santander Consumer Bank, Piotr Kończal took up the position of the President of the Management Board.

Corporate social responsibility

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

In 2017, Bank Zachodni WBK Group engaged in the following social projects: Jak Jeździsz (How's Your Driving), Santander Orchestra, Santander Universidades, Obsługa bez barier (Barrier-Free Banking), Bank Zachodni WBK Foundation and volunteering campaigns under which 580 of Bank's employees made a lasting difference.

Our commitment to the Customers

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

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

Michał Gajewski

President of Bank Zachodni WBK SA Management Board

FINANCIAL HIGHLIGHTS	PLN k		EUR k		
	for reporting period ended:	31.12.2017	31.12.2016	31.12.2017	31.12.2016
Consolidated financial statement of Bank Zachodni WBK Group					
I Net interest income		5 276 897	4 770 372	1 243 173	1 090 196
II Net fee and commission income		2 013 126	1 914 720	474 268	437 580
III Operating profit		3 700 772	3 453 821	871 857	789 319
IV Profit before tax		3 335 221	3 122 054	785 738	713 498
V Net profit attributable to owners of BZ WBK S.A.		2 213 054	2 166 847	521 369	495 200
VI Total net cash flows		(4 176 431)	(838 893)	(983 917)	(191 716)
VII Total assets		152 674 444	150 099 716	36 604 676	33 928 507
VIII Deposits from banks		2 783 083	2 561 281	667 262	578 951
IX Deposits from customers		111 481 135	112 522 457	26 728 316	25 434 552
X Total liabilities		129 330 815	129 081 240	31 007 892	29 177 495
XI Total equity		23 343 629	21 018 476	5 596 785	4 751 012
XII Non-controlling interests in equity		1 436 409	1 237 649	344 388	279 758
XIII Profit of the period attributable to non-controlling interests		305 460	217 245	71 963	49 648
XIV Number of shares		99 333 481	99 234 534		
XV Net book value per share in PLN/EUR		235,00	211,81	56,34	47,88
XVI Capital ratio		16,69%	15,05%		
XVII Profit per share in PLN/EUR		22,29	21,84	5,25	4,99
XVIII Diluted earnings per share in PLN/EUR		22,25	21,80	5,24	4,98
XIX Declared or paid dividend per share in PLN/EUR*		5,40	-	1,27	-

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

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

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

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



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

2017



Bank Zachodni WBK

 Grupa Santander

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In thousands of PLN

Consolidated income statement

for reporting period:		01.01.2017 31.12.2017	01.01.2016 31.12.2016
Interest income		6 529 307	6 060 920
Interest expenses		(1 252 410)	(1 290 548)
Net interest income	Note 6	5 276 897	4 770 372
Fee and commission income		2 526 814	2 388 464
Fee and commission expenses		(513 688)	(473 744)
Net fee and commission income	Note 7	2 013 126	1 914 720
Dividend income	Note 8	76 816	96 582
Net gains on subordinated entities	Note 49	3 757	100
Net trading income and revaluation	Note 9	194 974	280 820
Gains (losses) from other financial securities	Note 10	47 502	402 774
Other operating income	Note 11	150 587	140 764
Impairment losses on loans and advances	Note 12	(690 473)	(784 590)
Operating expenses incl.:		(3 372 414)	(3 367 721)
<i>Bank's staff, operating expenses and management costs</i>	Notes 13, 14	(2 939 432)	(2 935 229)
<i>Depreciation/amortisation</i>		(318 933)	(277 220)
<i>Other operating expenses</i>	Note 15	(114 049)	(155 272)
Operating profit		3 700 772	3 453 821
Share in net profits of entities accounted for by the equity method		58 264	55 439
Tax on financial institutions		(423 815)	(387 206)
Profit before tax		3 335 221	3 122 054
Corporate income tax	Note 16	(816 707)	(737 962)
Consolidated profit for the period		2 518 514	2 384 092
of which:			-
<i>attributable to owners of BZ WBK S.A.</i>		2 213 054	2 166 847
<i>attributable to non-controlling interests</i>		305 460	217 245
Net earnings per share (PLN/share)	Note 17		
Basic earnings per share		22,29	21,84
Diluted earnings per share		22,25	21,80

Consolidated statement of comprehensive income

for reporting period:		01.01.2017 31.12.2017	01.01.2016 31.12.2016
Consolidated profit for the period		2 518 514	2 384 092
Other comprehensive income which can be transferred to the profit and loss account:		452 578	(510 064)
Available-for sale financial assets valuation, gross		533 774	(738 327)
Deferred tax		(101 417)	140 282
Cash flow hedges valuation, gross		24 964	108 618
Deferred tax		(4 743)	(20 637)
Other comprehensive income which can't be transferred to the profit and loss account		(7 622)	5 556
Provision for retirement allowances – actuarial gains/losses, gross		(9 410)	6 859
Deferred tax		1 788	(1 303)
Other comprehensive income for the period, net of income tax		444 956	(504 508)
TOTAL COMPREHENSIVE INCOME FOR THE PERIOD		2 963 470	1 879 584
Attributable to:			
<i>owners of BZ WBK S.A.</i>		2 651 427	1 666 087
<i>non-controlling interests</i>		312 043	213 497

Notes presented on pages 8 – 114 constitute an integral part of this Financial Statement.

In thousands of PLN

Consolidated statement of financial position

	as at:	31.12.2017	31.12.2016
ASSETS			
Cash and balances with central banks	Note 18	4 146 222	4 775 660
Loans and advances to banks	Note 19	2 136 474	3 513 278
Financial assets held for trading	Note 20	3 416 108	3 180 985
Hedging derivatives	Note 21	218 061	67 645
Loans and advances to customers	Note 22	107 839 897	103 068 538
Financial assets available for sale	Note 23	28 415 812	29 307 878
Investments in associates	Note 24	889 372	871 491
Intangible assets	Note 25	490 327	486 762
Goodwill	Note 26	1 712 056	1 688 516
Property, plant and equipment	Note 27	930 717	878 298
Net deferred tax assets	Note 28	1 414 227	1 534 322
Assets classified as held for sale	Note 29	103	629
Other assets	Note 30	1 065 068	725 714
Total assets		152 674 444	150 099 716
LIABILITIES AND EQUITY			
Deposits from banks	Note 31	2 783 083	2 561 281
Hedging derivatives	Note 21	578 798	2 023 344
Financial liabilities held for trading	Note 20	1 237 704	1 809 060
Deposits from customers	Note 32	111 481 135	112 522 457
Sell-buy-back transactions	Note 42	2 650 846	1 632 613
Subordinated liabilities	Note 33	1 488 602	440 457
Debt securities in issue	Note 34	5 895 814	5 529 187
Current income tax liabilities		192 925	84 151
Provisions	Note 35	153 134	130 128
Other liabilities	Note 36	2 868 774	2 348 562
Total liabilities		129 330 815	129 081 240
Equity			
Equity attributable to owners of BZ WBK		21 907 220	19 780 827
Share capital	Note 37	993 335	992 345
Other reserve capital	Note 38	16 920 129	15 791 555
Revaluation reserve	Note 39	714 466	276 093
Retained earnings		1 066 236	553 987
Profit for the current period		2 213 054	2 166 847
Non-controlling interests in equity	Note 40	1 436 409	1 237 649
Total equity		23 343 629	21 018 476
Total liabilities and equity		152 674 444	150 099 716

Notes presented on pages 8 – 114 constitute an integral part of this Financial Statement.

In thousands of PLN

Consolidated statement of changes in equity

Consolidated statement of changes in equity	Equity attributable to equity holders of BZ WBK SA				Total	Non-controlling interests in equity	Total equity
	Share capital	Other reserve capital	Revaluation reserve	Retained earnings and profit for the period			
Note	37	38	39			40	
Opening balance as at 31.12.2016	992 345	15 791 555	276 093	2 720 834	19 780 827	1 237 649	21 018 476
Total comprehensive income	-	-	438 373	2 213 054	2 651 427	312 043	2 963 470
<i>Consolidated profit for the period</i>	-	-	-	2 213 054	2 213 054	305 460	2 518 514
<i>Other comprehensive income</i>	-	-	438 373	-	438 373	6 583	444 956
Issue of shares	990				990		990
Distributions of profits and losses	-	1 123 497	-	(1 123 497)	-	-	-
Share scheme charge	-	(2 512)			(2 512)	-	(2 512)
Dividends	-	-	-	(535 866)	(535 866)	(110 962)	(646 828)
Equity adjustment due to merger and liquidation of subsidiaries and controlling stake at the subsidiaries	-	7 589	-	4 765	12 354	(2 321)	10 033
As at 31.12.2017	993 335	16 920 129	714 466	3 279 290	21 907 220	1 436 409	23 343 629

The revaluation reserve of PLN 714,466k comprises valuation of debt securities of PLN 245,104k, equity shares of PLN 557,499k, cash flow hedges of PLN (88,574)k and the provision for retirement allowances with cumulative actuarial gains of PLN 437k.

Consolidated statement of changes in equity	Equity attributable to equity holders of BZ WBK SA				Total	Non-controlling interests in equity	Total equity
	Share capital	Other reserve capital	Revaluation reserve	Retained earnings and profit for the period			
Note	37	38	39			40	
Opening balance as at 31.12.2015	992 345	14 685 919	776 914	2 936 851	19 392 029	1 176 101	20 568 130
Total comprehensive income	-	-	(500 760)	2 166 847	1 666 087	213 497	1 879 584
<i>Consolidated profit for the period</i>	-	-	-	2 166 847	2 166 847	217 245	2 384 092
<i>Other comprehensive income</i>	-	-	(500 760)	-	(500 760)	(3 748)	(504 508)
Distributions of profits and losses	-	1 177 730	-	(1 177 730)	-	-	-
Share scheme charge	-	16 213	-	-	16 213	-	16 213
Dividends	-	-	-	(1 290 049)	(1 290 049)	(226 025)	(1 516 074)
Equity from acquisition of controlling interest in PSA Finanse sp. z o.o. and PSA Consumer Finanse sp. z o.o.	-	-	-	-	-	74 076	74 076
Settlement on account of merger of subsidiaries and other	-	(88 307)	(61)	84 915	(3 453)	-	(3 453)
As at 31.12.2016	992 345	15 791 555	276 093	2 720 834	19 780 827	1 237 649	21 018 476

The revaluation reserve of PLN 276,093k comprises valuation of debt securities of PLN (145,039)k, equity shares of PLN 521,877k, cash flow hedges of PLN (108,768)k and the provision for retirement allowances with cumulative actuarial gains of PLN 8,023k.

Notes presented on pages 8 – 114 constitute an integral part of this Financial Statement.

In thousands of PLN

Consolidated statement of cash flows

	for the period	01.01.2017- 31.12.2017	01.01.2016- 31.12.2016
Profit before tax		3 335 221	3 122 054
Total adjustments:			
Share in net profits of entities accounted for by the equity method		(58 264)	(55 439)
Depreciation/amortisation		318 933	277 220
Impairment losses		8 765	22 077
Profit from investing activities		(62 297)	(417 631)
		3 542 358	2 948 281
Changes:			
Provisions		23 006	(2 442)
Trading portfolio financial instruments		(1 506 362)	957 785
Hedging derivatives		(1 594 962)	40 671
Loans and advances to banks		(95)	4 589
Loans and advances to customers		(4 771 359)	(8 154 654)
Deposits from banks		110 032	164 897
Deposits from customers		(781 067)	10 336 381
Buy-sell/ Sell-buy-back transactions		1 018 233	(3 608 458)
Other assets and liabilities		277 134	683 114
		(7 225 440)	421 883
Interest accrued excluded from operating activities		(414 692)	(436 651)
Dividend		(76 270)	(96 051)
Paid income tax		(693 049)	(1 016 330)
Net cash flows from operating activities		(4 867 093)	1 821 132
Inflows		4 461 677	6 069 162
Sale of subordinated entities		-	100
Sale/maturity of financial assets available for sale		3 673 594	5 327 990
Sale of intangible assets and property, plant and equipment		45 342	26 800
Dividend received		76 270	95 903
Interest received		666 471	618 369
Outflows		(4 206 618)	(10 406 768)
Purchase of subordinated entities net of cash acquired		-	(61 197)
Purchase of financial assets available for sale		(3 792 409)	(9 991 588)
Purchase of intangible assets and property, plant and equipment		(414 209)	(353 983)
Net cash flows from investing activities		255 059	(4 337 606)
Inflows		4 983 948	6 037 678
Debt securities in issue		3 562 288	2 762 880
Proceeds from issuing/shares		990	-
Drawing of loans		1 420 670	3 274 798
Outflows		(4 548 345)	(4 360 097)
Debt securities buy out		(2 095 000)	(1 554 700)
Repayment of loans		(1 568 408)	(1 108 976)
Dividends and other payments to shareholders		(646 828)	(1 516 074)
Interest paid		(238 109)	(180 347)
Net cash flows from financing activities		435 603	1 677 581
Total net cash flows		(4 176 431)	(838 893)
Cash and cash equivalents at the beginning of the accounting period		11 838 799	12 677 692
Cash and cash equivalents at the end of the accounting period		7 662 368	11 838 799

Cash and cash equivalents are presented in Note 47.

Information regarding liabilities arising from financial activities in loans received, subordinated liabilities and the issue of debt securities were presented respectively in notes 31-34.

Notes presented on pages 8 – 114 constitute an integral part of this Financial Statement.

In thousands of PLN

Additional notes to consolidated financial statement

1. General information about issuer

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

Consolidated financial statements of Bank Zachodni WBK S.A. Capital Group (further: BZ WBK Group) includes Bank's Zachodni WBK S.A. stand-alone financial information as well as information from its subsidiaries (all together called Group) and shares in associated entities.

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

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

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

In thousands of PLN

BZ WBK Group consists of the following entities:

Subsidiaries:

Subsidiaries	Registered office	% of votes on AGM 31.12.2017	% of votes on AGM 31.12.2016
1. BZ WBK Finanse sp. z o.o.	Poznań	100.00	100.00
2. BZ WBK Faktor sp. z o.o.	Warszawa	100% of AGM votes are held by BZ WBK Finanse sp. z o.o.	100% of AGM votes are held by BZ WBK Finanse Sp. z o.o.
3. BZ WBK Leasing S.A. ¹⁾	Poznań	100% of AGM votes are held by BZ WBK Finanse sp. z o.o.	100% of AGM votes are held by BZ WBK Finanse Sp. z o.o.
4. BZ WBK Lease S.A. ¹⁾	Warszawa	-	100% of AGM votes are held by BZ WBK Finanse Sp. z o.o.
5. BZ WBK Inwestycje sp. z o.o.	Poznań	100.00	100.00
6. Gieldokracja sp. z o.o. w likwidacji	Poznań	100.00	100.00
7. BZ WBK F24 S.A. / BZ WBK Nieruchomości S.A. ²⁾	Poznań	100% of AGM votes are held by BZ WBK Finanse sp. z o.o.	99.99
8. BZ WBK Towarzystwo Funduszy Inwestycyjnych S.A. ³⁾	Poznań	50.00	50.00
9. Santander Consumer Bank S.A.	Wrocław	60.00	60.00
10. Santander Consumer Finanse sp. z o.o.	Wrocław	100% of AGM votes are held by Santander Consumer Bank S.A.	100% of AGM votes are held by Santander Consumer Bank S.A.
11. PSA Finance Polska sp. z o.o. ⁴⁾	Warszawa	50% of AGM votes are held by Santander Consumer Bank S.A. and 50% of AGM votes are held by Banque PSA Finance S.A.	50% of AGM votes are held by Santander Consumer Bank S.A. and 50% of AGM votes are held by Banque PSA Finance S.A.
12. PSA Consumer Finance Polska sp. z o.o. ⁴⁾	Warszawa	100% of AGM votes are held by PSA Finance Polska sp. z o.o.	100% of AGM votes are held by PSA Finance Polska Sp. z o.o.
13. Santander Consumer Multirent sp. z o.o.	Wrocław	100% of AGM votes are held by Santander Consumer Bank S.A.	100% of AGM votes are held by Santander Consumer Bank S.A.
14. AKB Marketing Services Sp. z o.o. ⁵⁾	Poznań	-	100% of AGM votes are held by Santander Consumer Bank S.A.
15. S.C. Poland Consumer 15-1 sp.zo.o. ⁶⁾	Warszawa	subsidiary of Santander Consumer Bank S.A.	subsidiary of Santander Consumer Bank S.A.
16. S.C. Poland Consumer 16-1 sp.zo.o. ⁶⁾	Warszawa	subsidiary of Santander Consumer Bank S.A.	subsidiary of Santander Consumer Bank S.A.

^{1,1)} Details about the merger of BZ WBK Leasing S.A. and BZ WBK Lease S.A. are provided in Note 49.

²⁾ On 18.10.2017, BZ WBK Nieruchomości S.A. with its registered office in Zakrzewo changed name to BZ WBK F24 SPÓŁKA AKCYJNA with its registered office in Poznań. On 24.11.2017, BZ WBK S.A. made contribution in kind of BZWBK F24 S.A. (formerly BZ WBK Nieruchomości S.A.) shares to BZWBK Finanse sp. z o.o. to cover the acquisition of BZWBK Finanse sp. z o.o. shares by BZWBK S.A. On 12.01.2018, in the Nation Court Register was registered increase of share capital BZWBK Finanse sp. z o.o. to PLN 1,630k. Share capital was fully paid.

³⁾ As at 30.09.2017, Bank Zachodni WBK was a co-owner of BZ WBK Towarzystwo Funduszy Inwestycyjnych S.A., together with Banco Santander S.A. Both owners are members of Santander Group and each holds an equal stake of 50% in the company's share capital. Bank Zachodni WBK exercises control over BZ WBK Towarzystwo Funduszy Inwestycyjnych S.A. Consequently, the company is treated as a subsidiary.

⁴⁾ Details about the controlling stake at the companies PSA Finance Polska sp. z o.o. and indirectly, PSA Consumer Finance Polska sp. z o.o. are provided in Note 2 and 50.

⁵⁾ Details about the liquidation of AKB Marketing Services sp. z o.o. in liquidation are provided in Note 49.

⁶⁾ SC Poland Consumer 16-1 sp. z o.o. set up for the purpose of securitisation of a part of the loan portfolio; its shareholder is polish legal entity who has no ties with the Group; the company is controlled by Santander Consumer Bank, in accordance with the control criteria set out in IFRS 10.7.

In thousands of PLN

Associates:

Associates	Registered office	% of votes on AGM 31.12.2017	% of votes on AGM 31.12.2016
1. POLFUND - Fundusz Poręczeń Kredytowych S.A.	Szczecin	50.00	50.00
2. BZ WBK - Aviva Towarzystwo Ubezpieczeń Ogólnych S.A.	Poznań	49.00	49.00
3. BZ WBK - Aviva Towarzystwo Ubezpieczeń na Życie S.A.	Poznań	49.00	49.00

2. Basis of preparation of consolidated financial statement

2.1. Statement of compliance

This annual consolidated financial statement of BZ WBK Group 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 December 2017 and, in the case of matters not governed by the above Standards, in accordance with the provisions of the Accounting Act of 29 September 1994 (consolidated text: Journal of Law of 22 November 2017, item 2342, as amended) and related implementing acts as well as the requirements imposed on issuers whose securities are admitted to trading on regulated markets or issuers who have applied to have securities admitted to trading on regulated markets outlined in Act dated 29 July 2005 on Public Offering, on Conditions for the Introduction of Financial Instruments to the Organized Trading System and on Public Companies.

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

In thousands of PLN

2.2. New standards and interpretations or changes to existing standards or interpretations which can be applicable to BZ WBK Group and are not yet effective or have neither been implemented earlier

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

In thousands of PLN

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

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

In thousands of PLN

IFRS 9 Financial Instruments

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

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

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

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

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

Classification and measurement

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

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

Business models

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

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

Qualitative criteria are assessed by the key management personnel of the units which are members of BZ WBK Group. The following aspects are taken into account during the assessment:

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

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

In thousands of PLN

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

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

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

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

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

Contractual cash flows test

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

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

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

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

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

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

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

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

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

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

In thousands of PLN

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

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

Identified changes in classification and measurement

In order to ensure correct classification and measurement of the financial assets held as at 31 December 2017, BZ WBK Group analysed its assets portfolios whereby it:

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

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

- profit sharing agreements identified in certain tranches of debt instruments that have additional cash flows, other than solely payments of principal and interest, representing a contractually determined share in the customer's profit or loss. The adjustment to the fair-value measurement has been set at PLN (64 726) k, without the deferred tax effect.
- financial instruments whose contractual cash flows are not payments of principal and interest, which applies to debt instruments classified as "Loans and advances" whose interest is accrued on the subscription price and capitalised over the life of the product (until maturity) whereas interest payments to BZ WBK Group will be calculated on the nominal price so these cash flows do not represent interest payments as defined in IFRS 9. The adjustment to the fair-value measurement has been set at PLN (15,897)k and unsettled provision amounted PLN (106) k without the deferred tax effect,
- a different recognition method for interest income from assets held, depending on the level of credit risk. Until the end of 2017, the interest income from exposures measured at amortised cost, for which IBNR impairment charge was calculated, was recognised at the net carrying amount, whereas from 1 January 2018 at the gross carrying amount of the exposure. IFRS 9 provides for two exceptions from this rule:
 - a) POCI (Purchased or Originated Credit Impaired) assets. The interest income from these exposures is calculated on the net carrying amount based on the credit risk-adjusted effective interest rate.
 - b) financial assets impaired after the initial recognition (stage 3) The interest income from these exposures is calculated based on the effective interest rate and the net carrying amount.

Considering the differences in the recognition of interest income from financial assets classified into stages 1 and 2, for which until end of 2017 the IBNR provision charge was calculated, on the effective date of IFRS 9, BZ WBK Group recognised an interest income adjustment of PLN (23,787) k without deferred tax effect.

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

Using the option permitted by IFRS 9, BZ WBK Group took an irrevocable decision to designate strategic equity investments from the portfolio of financial assets other than those held for trading as instruments measured at fair value through other comprehensive income. The equity investments for which BZ Group chose the option of fair value measurement through other comprehensive income were acquired to be maintained in the investment portfolio for a long term and strategically, without the intention to make a profit on selling them in the short or medium term. If the equity instrument designated to be measured at fair value through other comprehensive income is sold, the gain (loss) on the transaction is not recycled to profit or loss at the time of the sale. The

In thousands of PLN

adjustment to the fair-value measurement of equity instruments has been set at PLN (17,078) k and amount of reversed impairment charges at PLN 1,984 k, without the deferred tax effect.

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

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

Comparative data

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

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

Hedge accounting

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

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

For this reason, implementation of IFRS 9 will have no impact on the financial position of BZ WBK Group with regard to hedge accounting.

Impairment of credit exposures

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

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

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

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

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

- qualitative:

In thousands of PLN

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

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

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

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

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

The implementation of IFRS 9 requirements caused increase in impairment losses in BZ WBK Group. The total value of additional impairment charges recognised in retained earnings for previous years is PLN 193,864 k, without the deferred tax effect, of which PLN 240,637 k relates to balance sheet items, PLN 15,034 k the increase in provisions for off-balance sheet liabilities presented in the line "Provisions" and the reclassifications of financial instruments from the category of assets measured at amortized cost to measured at fair value through profit or loss triggered impairment charge reversal in the amount of PLN 61,807 k.

In addition, BZ WBK Group expects higher volatility of impairment charges due to changes in the classification of exposures between stage 1 and 2 and material changes in the coverage of the exposure resulting in write-offs due to different horizons for recognizing expected losses. An important element affecting the volatility of estimates is also the use of macroeconomic forecasts in the calculation expected credit losses.

Impact of IFRS 9 on financial position

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

Item	Measurement category – IAS 39	Measurement category – IFRS 9	Carrying amount – IAS 39	IFRS 9 implementation impact * Classification and measurement impact	IFRS 9 implementation impact * Impairment impact	Carrying amount – IFRS 9
ASSETS						
Loans and advances to customers	Amortised cost	Amortised cost	107 715 574	(23 787)	(240 637)	107 451 150
Loans and advances to customers	Amortised cost	Fair value through profit or loss	124 323	(80 729)	61 807	105 401
Financial assets available for sale	Historic cost/purchase price less impairment charges	Fair value through OCI	52 157	(17 078)	1 984	37 063
Total assets			107 892 054	(121 594)	(176 846)	107 593 614

* without deferred tax effect

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

In thousands of PLN

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

Item	Measurement category	Measurement category	Carrying amount	IFRS 9 implementation impact * Classification and measurement impact	IFRS 9 implementation impact * Impairment impact	Carrying amount – IFRS 9
LIABILITIES						
Provisions	IAS 37	IFRS 9	50 652	-	15 034	65 686
Total liabilities			50 652	-	15 034	65 686

* - without deferred tax effect

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

As at 1 January 2018, the total value of the impact of IFRS 9 implementation PLN (313,474) k, and the deferred tax effect in the form of deferred net tax asset increase PLN 59,020 k decreased the balance of retained earnings and revaluation reserve by the amount of PLN (254,454) k.

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

Impact of IFRS 9 on capital adequacy

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

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

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

In thousands of PLN

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

As a result of the adjustment of the regulatory capital requirements calculation, which include transitional arrangements for mitigating the impact of the introduction of IFRS 9 referred in the Regulation (EU) 2017/2395 of the European Parliament and of the Council of 12 December 2017, the Tier 1 capital ratio and total capital ratio on BZ WBK Group level decreased by 2 bps. In the case of non-application of the transitional arrangements related to IFRS 9 specified in this regulation and taking into account the full impact of the implementation of IFRS 9, the above-mentioned ratios would decrease by 20 bps.

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

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

IFRS 15 Revenue from Contracts with Customers

Description of changes

IFRS 15 *Revenue from Contracts with Customers* was published on 28 May 2014 by the International Accounting Standards Board and applies to annual reporting periods beginning on or after 1 January 2018.

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

As of 1 January 2018, IFRS 15 replaces the following standards and interpretations:

- IAS 18 Revenue
- IAS 11 Construction contracts
- SIC-31 Revenue - Barter Transactions Involving Advertising Services
- IFRIC 13 Customer Loyalty Programmes
- IFRIC 15 Agreements for the Construction of Real Estate
- IFRIC 18 Transfers of Assets from Customers

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

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

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

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

- over time or
- at a point in time.

The core principle of IFRS 15 is that an entity will recognise revenue to depict the transfer of promised assets to customers in an amount that reflects the consideration to which BZ WBK Group expects to be entitled in exchange for those assets.

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

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

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

In thousands of PLN

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

- the contract has been approved in writing, orally, or in accordance with other customary business practices and the parties are committed to perform their obligations in the contract,
- BZ WBK Group can identify each party's rights regarding the assets to be transferred,
- BZ WBK Group can identify payment terms for the assets to be transferred,
- the contract has commercial substance (i.e. the risk, timing or amount of the vendor's future cash flows to BZ WBK Group are expected to change as a result of the contract),
- it is probable that BZ WBK Group will collect the consideration to which it will be entitled in exchange for the assets that will be transferred to the customer. In evaluating whether collectability of an amount of consideration is probable, BZ WBK Group shall consider only the customer's ability and intention to pay that amount of consideration when it is due.

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

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

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

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

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

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

Factors that indicate that BZ WBK Group promise to transfer an asset to a customer is separately identifiable include, but are not limited to, the following:

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

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

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

In thousands of PLN

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

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

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

According to BZ WBK Group, the indicators of the transfer of control include the following:

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

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

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

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

BZ WBK Group applies IFRS 15 starting from 1 January 2018.

Status

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

- revenue from advisory services
- revenue from the sale of fixed assets used for operational activities or repossessed, which are presented together with cost of assets sold as the result on sale in line "Other operating income"

In thousands of PLN

- loyalty programmes,
- success fee - i.e. contracts which do not guarantee the remuneration for BZ WBK Group or provide for the minimum level of remuneration during the term of the contract until a certain condition is met (e.g. a transaction is finalised), entitling BZ WBK Group to receive significant remuneration to compensate for the effort made by BZ WBK Group in a long term.
- revenue from asset management
- revenue from the sale of insurance products which show indications of a connection with financial instruments to an extent not covered by separate standards, and
- costs of contracts with customers.

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

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

Impact of IFRS 15 on the financial standing and own funds

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

IFRS 16 Leases

Description of changes

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

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

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

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

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

The new standard presents the overall model for identification and accounting for leases in financial statements of lessors and lessees. Significant changes have been introduced to lessee accounting, e.g. the distinction between operating and finance lease is no longer applied. For the purpose of identification of leases, IFRS 16 introduces a control model which differentiates between leases and service agreements depending on the existence of an asset controlled by the lessee.

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

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

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

In thousands of PLN

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

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

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

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

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

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

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

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

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

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

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

Status

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

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

- buildings and commercial units
- land and perpetual usufruct of land

In thousands of PLN

- vehicles and
- technical equipment.

BZ WBK Group plans to apply two exemptions regarding:

- short-term leases (whose term is 12 months or less and which do not contain purchase option) and
- low-value assets (assets with the initial value of PLN 17,000 or less).

by taking them directly to costs, usually on a straight-line basis, over the lease term.

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

In addition, at the date of first adoption of the standard, BZ WBK Group plans to use additional simplifications available for first-time adopters, specifically:

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

Estimated impact of IFRS 16 on BZ WBK Group

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

The value of lease payments by their maturity dates as at 31 December 2017 is presented in Note 46.

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

IFRS	Nature of changes	1 January 2018	Influence on BZ WBK Group
Amendments to IAS 7 Statement of Cash Flows	Amendments to IAS 7 introduce the requirements to disclose changes in liabilities arising from financing activities in statement of cash flows, including both changes arising from cash flows and non-cash changes. To fulfill the requirement the standard requires a reconciliation between the opening and closing balances in the statement of financial position for liabilities arising from financing activities in cash flow statement.	1 January 2017	Reconciliation of changes in liabilities arising from financing activities are presented in notes 31-34.
Amendment to IAS 12 Income Taxes	Amendments to IAS 12 clarify the requirements on recognition of deferred tax assets for unrealized losses on debt instruments measured at fair value. The amendments introduce the guidance on the identification of deductible temporary differences. Especially the standard confirms that decreases below cost in the carrying amount of a fixed-rate debt instrument measured at fair value for which the tax base remains at cost give rise to a deductible temporary difference. This applies irrespective of whether the debt instrument's holder expects to use it or sale it.	1 January 2017	The amendments does not have any material impact on the financial statements.
Annual Improvements to IFRS 2014-2016*	In December 2016, the International Accounting Standards Board published 'Annual Improvements to IFRS Standards 2014-2016 Cycle' which amended 3 standards, i.e. IFRS 12 'Disclosure of Interests in Other Entities', IFRS 1 'First-time Adoption of International Financial Reporting Standards' and IAS 28 'Investments in Associates'. The improvements feature guidelines and amendments re: the scope of applicability, recognition and valuation as well as terminology and editing changes.	1 January 2017 for improvements to IFRS 12	The amendment did not have a significant impact on financial statements.

In thousands of PLN

2.4. Basis of preparation

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

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

2.5. Use of estimates and judgments

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

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

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

2.6. Main estimates and judgments made by the BZ WBK Group

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 BZ WBK Group 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 BZ WBK Group 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 impairment charges for loans receivables are independently monitored by head office personnel on a regular basis. A group-wide system for grading advances according to agreed credit criteria exists 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 BZ WBK Group. 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 the customers classified to global corporate banking segment, customers with a commercial grading, property customers and local authorities, and for significant retail exposures (individual analysis);
- with reference to the portfolio of individually insignificant credit exposures (collective analysis) or individually significant exposures, but with no identified indications of impairment.

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

Net impairment losses on loans and advances are presented in Note 12.

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

Impairment loss on non-financial assets

The valuation of the fixed-assets of the BZ WBK Group is reviewed as 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.

In thousands of PLN

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

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

The value of impairment losses on individual tangible and intangible fixed assets is presented in Notes 25 and 27.

Fair value of financial instruments

Some of the BZ WBK Group's financial instruments are carried at fair value, including all derivatives, other financial assets at fair value through profit and loss and financial investments classified as available for sale. Financial instruments are either priced with reference to a quoted market price for that instrument or 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 BZ WBK Group takes into account the need to identify additional adjustments to the fair value of the counterparty credit risk.

A summary of the carrying amounts and fair values of the individual groups of assets and liabilities is presented in Note 43.

Consolidation scope

The preparation of consolidated financial statements by Bank Zachodni WBK as a parent entity of BZ WBK Group requires an extensive use of judgement and multiple assumptions as to the nature of equity investments, including, above all, determination of whether Bank Zachodni WBK S.A. as a parent entity exercises control over the investee. Presented below are the key judgements and assumptions regarding the bank's equity investments where the bank has 50% voting rights in the investee.

According to the Management Board of BZ WBK Group, investment in BZ WBK Towarzystwo Funduszy Inwestycyjnych S.A. is an investment in a subsidiary for the purpose of preparation of the consolidated financial statement in the light of the strategy adopted by the ultimate parent entity. As at 31 December 2017, Bank Zachodni WBK S.A. co-owns BZ WBK Towarzystwo Funduszy Inwestycyjnych S.A. with Banco Santander S.A. Both owners are members of Santander Group and each holds 50% of the shares in the company. In practice, Bank Zachodni WBK S.A. exercises control over the subsidiary company, BZ WBK Towarzystwo Funduszy Inwestycyjnych S.A. due to the fact that:

- Bank Zachodni WBK S.A. has rights to manage significant current operations,
- Bank Zachodni WBK S.A. has rights to variable returns due to its exposure,
- Bank Zachodni WBK may use its powers to affect the amount of its financial results.

The investment in POLFUND - Fundusz Poręczeń Kredytowych S.A., where 50% of the voting rights are held by the Bank Zachodni WBK S.A. on Annual General Meeting, was classified, in accordance with the best knowledge and estimates, as an investment in an associate as the ownership structure does not allow Bank Zachodni WBK S.A. to control and to joint-control the company.

According to BZ WBK Group Management Board, investing in PSA Finance Polska Sp. z o.o., a subsidiary company, resulted from the need to draft consolidated financial statements due to the fact that Santander Consumer Bank S.A. has a direct control and Bank Zachodni WBK S.A. has indirect control over the investment. The need of controlling the company results from the fact that:

– Santander Consumer Bank S.A. exercises control over PSA Finance Polska Sp. z o.o. as it has existing rights that give it the current ability to direct the relevant activities, namely the activities which materially influence the returns made by PSA Finance Polska Sp. z o.o.. Taking into account the core business of PSA Finance Polska Sp. z o.o., which is leasing, activities supporting financial services, car lease and rental and activities of insurance agents and brokers, and the sector in which PSA Finance Polska Sp. z o.o. is active, Bank Zachodni WBK S.A. has decided that PSA Finance Polska Sp. z o.o. relevant activities are:

- funding and ALM activity;
- risk management activity
- commercial activity.

On the basis of an analysis of written agreements between the shareholders of PSA Finance Polska Sp. z o.o., Santander Consumer Bank S.A. manages the first two types of activities indicated above, namely the activity connected with the provision of funding and risk management. The right to manage those activities results from the fact that committee members appointed by Santander Consumer Bank S.A. have casting votes in the event of a tied vote, and the fact that Santander Consumer Bank S.A. has the right to shape the company's external funding policy in a manner consistent with the internal rules of Santander Consumer Bank S.A.

– As Santander Consumer Bank S.A. plays a key role in funding the activities of PSA Finance Polska Sp. z o.o., the former is exposed to variable returns from its investment into the investee and

In thousands of PLN

– Santander Consumer Bank S.A. may use its power to affect returns from its investment into PSA Finance Polska Sp. z o.o. as the former does not act for or on behalf of another entity (acts as a principal rather than as an agent).

The list of fully consolidated subsidiaries is presented in note 1 “Information about the issuer”.

Revenues arising from insurance mediation

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

BZ WBK Group performs the link assessment:

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

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

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

Classification of leases

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

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

Note 46 presents gross receivables in respect of finance leases by maturity dates, present value of due minimum lease payments by maturity dates, reconciliation of differences between finance lease receivables and the present value of due minimum lease payments, and operating lease payments by maturity dates.

Economic life of intangible and tangible fixed assets

At initial recognition of an intangible or tangible fixed asset, BZ WBK Group determines their estimated economic life.

For the purpose of this process, BZ WBK Group takes into account in particular:

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

Economic life of fixed assets is periodically reviewed by BZ WBK Group.

Other accounting estimates and judgements

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 51 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 BZ WBK Group assesses probability of the programme vesting which affects the programme value in the costs of the reporting period. Description of the share-based incentive scheme is contained in Note 52.

Provisions for legal claims have been estimated considering the expected loss arising on individual cases. Provisions for cases disputed in court are presented in Note 35.

In thousands of PLN

Changes in judgments and estimates

In 2017, the scope of data covered by estimates did not change in comparison with the consolidated financial statements of BZ WBK Group's for 2016 with the exception of those listed above.

2.7. Basis of consolidation

Subsidiaries

Bank Zachodni WBK S.A. defines the consolidation scope by assessing whether it controls an investee. Bank Zachodni WBK S.A. controls an entity if, due to its involvement, Bank Zachodni WBK S.A. is exposed or has rights to variable returns and can affect those returns through its power over the investee.

Bank Zachodni WBK S.A., being the parent entity, controls directly or indirectly an investee when:

- Bank Zachodni WBK S.A. has power over the investee;
- Bank Zachodni WBK S.A. has exposure or rights to variable returns from its involvement with the investee;
- Bank Zachodni WBK S.A. has the ability to use its power over the investee to affect the amount of the investor's financial results.

When assessing whether it controls an investee, Bank Zachodni WBK S.A. considers all facts and circumstances, among other things following factors:

- the purpose and design of the investee;
- what the relevant activities are and how decisions about those activities are made;
- whether the rights of Bank Zachodni WBK S.A. give it the current ability to direct the relevant activities;
- whether Bank Zachodni WBK S.A. is exposed or has rights to variable returns from its involvement with the investee;
- whether Bank Zachodni WBK S.A. has the ability to use its power over the investee to affect the amount of the investor's returns.

The financial statements of subsidiaries are included in the consolidated financial statements from the date that control commences until the date that control ceases.

Purchase method

BZ WBK Group applies the purchase method to account for acquisition of subsidiaries. Under this method, the acquirer has to:

- recognise and measure all identifiable assets acquired, the liabilities assumed and any non-controlling interest in the acquiree as at the acquisition date (the date on which the acquirer obtains control of the acquiree);
- recognise and measure goodwill or gain from a bargain purchase.

The acquirer measures:

- identifiable assets acquired and liabilities assumed - at fair value as at the acquisition date;
- any non-controlling interest – at fair value or pro-rata to their share in the identifiable net assets of the acquiree.

Joint ventures

Joint ventures are those entities over whose activities the BZ WBK Group has joint control, established by contractual agreement. In consolidated financial statements joint ventures are included using equity method.

Associates

Associates are those entities in which the BZ WBK Group has significant influence, but are not subsidiaries, neither joint ventures.

They are accounted for in accordance with the equity method in consolidated financial statements.

The consolidated financial statements include the BZ WBK Group's share of the total recognised gains and losses of associates on an equity accounted basis, from the date that significant influence commences until the date that significant influence ceases. When the BZ WBK Group's share of losses exceeds its interest in an associate, the BZ WBK Group's carrying amount is reduced to nil and recognition of further losses is discontinued except to the extent that the BZ WBK Group has incurred legal or constructive obligations or made payments on behalf of an associate.

Transactions eliminated on consolidation

Intragroup balances and any unrealised gains and losses or incomes (including dividends) and expenses arising from intragroup transactions, are eliminated in the preparation of consolidated financial statements.

In thousands of PLN

2.8. Accounting principles

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

The accounting policies have been applied consistently by BZ WBK Group entities.

Changes in accounting policies

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

Comparability with results of previous periods

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

Foreign currency

Foreign currency transactions

The Polish zloty (PLN) is the functional currency of the units which are members of BZ WBK Group.

Transactions in foreign currencies are translated at the foreign exchange rate ruling 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 ruling at the balance sheet date. Non-monetary assets and liabilities denominated in foreign currencies, which are stated at historical cost, are translated at the foreign exchange rate ruling 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 BZ WBK Group 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 BZ WBK Group at fair value through profit and loss. As at the current balance sheet date and in previous financial year the BZ WBK Group did not hold this category of financial instrument.

Held-to-maturity investments

These are non-derivative financial assets with fixed or determinable payments and fixed maturity that the BZ WBK Group's management has the positive intention and ability to hold to maturity. If the BZ WBK Group 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 BZ WBK Group would not classify financial assets as held to maturity. As at the current balance sheet date and in previous financial year the BZ WBK Group 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. Loans and receivables also include finance lease receivables of BZ WBK Leasing S.A., Santander Consumer Multirent Sp. z o.o. and PSA Finance Polska Sp. z o.o. and factoring receivables of BZ WBK Faktor Sp. z o.o.

Available-for-sale financial assets

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

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

Other financial liabilities

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

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

Recognition

The BZ WBK Group 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 provisions of the instrument.

Lease receivables of BZ WBK Leasing S.A., Santander Consumer Multirent Sp. z o.o. and PSA Finance Polska Sp. z o.o. are accounted for in statement of financial position as of the date from which the lessee is entitled to exercise its rights to use the leased asset. Other agreements where the leased assets have not yet been made available to the lessee are recognised as contingent liabilities.

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

Derecognition

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

A regular way purchase or sale of a financial asset is derecognised using settlement date accounting. The method is applied consistently for all purchases and sales of financial assets.

The BZ WBK Group 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, cancelled or expires.

In thousands of PLN

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 BZ WBK Group measures financial assets, including derivatives that are assets, at their fair values, without any deduction for transaction costs it may incur on sale or other disposal, except for:

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

The fair values of quoted financial instruments in active markets are based on current bid prices. If the market for a financial asset is not active (and for unlisted securities) the BZ WBK Group 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.

Lease payment receivables of BZ WBK Leasing S.A., Santander Consumer Multirent Sp. z o.o. and PSA Finance Polska Sp. z o.o. are accounted for in the statement of financial position at an amount equal to the net investment in the lease. Receivables to clients are measured at amortised cost using the effective interest rate.

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 or 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 directly in other comprehensive income, until the financial asset is derecognised, at which time the comprehensive income previously recognised in equity 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 or 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,

Repurchase and reverse repurchase transactions

The BZ WBK Group 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.

In thousands of PLN

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

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

Derivative financial instruments

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

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

The BZ WBK Group uses derivative financial instruments to hedge its exposure to foreign exchange and interest rate risks arising from BZ WBK Group 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 BZ WBK Group'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 BZ WBK Group 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 BZ WBK Group uses derivative financial instruments among others to hedge its exposure to interest rate risks arising from BZ WBK Group operational, financing and investment activities.

The BZ WBK Group discontinues hedge accounting when:

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

Fair value hedge

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

- 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
- could affect profit and losses.

In thousands of PLN

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

Interest income and expenses hedged and hedging instruments 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 BZ WBK Group 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 income statement.

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

Impairment of financial assets

Assets carried at amortised cost - loans and receivables

The BZ WBK Group 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, 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 debtor;
- (b) a breach of contract, such as a default or delinquency in interest or principal payments;
- (c) the BZ WBK Group, for economic or legal reasons relating to the debtor's financial difficulty, granting to the debtor a concession that the BZ WBK Group would not otherwise consider;
- (d) it becoming probable that the debtor 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, including:
 - (i) adverse changes in the payment status of debtors in the BZ WBK Group, or
 - (ii) national or local economic conditions that correlate with defaults on the assets in the BZ WBK Group.

If there is objective evidence that an impairment charge on loans and receivables has been incurred, the amount of the impairment charges 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 establishing an 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.

The BZ WBK Group 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, which is assessed jointly (collective approach), is verified monthly. The BZ WBK Group carries out validation (so called "back tests") of parameters which are used to calculate impairment charges under collective approach, on the basis of historical observations, at least twice a year.

In thousands of PLN

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

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

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

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

- Internal grade;
- Timeliness of debt service;
- Time that has elapsed from the moment of default, i.e. from identification of an indication of impairment;
- Time that has elapsed after an indication of impairment has 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 BZ WBK Group 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 BZ WBK Group 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 BZ WBK Group's credit risk evaluation or the BZ WBK Group'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 BZ WBK Group reviews regularly the methodology and assumptions used for estimating future cash flows in order to reduce any differences between estimates and actual impairment charge 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 impairment charges in the portfolio.

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

In thousands of PLN

- EP - Emergence Period i.e. time between the occurrence of event of default and its identification by the BZ WBK Group;
- 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 either directly or 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.

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 impairment charge for loan. Subsequent recoveries of amounts previously written off decrease the amount of the charge for loan impairment in the income statement.

Impairment calculation methods are standardised across the BZ WBK Group.

Available-for-sale financial assets

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

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

Contingent liabilities

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

Property, plant and equipment

Owned fixed assets

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

Leased assets

Leases for which the BZ WBK Group assumes substantially all the risks and rewards of ownership are classified as finance leases. The 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 BZ WBK Group 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 BZ WBK Group and the cost of the item can be measured reliably. All other costs are recognised in the income statement as an expense as incurred.

In thousands of PLN

Depreciation

Depreciation is charged to the income statement on a straight-line basis over the estimated economic useful lives of each part of an item of property, plant and equipment.

The estimated economic useful lives are as follows:

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

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

Fixed assets held for sale

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

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

Goodwill and Intangible assets

Goodwill

Goodwill as of the acquisition date measured as the excess of the consideration transferred over the net of the acquisition-date amounts of the identifiable assets acquired and the liabilities, contingent 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 BZ WBK Group, 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 BZ WBK Group are stated at cost less accumulated amortisation and total 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 the statement of financial position

Other trade and other receivables

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

Other liabilities

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

In thousands of PLN

Equity

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

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

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

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

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

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

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

Except for own equity, non-controlling interests are also recognised in BZ WBK Group capital.

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

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

Custody services

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

Capital payments (Dividends)

Own 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 BZ WBK Group'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 BZ WBK Group's obligation in respect of long-term employee benefits is the amount of future benefits 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 method. The valuation of those provisions is updated at least once a year.

Equity-settled share-based payment transactions

For equity-settled share-based payment transactions, the entity 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 BZ WBK Group cannot estimate reliably the fair value of the goods or services received, the BZ WBK Group measures their value, and the corresponding increase in equity, indirectly, by reference to the fair value of the equity instruments granted.

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

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

In thousands of PLN

Cash-settled share-based payment transactions

For cash-settled share-based payment transactions, the BZ WBK Group measures the goods or services acquired and the liability incurred at the fair value of the liability. Until the liability is settled, the BZ WBK Group 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 BZ WBK Group 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 when the BZ WBK Group 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 the risks specific to the liability.

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

Net interest income

Interest income from a financial asset is recognised when it is probable that the economic benefits will flow to the BZ WBK Group 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 BZ WBK Group 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 fees (e.g. arrangement, drawdown, renewal, restructure fees and fees for annexes which modify payments) 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 BZ WBK Group splits realised income into a portion recognised as interest income according to effective interest rate method and a portion recognised as fee income. The BZ WBK Group 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 the effective interest rate, are included in income statement in accordance with accrual method.

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

In thousands of PLN

Net income on bancassurance

For the selected loan products, where linkage to the insurance product has been identified, the BZ WBK Group splits realised income into a portion recognised as interest income according to effective interest rate method and a portion recognised as fee income. The BZ WBK Group 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 BZ WBK Group 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 BZ WBK Group as fee income when the fee is charged for sales of an insurance product.

The BZ WBK Group verifies the accuracy of the assumed allocation of different types of income at least annually.

Net trading income and revaluation

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

Dividend income

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

Profit on disposal of subsidiaries, associates and joint ventures

Gain or loss on the sale of shares in subsidiaries is determined as the difference between the subsidiary's net asset value adjusted for unwritten-off portion of goodwill and the sale price.

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

Gains on other financial instruments

Gains on other financial instruments include:

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

BZ WBK Group uses fair value hedge accounting and cash flow hedge accounting. Details are presented in Note 41 "Hedge accounting".

Other operating income and other operating costs

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

Impairment losses on loans and advances

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

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

In thousands of PLN

Staff and general and administrative expenses of the bank

The “Staff expenses” line item presents the following costs:

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

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

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

Operating lease payments

Operating lease payments are taken to BZ WBK Group’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.

Tax on financial institutions

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

BZ WBK Group reports the tax charge under “Tax on financial institutions”, separately from the income tax charge.

Corporate income tax

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

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

In thousands of PLN

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

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

3. Operating Segments reporting

Presentation of information about business segments in Bank Zachodni WBK Group bases on management information model which is used for preparing of reports for the Management Board, which are used to assess performance of results and allocate resources. Operational activity of Bank Zachodni WBK Group has been divided into five segments: Retail Banking, Business & Corporate Banking, Global Corporate Banking, ALM (Assets and Liabilities Management) and Centre, and Santander Consumer. They were identified based on customers and product types.

Profit before tax is a key measure which Management Board of Bank Zachodni WBK Group uses to assess performance of business segments activity.

Income and costs assigned to a given segment are generated on sale and service of products or services in the segment, according to description presented below. Such income and costs are recognized in the profit and loss account for the Group and may be assigned to a given segment either directly or based on reasonable assumptions.

Interest and similar income split by business segments is assessed by Management Board of Bank Zachodni WBK Group on the net basis including costs of internal transfer funds and without split by interests income and costs.

Settlements among business segments relate to rewarding for delivered services and include:

- sale and/or service of customers assigned to a given segment, via sale/service channels operated by another segment;
- sharing of income and costs on transactions in cases where a transaction is processed for a customer assigned to a different segment;
- sharing of income and cost of delivery of common projects.

Income and cost allocations are regulated by agreements between segments, which are based on single rates for specific services or breakdown of total income and/or cost.

Assets and liabilities of a given segment are used for the operational activity and may be assigned to the segment directly or on a reasonable basis.

Bank Zachodni WBK Group focuses its operating activity on the domestic market.

In 2017 introduced the following changes:

- customer resegmentation between business segments; Once a year, BZWBK Group carry out the resegmentation / migration of customers between operating segments which results from the fact that customer meet the criteria of assignment for different operating segment than before. This change is intended to provide services at the highest level of quality and tailored to individual needs or the scale of customer operations;
- Transfer of the largest corporate clients from the Business and Corporate Banking segment to the Global Corporate Banking Segment;
- Transfer of results and volumes of subsidiary BZ WBK Inwestycje Sp. z.o.o from the Global Corporate Banking segment to ALM and Central Operations segment;
- Change the methodology of Bank Guarantee Fund costs split by operating segments.

Comparable data are adjusted accordingly.

The principles of income and cost identification, as well as assets and liabilities for segmental reporting purposes are consistent with the accounting policy applied in Bank Zachodni WBK Group.

In thousands of PLN

The total result achieved by Bank Zachodni WBK SA from the transaction of acquisition of Visa Europe Limited by Visa Inc. in 2016 (described in note 10) is presented in ALM and Center Segment, whereas the result from described above transaction in Santander Consumer Bank is presented in Santander Consumer Segment.

Retail Banking

Retail Banking generates income from the sale of products and services to personal customers and small and medium companies. In the offer for customers of this segment there are a wide range of savings products, consumer and mortgage loans, credit and debit cards, insurance and investment products, clearing services, brokerage house services, GSM phones top-ups, foreign payments and Western Union and private-banking services. For small and medium companies, the segment provides, among others, lending and deposit taking services, cash management services, leasing, factoring, letters of credit and guarantees. Furthermore, the Retail Banking segment generates income through offering asset management services within investment funds and private portfolios. It also covers insourcing services provided to retail customers based on mutual agreements with other banks and financial institutions.

Business & Corporate Banking

Business & Corporate Banking segment covers products and activities targeted at business entities, local governments and the public sector. In addition to banking services covering lending and deposit activities, the segment provides services in the areas of cash management, leasing, factoring, trade financing and guarantees.

Global Corporate Banking

In the Global Corporate Banking segment, the Group derives income from the sale of products and services to the largest international and local corporations, including:

- transactional banking with such products as cash management, deposits, leasing, factoring, letters of credit, guarantees, bilateral lending and trade finance;
- lending, including project finance, syndicated facilities and bond issues;
- FX and interest rate risk management products provided to all the Bank's customers (segment allocates revenues from this activity to other segments, the allocation level may be subject to changes in consecutive years);
- underwriting and financing of securities issues, financial advice and brokerage services for financial institutions .

Through its presence in the wholesale market, Global Corporate Banking also generates revenues from interest rate and FX risk positioning activity.

ALM and Centre

The segment covers central operations such as financing of other Group's segments, including liquidity, interest rate risk and FX risk management. It also includes managing the Bank's strategic investments and transactions generating income and/or costs that cannot be directly or reasonably assigned to a given segment.

Santander Consumer

Santander Consumer business segment includes activities of the Santander Consumer Group, which was consolidated to the BZ WBK Group from 01.07.2014.

Activities of this segment focus on selling products and services addressed to both individual and business customers. This segment focuses mainly on loans products, i.e. car loans, credit cards, cash loans, installment loans and lease products. In addition, Santander Consumer segment includes term deposits and insurance products (mainly related to loans products).

The transaction concerning the takeover of control by Santander Consumer Bank SA over the companies: PSA Finance Polska Sp. z o.o. and indirectly PSA Consumer Finance Polska Sp. z o.o on 1.10.2016 as well as the transaction regarding the redemption of shares of PSA Finance Polska Sp. z o.o. concluded on 05.04.2017 were both presented in the Santander Consumer business segment.

In thousands of PLN

Consolidated income statement (by business segments)

01.01.2017-31.12.2017	Segment Retail Banking *	Segment Business and Corporate Banking	Segment Global Corporate Banking	Segment ALM and Centre	Segment Santander Consumer	Total
Net interest income	2 495 841	519 490	205 591	703 821	1 352 154	5 276 897
incl. internal transactions	(110 472)	(52 758)	1 167	161 533	530	-
Net fee and commission income	1 392 788	265 186	229 255	(2 504)	128 401	2 013 126
incl. internal transactions	96 172	44 897	(153 620)	14 550	(1 999)	-
Other income	74 153	70 304	86 560	99 116	66 687	396 820
incl. internal transactions	9 717	41 218	(46 929)	(45 447)	41 441	-
Dividend income	-	-	546	76 249	21	76 816
Operating costs	(1 916 292)	(285 103)	(217 611)	(88 933)	(545 542)	(3 053 481)
incl. internal transactions	(8 468)	(1 548)	(7)	14 022	(3 999)	-
Depreciation/amortisation	(199 422)	(21 917)	(16 680)	(45 617)	(35 297)	(318 933)
Impairment losses on loans and advances	(469 571)	(94 839)	(10 669)	(4 577)	(110 817)	(690 473)
Share in net profits (loss) of entities accounted for by the equity method	-	-	-	58 264	-	58 264
Tax on financial institutions	-	-	-	(387 988)	(35 827)	(423 815)
Profit before tax	1 377 497	453 121	276 992	407 831	819 780	3 335 221
Corporate income tax						(816 707)
Consolidated profit for the period						2 518 514

*Includes individual customers and small & micro companies.

In thousands of PLN

Consolidated statement of financial position (by business segment)

31.12.2017	Segment Retail Banking *	Segment Business and Corporate Banking	Segment Global Corporate Banking	Segment ALM and Centre	Segment Santander Consumer	Total
Loans and advances to customers	57 188 615	24 070 378	11 777 530	253 168	14 550 206	107 839 897
Investments in associates	-	-	-	889 372	-	889 372
Other assets	5 741 357	1 016 202	3 838 044	29 451 874	3 897 698	43 945 175
Total assets	62 929 972	25 086 580	15 615 574	30 594 414	18 447 904	152 674 444
Deposits from customers	73 092 023	17 691 913	8 087 291	4 454 998	8 154 910	111 481 135
Other liabilities and equity	4 958 454	3 065 934	5 348 294	17 527 633	10 292 994	41 193 309
Total equity and liabilities	78 050 477	20 757 847	13 435 585	21 982 631	18 447 904	152 674 444

*Includes individual customers and small & micro companies.

In thousands of PLN

Consolidated income statement (by business segments)

01.01.2016-31.12.2016	Segment Retail Banking *	Segment Business and Corporate Banking	Segment Global Corporate Banking	Segment ALM and Centre	Segment Santander Consumer	Total
Net interest income	2 246 151	563 216	184 569	620 009	1 156 427	4 770 372
incl. internal transactions	(94 824)	(41 943)	227	133 417	3 123	-
Net fee and commission income	1 332 229	209 167	203 125	(6 804)	177 004	1 914 721
incl. internal transactions	90 149	33 991	(133 145)	10 781	(1 775)	1
Other income	68 930	90 043	138 046	495 583	31 856	824 458
incl. internal transactions	20 290	48 211	(54 270)	(18 330)	4 099	-
Dividend income	-	-	531	96 041	10	96 582
Operating costs	(1 935 000)	(300 735)	(195 019)	(155 490)	(504 257)	(3 090 501)
incl. internal transactions	(19 633)	(1 858)	(6)	24 044	(2 547)	-
Depreciation/amortisation	(172 112)	(20 174)	(20 318)	(30 090)	(34 526)	(277 220)
Impairment losses on loans and advances	(451 911)	(154 609)	4 874	(1 690)	(181 254)	(784 590)
Share in net profits (loss) of entities accounted for by the equity method	-	-	-	55 439	-	55 439
Tax on financial institutions	-	-	-	(356 078)	(31 128)	(387 206)
Profit before tax	1 088 287	386 908	315 808	716 920	614 131	3 122 054
Corporate income tax						(737 962)
Consolidated profit for the period						2 384 092

*Includes individual customers and small & micro companies.

In thousands of PLN

Consolidated statement of financial position (by business segment)

31.12.2016	Segment Retail Banking *	Segment Business and Corporate Banking	Segment Global Corporate Banking	Segment ALM and Centre	Segment Santander Consumer	Total
Loans and advances to customers	54 619 128	23 814 352	10 472 147	130 645	14 032 266	103 068 538
Investments in associates	-	-	-	871 491	-	871 491
Other assets	5 978 453	1 225 562	3 678 704	31 209 593	4 067 375	46 159 687
Total assets	60 597 581	25 039 914	14 150 851	32 211 729	18 099 641	150 099 716
Deposits from customers	70 895 234	19 119 628	9 405 610	4 874 584	8 227 401	112 522 457
Other liabilities and equity	4 724 836	3 013 479	3 484 623	16 482 081	9 872 240	37 577 259
Total equity and liabilities	75 620 070	22 133 107	12 890 233	21 356 665	18 099 641	150 099 716

*Includes individual customers and small & micro companies.

In thousands of PLN

4. Risk management

Bank Zachodni WBK Capital Group is exposed to a variety of risks in its ordinary business activities. The role of risk management is to ensure that BZ WBK Group 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 BZ WBK Group'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 appropriate risk limits, which restrict the risk exposure. BZ WBK Group continues to modify and enhance its risk management practices to reflect changes in Group's risk profile, economic environment, regulatory requirements and evolving best practice.

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.

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

Risk 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 Group.

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

Management Board is responsible for the effectiveness of the risk management. In particular, the Management Board introduces the organisational structure aligned with the level and profile of the risk being undertaken, split of the responsibilities providing the separation of the risk measurement and control function from the operational activity, is responsible for implementation and updating of the written risk management strategies, and transparency of the activities. The Management Board reviews the financial results of the Group. 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:

In thousands of PLN

- **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, both in individual and portfolio approach to credit exposures, as well as for other financial instruments and assets and the legal provisions. The Committee formulates the methodology, reviews and verifies the adequacy of the parameters used for the calculation of impairment on a portfolio and individual level for BZ WBK Group, excluding Santander Consumer 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, 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 BZ WBK Group, including business continuity management, information security and fraud prevention.

Assets and Liabilities Committee (ALCO) supervises the activity on the banking book, manages liquidity interest rate risk in the banking book. It is responsible for the funding and balance sheet management, including for the pricing policy.

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

Disclosures Committee verifies the Group'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.

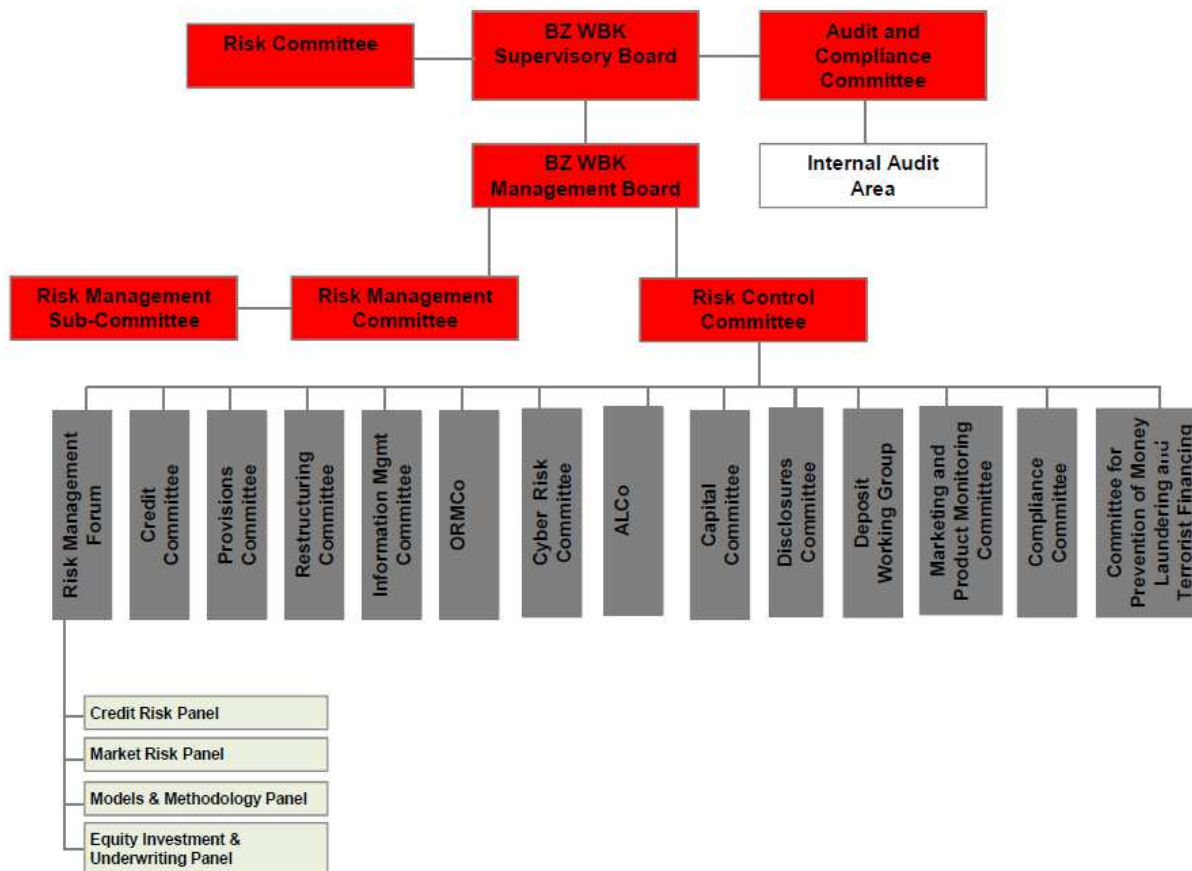
Compliance Committee is responsible for setting standards with respect to the management of compliance risk and the codes of conducts adopted by the Group.

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

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

In thousands of PLN

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



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

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

BZ WBK Group is exposed to a variety of risks impacting the strategic goals. The Group continuously analyses the risks, identifies their sources, creates the relevant risk management mechanisms including among others the measurement, control, mitigation and reporting. Within the risks of the most importance to the BZ WBK Group are the following:

- credit risk,
- concentration risk,
- market risk in the banking and trading book,
- liquidity risk,
- operational risk,
- compliance risk.

Detailed principles, roles and responsibilities of the BZ WBK Group have been described in relevant internal policies on the management of the particular risks.

BZ WBK Group pays special attention to the consistency of risk management processes across the Group, which allows for adequate control of the risk exposure. The subsidiaries implement risk management policies and procedures reflecting the principles adopted by the BZ WBK Group.

In thousands of PLN

Acting under the applicable law, the Bank exercises oversight over risk management in Santander Consumer Bank (SCB) in line with the same oversight rules as applied to other Bank Zachodni WBK Group companies. Bank Zachodni WBK Management Board Members in charge of the Risk Management Division and Financial Management Division (respectively) sit on the Supervisory Board of SCB. Pursuant to the "BZ WBK strategy of investments in capital market instruments", they are responsible for supervision over SCB and they ensure, together with the SCB Supervisory Board, that the company operates in line with adopted plans and operational security procedures. The Bank monitors the profile and level of SCB risk via BZ WBK risk management committees.

Credit risk

BZ WBK Group's credit activities focus on growing a high quality loan book with a good quality, a good yield and customer satisfaction.

Credit activity includes all products subject to credit risk (credit facilities), originated by the Bank or its leasing and factoring subsidiaries.

Credit risk is defined as the possibility of suffering a loss as a result that a borrower will fail to meet its credit obligation, including interest and fees. Credit risk arises from the impairment of credit assets and contingent liabilities, resulting from worsening of the borrower's 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.

Credit risk in BZ WBK Group arises mainly from lending activities on the retail, corporate and interbank 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 Group's internal system of credit grading and monitoring allows for an early identification of likely defaults that might impair the loan book. Additionally the Group uses large set of credit risk mitigation tools, both collaterals (financial and non-financial) and specific credit provisions and clauses (covenants).

The Group 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 Group also continues to review processes and procedures of managing and monitoring of credit portfolio risk adjusting them to the revised regulatory requirements, especially to Recommendations of KNF.

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

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

Risk Management Forum

The credit risk oversight in BZ WBK Group 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 Group'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).

In thousands of PLN

The Group reviews and updates its credit policies on a regular basis, aiming to bring them in line with the Group'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 25m 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 BZ WBK Group continually strives to ensure best quality credit service while satisfying the borrowers' expectations and ensuring security of the credit portfolio. To this end, the credit risk approval function has been segregated from the sales function.

Credit Grading

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

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

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

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

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

Retail customers

Type of loan/receivables	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)

In thousands of PLN

Business customers

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

Collateral management process

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

- verification of the security valuation prepared by external valuers, and assessment of the security value,
- assessment of the legal status of the security,
- assessment of the investment process for the properties,
- seeking legal advises on the proposed securities.

The Collateral and Credit Agreements Department actively participates in credit processes, executing tasks including:

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

In managing its receivables, BZ WBK Group carries out the process of collateral execution. Selection of proper action towards execution of specific collateral depends on the type of the collateral (personal or tangible). In principle the Group aims at voluntary proceedings in the course of collateral execution. When there is no evidence of cooperation with a collateral provider, the Group's rights are fulfilled in compliance with the law and internal regulations in the bankruptcy and enforcement proceedings.

Financial effect of the collateral

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

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

Financial effect of collateral	Gross Amount	Financial effect of collateral
Loans and advances to customers		
housing loans	33 723 865	(175 822)
business	49 011 673	(560 443)
Total balance sheet	93 569 128	(736 265)
Total off-balance sheet	24 642 271	(8 634)

In thousands of PLN

Credit risk stress testing

Stress testing is a part of the credit risk management process used to evaluate potential effects of specific events or movement of a set of financial and macroeconomic variables or change in risk profile on BZ WBK Group's condition. Stress tests are composed of assessment of potential changes in credit portfolio quality when faced with adverse conditions. The process also delivers management information about adequacy of agreed limit and internal capital allocation.

Calculation of Impairment

In BZ WBK Group, charges updating impairment are recognised in accordance with the International Accounting Standards (IAS 39). The charges reflect credit impairment, which is recognised if the Group presents objective evidence that such amounts cannot be recovered in line with the signed loan, lease or factoring agreement. Objective evidences of impairment were defined in accordance with recommendation of Basel Committee, with the International Accounting Standards (IAS 39) and Recommendation R.

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

Twice a year, the Group compares the assumptions and parameters used for loss calculations with the actual situation. The comparison includes changes of economic conditions, amendments to Group's credit policies and recovery process. The process provides assurance that impairments are recognized correctly. The responsibility for adequate level of charges rests with the Provisions Committee.

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

31.12.2017	Provision cover/ number of days	Loans and advances to customers			Total
		individuals	housing loans	business	
Individually impaired portfolio					
Gross amount		-	-	2 378 258	2 378 258
Impairment		-	-	(1 225 187)	(1 225 187)
Net amount		-	-	1 153 071	1 153 071
Collectively impaired					
Gross amount		1 819 031	998 123	1 312 162	4 129 316
Impairment		(1 327 612)	(659 864)	(894 931)	(2 882 407)
Net amount		491 419	338 259	417 231	1 246 909
IBNR portfolio- non-past due					
	up to 0,10%	1 459 972	29 515 446	31 767 897	62 743 315
	0,10% - 0,30%	2 626 977	1 325 621	11 194 309	15 146 907
	0,30% - 0,65%	5 405 252	2 968 339	2 211 931	10 585 522
	over 0,65%	7 873 202	926 174	4 878 661	13 678 037
IBNR portfolio- past due					
	1-30 days	1 066 555	1 206 932	953 539	3 227 026
	31-60 days	176 603	246 121	104 475	527 199
	61-90 days	96 748	106 335	38 985	242 068
	> 90 days	4 778	205	13 916	18 900
Gross amount-IBNR portfolio					106 168 974
Impairment					(738 536)
Net amount					105 430 438
Gross amount -total					
		20 529 118	37 293 296	54 854 134	112 676 548
					(4 846 130)
Other receivables*					9 479
Total net amount					107 839 897

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

In thousands of PLN

31.12.2016	Provision cover/ liczba dni przeterminowania	Loans and advances to customers			Total
		individuals	housing loans	business	
Individually impaired portfolio					
Gross amount		-	-	2 641 177	2 641 177
Impairment		-	-	(1 265 943)	(1 265 943)
Net amount		-	-	1 375 234	1 375 234
Collectively impaired					
Gross amount		1 823 020	1 006 226	1 631 203	4 460 449
Impairment		(1 503 362)	(639 969)	(778 524)	(2 921 855)
Net amount		319 658	366 257	852 679	1 538 594
IBNR portfolio- non-past due					
	do 0,10%	1 184 224	24 478 265	29 280 750	54 943 240
	0,10% - 0,30%	1 863 857	5 319 953	9 004 336	16 188 146
	0,30% - 0,65%	5 361 682	2 614 911	2 392 816	10 369 409
	powyżej 0,65%	7 488 185	1 869 021	3 677 435	13 034 641
IBNR portfolio- past due					
	1-30 dni	1 306 480	1 286 045	2 512 350	5 104 875
	31-60 dni	164 618	302 606	242 749	709 972
	61-90 dni	86 472	131 316	84 039	301 827
	> 90 dni	4 485	38	7 347	11 870
Gross amount-IBNR portfolio					100 663 980
Impairment					(691 083)
Net amount					99 972 897
Gross amount -total		19 283 024	37 008 380	51 474 202	107 765 606
					(4 878 881)
Other receivables*					181 813
Total net amount					103 068 538

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

Loans and advances to banks are assessed using ratings. The assessment method was set out in the Group's internal regulations. Each institutional client (exposure) is assigned a rating by one of the reputable rating agencies (Fitch, Moody's, S&P), in accordance with the CRR. Then, a relevant grade is allocated to the client. Grade 1 is equivalent to 20% risk weight.

Loans and advances to banks	31.12.2017	31.12.2016
Credit quality step:		
1	518 202	410 952
2	1 401 747	2 736 116
3	160 710	322 262
4	3 709	26 677
5	1 241	601
6	-	-
none	50 865	16 670
Total	2 136 474	3 513 278

Financial instruments from the available-for-sale and held-for-trading portfolio are assessed in accordance with the sovereign rating (treasury bonds, securities issued by the National Bank of Poland [NBP], Bank Gospodarstwa Krajowego [BGK], available-for-sale and held-for trading instruments). The sovereign rating is the same as the NBP/BGK rating. All have the same rating as Poland, according to Fitch it is A-. There are no overdue or impaired instruments in these categories.

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

In thousands of PLN

Credit risk concentration

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

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

- PLN 4 965 120 k (25% of Group's own funds).

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

- PLN 4 146 204k (25% of Group's own funds).

The policy pursued by the Group 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 Group's exposures in terms of sector concentrations, proved that the Group does not have any exposures in excess of the limits imposed by the regulator in 2017.

A list of the 20 largest borrowers (or capital-related group of borrowers) of Bank Zachodni WBK Group (performing loans) as at 31.12.2017 (including exposures of individual customers towards subsidiaries of BZ WBK).

Industry code (PKD)	Industry description	Total credit exposure	Balance sheet exposure incl. towards subsidiaries	Committed credit lines, guarantees, treasury limits and capital investments
61	TELECOMMUNICATION	1 739 072	1 654 095	84 977
47	RETAIL	1 007 000	749 928	257 072
07	MINING	988 025	187 406	800 619
61	TELECOMMUNICATION	952 545	691 708	260 837
35	POWER INDUSTRY	878 972	458 972	420 000
70	CONSULTING	831 420	648 989	182 431
06	MINING	825 213	214 052	611 161
35	POWER INDUSTRY	792 000	153 100	638 900
68	REAL ESTATE SERVICES	652 521	561 091	91 430
68	REAL ESTATE SERVICES	652 284	630 178	22 106
35	POWER INDUSTRY	619 853	329 853	290 000
41	CONSTRUCTION	616 378	537 965	78 413
19	RAFINERY	568 390	0	568 390
41	CONSTRUCTION	541 219	1 233	539 986
20	CHEMICAL INDUSTRY	513 959	446 857	67 102
70	CONSULTING	454 351	277 400	176 951
47	RETAIL	400 000	187 896	212 104
35	POWER INDUSTRY	398 116	398 116	-
68	REAL ESTATE SERVICES	373 264	353 953	19 311
35	POWER INDUSTRY	361 922	300 436	61 486
Total gross exposure		14 166 504	8 783 228	5 383 276

In thousands of PLN

A list of the 20 largest borrowers (or capital-related group of borrowers) of Bank Zachodni WBK Group (performing loans) as at 31.12.2016 (including exposures of individual customers towards subsidiaries of BZ WBK).

Industry code (PKD)	Industry description	Total credit exposure	Balance sheet exposure incl. towards subsidiaries	Committed credit lines, guarantees, treasury limits and capital investments
61	TELECOMMUNICATION	1 857 349	1 612 419	244 930
06	MINING	1 180 593	15 047	1 165 546
07	MINING	1 173 796	228 506	945 290
47	RETAIL	1 074 502	670 571	403 931
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	657 954	591 470	66 484
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
20	CHEMICAL 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
86	HEALTHCARE	398 521	327 066	71 455
68	REAL ESTATE SERVICES	392 753	392 753	-
61	TELECOMMUNICATION	387 002	2	387 000
70	CONSULTING	384 922	156 757	228 165
Total gross exposure		14 191 648	7 289 999	6 901 649

Industry concentration

The credit policy of Bank Zachodni WBK Group 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 Group provides funding to sectors and groups or capital units representing a variety of industries.

As at 31.12.2017, the highest concentration level was recorded in the "distribution" sector (13% of the BZ WBK Group exposure), "manufacturing" (10%) and "property" (7%).

Groups of PKD by industries:

Industry	Gross exposure	
	31.12.2017	31.12.2016
Distribution	14 535 418	12 834 912
Manufacturing	11 234 366	10 892 968
Property	7 958 554	8 724 541
Energy	3 602 532	2 868 057
Transportation	3 472 978	3 055 197
Agriculture	2 528 768	2 133 411
Financial sector	1 449 395	966 677
Construction	1 509 824	1 411 827
Other industries	8 562 299	8 282 577
A	Total Business Loans	54 854 134
B	Retail (including mortgage loans)	57 822 414
A+B	BZ WBK Group portfolio	112 676 548
C	Other receivables (commercial bonds)	9 479
A+B+C	Total BZ WBK Group	112 686 027

In thousands of PLN

Forbearance Policy

Pursuant to the definition set out in the draft Implementing Technical Standards of the European Banking Authority, a forbearance measure (i.e. customer debt restructuring) consists of a concession towards a debtor facing financial difficulties or prospect difficulties which threaten the repayment of debt towards BZ WBK Group 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).

		31.12.2017	31.12.2016
Loans and advances to customers- gross amount			
under forbearance measure:		3 460 838	4 041 684
	corporate exposures	1 972 878	2 575 162
	mortgage exposures	1 227 239	1 260 580
	individuals exposures	260 721	205 942
Allowance for impairment - forbearance clients		(847 582)	(954 595)
		-	-
	of which: individually impaired	(413 613)	(503 469)
		-	-
Loans and advances to forbearance clients- net amount		2 613 256	3 087 089

Analysis of credit quality of financial assets subject to forbearance:

Loans and advances to customers under forbearance	Gross exposure		Collateral value		Allowance for impairment	
	31.12.2017	31.12.2016	31.12.2017	31.12.2016	31.12.2017	31.12.2016
Loans and advances -impaired	1 774 300	2 099 884	9 354 162	6 985 767	(793 791)	(875 886)
Loans and advances -unimpaired	1 686 538	1 941 800	3 079 351	5 378 460	(53 791)	(78 709)
non-overdue	1 316 773	1 190 359	2 488 941	2 868 868	(32 470)	(43 336)
from 1 to 30 days overdue	254 422	609 743	421 737	2 260 936	(13 531)	(22 813)
from 31 to 60 days overdue	76 150	92 091	113 030	115 416	(3 916)	(6 242)
from 61 to 90 days overdue	39 193	49 607	55 643	133 240	(3 874)	(6 318)
Total gross amount	3 460 838	4 041 684	12 433 513	12 364 227	(847 582)	(954 595)

In thousands of PLN

Interest income on assets subject to forbearance was PLN 82,418k as at 31 December 2017 and PLN 108,775k as at 31 December 2016.

Loans and advances to customers under forbearance by geographical region (gross amount)	31.12.2017	31.12.2016
Dolnośląskie	357 370	344 929
Kujawsko-Pomorskie	67 175	70 613
Lubelskie	50 461	48 282
Lubuskie	61 876	62 642
Mazowieckie	1 376 072	1 937 784
Małopolskie	222 240	122 639
Opolskie	30 244	28 061
Podkarpackie	34 630	35 734
Podlaskie	38 677	34 491
Pomorskie	180 989	191 445
Warmińsko-Mazurskie	41 277	39 366
Wielkopolskie	187 622	188 845
Zachodniopomorskie	76 702	75 893
Śląskie	574 185	570 193
Świętokrzyskie	76 776	195 961
Łódzkie	84 542	94 806
Total	3 460 838	4 041 684

Loans and advances to customers under forbearance by industry (gross amount)	31.12.2017	31.12.2016
Construction	224 891	274 516
Distribution	82 793	74 408
Energy	398 913	399 368
Financial sector	557	341
Other industries	192 709	196 909
Property	799 621	1 360 369
Manufacturing	169 215	227 267
Agriculture	69 065	8 410
Transportation	35 114	33 574
Individuals	1 487 960	1 466 522
Total	3 460 838	4 041 684

	31.12.2017	31.12.2016
Net carrying amount at beginning of the period	3 087 089	2 984 876
Allowance for impairment	107 013	409 088
Loans and advances derecognised during the period	(144 515)	(758 110)
Loans and advances recognised during the period	1 174 068	1 305 291
Other changes/repayments	(1 610 399)	(854 056)
Net carrying amount at the end of the period	2 613 256	3 087 089

In thousands of PLN

Mortgage loans – currency analysis

Mortgage portfolio of Bank Zachodni consist credit exposures denominated both in PLN and foreign currencies. From the perspective of exposure to currency risk the most important category of retail FX loans are loans denominated in CHF.

The table below presents the PLN equivalent of the mortgage loan-book value of Bank Zachodni WBK Group as at 31 December 2017 and 31 December 2016:

Gross mortgage loans by currency	31.12.2017	31.12.2016
CHF denominated mortgage loans, of which:	10 771 859	13 458 166
<i>Bank Zachodni WBK</i>	8 425 648	10 507 854
<i>Santander Consumer Bank</i>	2 346 211	2 950 312
Mortgage loans denominated in other currencies, of which:	26 521 437	23 550 214
<i>in PLN</i>	24 560 622	21 287 359
Total	37 293 296	37 008 380

Risk profile of CHF-indexed/denominated loans

CHF gross mortgage loans as at 31.12.2017	Gross amount	Impairment losses	Coverage ratio
Performing loans	10 595 020	51 774	0,49%
Non-performing loans	176 839	77 549	43,85%
Total	10 771 859	129 323	

CHF gross mortgage loans as at 31.12.2016	Gross amount	Impairment losses	Coverage ratio
Performing loans	13 273 975	84 051	0,63%
Non-performing loans	184 191	87 338	47,42%
Total	13 458 166	171 389	

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).

BZ WBK Group is exposed to market risk arising from its activity on money and capital markets and services provided to customers. Additionally the Group 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 Group is to reduce the impact of interest and FX rate changes on the Group's profitability and market value as well as to grow income within the strictly defined risk limits while ensuring the Group's liquidity.

BZ WBK Group's market risk policies establish a number of measurement and risk limitation parameters in the form of limits, mandatory and monitoring ratios. Risk limits are periodically reviewed to align them with the Group's strategy and the current objectives of the Group.

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.

In thousands of PLN

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 Group's trading activity is subject to a system of measures and limits, including Value at Risk, stop loss, position limits and sensitivity limits. These 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 Group. 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.

The market risk of equity instruments held by Brokerage Office (shares, index-linked securities) is managed by the Brokerage Office itself and supervised by BZ WBK Risk Management Forum.

Assessment methods

BZ WBK Group 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).

VaR in the trading portfolio 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. VaR is calculated separately for interest rate risk, FX risk and the repricing risk of the equity instruments portfolio of Brokerage Office.

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

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

Interest rate risk in the banking book

The interest rate risk in the banking book is the risk of adverse impact of interest rate changes on the Group'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, responsible for shaping the balance sheet structure of the Bank by entering 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 bank's subsidiaries also mitigate their exposure to the interest rate risk. If there is a mismatch between the repricing of assets and liabilities, the company enters into appropriate transactions via the standard bank accounts held with the Bank or makes derivative transactions with the bank, which from the transaction date manages the risk as part of the global limit of BZ WBK Group.

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

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

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

In thousands of PLN

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

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

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

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

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

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

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

In 2017, the VaR limit for the 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 Group's trading portfolio and by Brokerage Office which has been granted an FX VaR limit, used for managing the open positions linked to the market maker activity. 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 Group 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.

Open positions of subsidiaries are negligible and are not included in the daily risk assessment.

In thousands of PLN

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

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

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

FX Balance Sheet

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

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

The tables below present the Group's key FX positions as at 31 December 2017 and in the comparable period.

31.12.2017	PLN	EUR	CHF	USD	Other	Total
ASSETS						
Cash and balances with central banks	3 678 110	316 343	16 408	74 683	60 678	4 146 222
Loans and advances to banks	372 076	1 293 529	2 738	312 260	155 871	2 136 474
Loans and advances to customers	80 699 235	15 591 398	10 769 691	644 332	135 241	107 839 897
Financial assets available for sale	27 163 287	803 777	-	448 748	-	28 415 812
Selected assets	111 912 708	18 005 047	10 788 837	1 480 023	351 790	142 538 405
LIABILITIES						
Deposits from banks	1 279 330	1 452 388	4 811	37 246	9 308	2 783 083
Deposits from customers	90 954 915	14 979 642	357 006	4 097 331	1 092 241	111 481 135
Subordinated liabilities	-	1 488 602	-	-	-	1 488 602
Selected liabilities	92 234 245	17 920 632	361 817	4 134 577	1 101 549	115 752 820

31.12.2016	PLN	EUR	CHF	USD	Other	Total
ASSETS						
Cash and balances with central banks	4 420 741	221 877	18 083	48 073	66 886	4 775 660
Loans and advances to banks	474 505	2 712 604	23 120	204 939	98 110	3 513 278
Loans and advances to customers	70 939 453	17 835 604	13 466 073	675 748	151 660	103 068 538
Financial assets available for sale	27 870 140	995 506	-	442 232	-	29 307 878
Selected assets	103 704 839	21 765 591	13 507 276	1 370 992	316 656	140 665 354
LIABILITIES						
Deposits from banks	1 306 701	1 223 688	-	29 928	964	2 561 281
Deposits from customers	95 131 257	13 251 280	302 495	2 941 889	895 536	112 522 457
Subordinated liabilities	-	440 457	-	-	-	440 457
Selected liabilities	96 437 958	14 915 425	302 495	2 971 817	896 500	115 524 195

Equity investment risk

The unit responsible for equity (listed on active markets) 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 Office, approves changes in the risk measurement methodology and oversees the risk management process.

In thousands of PLN

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

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

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 Group Liquidity Risk Policy is designed to:

- ensure the ability to finance assets and satisfy claims, both current and future, in a timely manner and at an economic price;
- manage the maturity mismatch between assets and liabilities;
- set a scale of the liquidity risk in the form of various internal limits;
- ensure proper organization of the liquidity management process within the Group;
- 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 Group in its liquidity management process is that all expected outflows occurring within 1 month in respect of deposits, current funds, loan drawdowns, guarantee payments and transaction settlements should be at least fully covered by the anticipated inflows or available High Quality Liquid Assets (HQLA) assuming normal or predictable conditions for the bank's operations. The QLA category includes: cash on hand, cash deposited with NBP (National Bank of Poland), securities which may be sold or pledged under repo transactions or NBP lombard loans. As at 31 December 2017, the value of easy resalable assets buffer amounted to PLN 27,8 bn.

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 structural liquidity ratios at pre-defined levels.

The bank uses a suite of additional watch limits and indicators with respect to the following:

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

As at 31 December 2017, LCR ratio for the Group was at 169% and as at 31 December 2016 - 176%.

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, including strategies of Bank's activity's financing.

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.

In thousands of PLN

The Group 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. ALCO supervises liquidity risk management process in subsidiaries.

Risk Measurement and Reporting

The responsibility for assessment and reporting of the liquidity risk rests on the Risk Management Division, specifically the Financial Risk Department. The role of the Department is to draft liquidity management policies, carry out stress tests and to measure and report on risk.

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

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

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

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

Stress tests and the contingency plan

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

- Baseline scenario, which assumes non-renewability of wholesale funding;
- Idiosyncratic liquidity crisis scenarios (specific to the bank);
- Local systemic liquidity crisis scenario;
- 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, BZ WBK Group 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 Group performs stress tests for intraday liquidity as well as reverse stress tests.

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

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

In 2017, as in previous years, BZ WBK Group focused on keeping its loan-to-deposit ratio at a comfortable level (which totalled 86% as at 31 December 2017) and controlling key short- and long-term liquidity measures.

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

In thousands of PLN

Liquidity Policy Report - (excluding Santander Consumer Group):

31.12.2017	A'vista	up to 1 month	from 1 to 3 months	from 3 to 6 months	from 6 to 12 months	from 1 to 2 years	from 2 to 5 years	above 5 years
Assets	16 285 962	5 487 477	2 737 369	7 877 137	6 474 997	11 747 539	29 354 839	52 897 949
Liabilities and equity	18 843 600	27 882 654	16 438 439	9 538 471	7 722 235	6 373 358	10 297 600	35 766 911
including:	-	-	-	-	-	-	-	-
- Self-buy-back transactions	-	-	-	-	-	-	-	-
- Deposits from banks	746 740	2 101 959	410 361	73 443	15 400	-	-	-
- Deposits from customers	18 096 859	25 572 150	15 250 513	8 942 409	6 832 174	6 014 336	8 958 040	9 081 624
- Debt securities in issue	-	-	750 000	485 000	-	-	-	-
- Subordinated liabilities	-	-	-	-	-	-	-	1 489 428
Contractual liquidity mismatch/ gap	(2 557 638)	(22 395 177)	(13 701 070)	(1 661 334)	(1 247 239)	5 374 180	19 057 239	17 131 038
Cumulative liquidity gap	(2 557 638)	(24 952 815)	(38 653 886)	(40 315 219)	(41 562 458)	(36 188 277)	(17 131 038)	0
Net derivatives	-	(63 970)	13 782	(76 812)	(33 280)	12 856	(6 049)	(119 732)

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

Operational Risk

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

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

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

BZ WBK Group has defined "the Operational Risk Management Strategy".

The Operational Risk Management Committee (ORMCo) established by the Management Board is responsible for setting operational risk management standards for BZ WBK Group. 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. 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.

BZ WBK Group uses the following tools:

- Identification and assessment of operational risk

In thousands of PLN

Primary tool for identification and assessment of operational risk is self-assessment. In the self-assessment process, BZ WBK Group 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

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

The Group 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 Group.

- Analysis of risk indicators

Primary tool for monitoring of operational risk are risk indicators. BZ WBK Group 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 Group. Monitoring is based both on financial and technological and operational meters.

- Defining actions lowering the risk

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

- Business continuity management (BCM)

Each organisational unit is required to develop and update its business continuity management plans to ensure that critical business processes remain uninterrupted following an unplanned disruption. BCM plans are tested on a regular basis to provide assurance to BZ WBK Group that critical business processes may be restored at the required service level and within the agreed timeframe. BZ WBK Group has backup locations in place where critical processes can be restored and continued should an incident occur.

- Information Security

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

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

- Insurance

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

- Regular reporting to the Risk Management Committee and Supervisory Board

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

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

In thousands of PLN

Compliance Risk

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, BZ WBK is exposed to the compliance risk mainly in the following areas:

- 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 Group, including in connection with membership in domestic or international trade associations ;
- 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.;

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

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

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

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

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

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

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

The Audit and Compliance Committee regularly reviews key compliance issues identified by the Compliance Area as well as 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.

The Compliance Unit's tasks are delivered through:

In thousands of PLN

- independent identification, assessment and monitoring of compliance risk that the Group 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
- cooperation with compliance units within the Group and with central compliance unit in Santander Group.

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

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

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

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

5. Capital management

Introduction

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

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

In thousands of PLN

The Management Board delegated on-going capital management to Capital Committee. Capital Committee conducts regular assessment of capital adequacy of the Bank and the Group, 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 both for the Bank and the Group. Any ultimate decisions regarding increase or decrease of capital are taken by relevant authorities of the bank and subsidiaries 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 December 2017".

In 2017, Bank Zachodni WBK Group 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 December 2017, the minimum capital ratios of the Bank satisfying the regulatory recommendations and additional own fund requirements under Pillar 2 were as follows:

- a Tier 1 capital ratio of 11.16%;
- a total capital ratio of 14.29%;

and for the BZ WBK Group were as follows:

- a Tier 1 capital ratio of 11.08%;
- a total capital ratio of 14.19%;

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

Pursuant to the KNF decisions of 15 December 2017 and 20 November 2017, Bank Zachodni WBK Group and Bank Zachodni WBK maintain own funds to cover an additional capital requirement for risk attached to foreign currency home mortgages for households. As at 31 December 2017, the buffer was set at 0.54 p.p. above the total capital ratio for Bank Zachodni WBK, and at 0.44 p.p. for Bank Zachodni WBK Group. The buffer includes at least 75% of Tier 1 capital (which corresponds to the capital requirement of 0.41 p.p. above Tier 1 capital ratio for Bank Zachodni WBK, and 0.33 p.p. for Bank Zachodni WBK Group) and at least 56% of the Common Equity Tier 1 capital (which corresponds to the capital requirement of 0.30 p.p. above the Common Equity Tier 1 capital for Bank Zachodni WBK, and 0.25 p.p. for Bank Zachodni WBK Group).

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

On 4 October 2016, KNF identified Bank Zachodni WBK as other systemically important institution and imposed an additional capital buffer of 0.5 p.p. Pursuant to the KNF decision of December 2017, Bank Zachodni WBK Group maintains capital buffer on the same level.

From 1 January 2018, Bank Zachodni WBK and the Group will have to comply with the systemic risk buffer of 300 p.p. and the conservation buffer of 1.875 p.p., which in turn will affect the minimum ratios for the bank, i.e.:

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

For Bank Zachodni WBK Group, those ratios will be as follows:

- a Tier 1 capital ratio of 11.71%;
- a total capital ratio of 13.82%.

In thousands of PLN

Regulatory Capital

The capital requirement for Bank Zachodni WBK Group is determined in accordance with Part 3 of CRR, which formed a legal basis as at 31 December 2017.

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

Calculation of capital ratio for Bank Zachodni WBK Group as at 31.12.2017 and 31.12.2016

		31.12.2017	31.12.2016
I	Total Capital requirement (Ia+Ib+Ic+Id), of which:	9 520 249	8 816 625
Ia	- due to credit risk & counterparty credit risk	8 361 481	7 713 572
Ib	- due to market risk	107 752	93 321
Ic	- due to credit valuation adjustment risk	42 400	42 739
Id	- due to operational risk	1 008 616	966 993
II	Total own funds*	22 314 566	19 179 697
III	Reductions	2 454 088	2 594 883
IV	Own funds after reductions (II-III)	19 860 478	16 584 814
V	CAD [IV/(I*12.5)]	16,69%	15,05%
VI	Tier 1 ratio	15,28%	14,56%

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

Internal Capital

Notwithstanding the regulatory methods for measuring capital requirements, Bank Zachodni WBK Group 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 Group's strategy, the process of defining risk appetite and the process of planning.

The Group 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 Group customers (PD - probability of default) and loss given default (LGD loss given default).

Bank Zachodni WBK Group 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 Group's business and to take account of any new risks and the management judgement.

The review and assessment is the responsibility of the Group'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 August 2010 and taken up by the European Bank for Reconstruction and Development. The amendments included the extension of maturity until 5 August 2025, among other things. Pursuant to the KNF decision of 18 May 2016, the foregoing subordinated bonds of EUR 100,000 k were allocated to the Tier II capital.

On 2 December 2016, the bank issued bonds worth EUR 120,000 k as part of its strategy aimed at increasing Tier 2 capital. On 24 February 2017, the bank was granted consent from the KNF to allocate the above bonds to Tier 2 capital.

Furthermore, on 22 May 2017, the bank issued additional subordinated bonds with a nominal value of EUR 137,100 k. Pursuant to the KNF decision of 19 October 2017, these instruments were allocated to Tier 2 capital.

Detailed information on subordinated liabilities is presented in Note 33.

In thousands of PLN

6. Net interest income

	01.01.2017- 31.12.2017	01.01.2016- 31.12.2016
Interest income		
Loans and advances to enterprises	1 676 521	1 635 420
Loans and advances to individuals, of which:	3 602 440	3 221 059
<i>Home mortgage loans</i>	1 066 596	932 067
Debt securities incl.:	660 999	614 764
<i>Investment portfolio available for sale</i>	627 398	582 458
<i>Trading portfolio</i>	33 601	32 306
Leasing agreements	260 542	194 467
Loans and advances to banks	64 225	63 753
Public sector	6 376	6 929
Reverse repo transactions	27 342	8 957
Interest recorded on hedging IRS	230 862	315 571
Total	6 529 307	6 060 920
Interest expenses		
Deposits from individuals	(558 060)	(632 301)
Deposits from enterprises	(342 180)	(382 886)
Repo transactions	(54 367)	(36 728)
Deposits from public sector	(54 061)	(48 081)
Deposits from banks	(46 645)	(38 660)
Subordinated liabilities and issue of securities	(197 097)	(151 892)
Total	(1 252 410)	(1 290 548)
Net interest income	5 276 897	4 770 372

As at 31.12.2017 net interest income includes interest on impaired loans of PLN 250,588 k (as at 31.12.2016 - PLN 268,084 k).

In thousands of PLN

7. Net fee and commission income

	01.01.2017- 31.12.2017	01.01.2016- 31.12.2016
Fee and commission income		
eBusiness & payments	627 600	578 420
Current accounts and money transfer	338 306	338 374
Asset management fees	306 474	256 270
Foreign exchange commissions	346 056	320 003
Credit commissions	316 125	267 195
Insurance commissions	213 572	282 723
Brokerage activities	88 129	71 580
Credit cards	169 548	161 371
Off-balance sheet guarantee commissions	60 303	63 770
Finance lease commissions	16 228	15 041
Issue arrangement fees	14 502	15 104
Distribution fees	9 730	6 035
Other commissions	20 241	12 578
Total	2 526 814	2 388 464
Fee and commission expenses		
eBusiness & payments	(225 707)	(201 454)
Distribution fees	(21 578)	(22 695)
Brokerage activities	(11 175)	(10 368)
Credit cards	(33 262)	(39 827)
Credit commissions paid	(98 335)	(58 018)
Insurance commissions	(17 523)	(37 919)
Finance lease commissions	(27 184)	(25 124)
Asset management fees and other costs	(6 607)	(6 107)
Other	(72 317)	(72 232)
Total	(513 688)	(473 744)
Net fee and commission income	2 013 126	1 914 720

Included above is fee and commission income on credits, credit cards, off-balance sheet guarantees and finance leases of PLN 562,204 k (31.12.2016: PLN 507,377 k) and fee and commission expenses on credit cards, finance leases and paid to credit agents of PLN (158,781) k (31.12.2016: PLN (122,969) k) other than fees included in determining the effective interest rate, relating to financial assets and liabilities not carried at fair value through profit and loss.

8. Dividend income

	01.01.2017- 31.12.2017	01.01.2016- 31.12.2016
Dividend income		
Dividends from equity financial assets available for sale	76 270	96 051
Dividends income from equity financial assets at fair value through profit or loss	546	531
Total	76 816	96 582

In thousands of PLN

9. Net trading income and revaluation

	01.01.2017- 31.12.2017	01.01.2016- 31.12.2016
Net trading income and revaluation		
Derivative instruments and interbank fx transactions	153 040	254 446
Other FX related income	43 673	20 204
Profit on equity instruments	4 265	(1 710)
Profit on debt instruments	(6 004)	7 880
Total	194 974	280 820

Net trading income and revaluation includes the change of the value of derivative instruments in the amount of PLN (10,287) k for 2017 and PLN (5,817) k for 2016.

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

10. Gains (losses) from other financial securities

	01.01.2017- 31.12.2017	01.01.2016- 31.12.2016
Gains (losses) from other financial securities		
Profit on sale of equity shares available for sale	26 464	317 828
Profit on sale of debt securities available for sale	20 824	93 184
Charge due to impairment losses	(461)	(10 398)
Total profit (losses) on financial instruments	46 827	400 614
Change in fair value of hedging instruments	23 760	57 112
Change in fair value of underlying hedged positions	(23 085)	(54 952)
Total profit (losses) on hedging and hedged instruments	675	2 160
Total	47 502	402 774

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

- Bank Zachodni WBK and Santander Consumer Bank (SCB) – EUR 49,974,289 and EUR 1,654,744 in cash, respectively
- Bank Zachodni WBK and SCB – 18,092 and 600 series C preference shares of Visa Inc., respectively.

Furthermore, the earn-out of EUR 1.12bn payable to all transaction participants was settled. The share of Bank Zachodni WBK in the above amount is 0.3839946336% and the share of SCB is 0.0127491571%. The earn-out payable to the Group may be adjusted within three years of the transaction date in the circumstances stipulated in the agreement.

In 2016, the total profit made by Bank Zachodni WBK and SCB on the above transaction was PLN 305,865 k and PLN 10,154 k, respectively and was recognised under “Gains from other financial securities” in the income statement.

11. Other operating income

	01.01.2017- 31.12.2017	01.01.2016- 31.12.2016
Other operating income		
Income on sale of services	20 535	15 769
Reimbursements of BGF charges *	433	54 215
Release of provision for legal cases and other assets	43 297	14 830
Settlements of leasing agreements	3 266	4 470
Recovery of other receivables	5 641	6 919
Profit on sales or liquidation of fixed assets, intangible assets and assets for disposal	11 543	6 680
Received compensations, penalties and fines	1 039	1 296
Other income from legal cases	24 238	-
Other	40 595	36 585
Total	150 587	140 764

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

In thousands of PLN

12. Impairment losses on loans and advances

Impairment losses on loans and advances	01.01.2017- 31.12.2017	01.01.2016- 31.12.2016
Collective and individual impairment charge	(668 164)	(828 170)
Incurred but not reported losses charge	(65 420)	(27 015)
Recoveries of loans previously written off	43 534	45 166
Off-balance sheet credit related facilities	(423)	25 429
Total	(690 473)	(784 590)

13. Employee costs

Employee costs	01.01.2017- 31.12.2017	01.01.2016- 31.12.2016
Salaries and bonuses	(1 293 085)	(1 246 336)
Obligatory salary related costs	(216 933)	(205 215)
Staff benefits costs	(39 705)	(37 736)
Professional trainings	(18 730)	(20 057)
Retirement fund, holiday provisions and other employee costs	5 836	(1 020)
Total	(1 562 617)	(1 510 364)

14. General and administrative expenses

General and administrative expenses	01.01.2017- 31.12.2017	01.01.2016- 31.12.2016
Maintenance and rentals of premises	(348 290)	(355 529)
Marketing and representation	(133 906)	(146 587)
IT systems costs	(213 047)	(197 510)
Bank Guarantee Fund, Polish Financial Supervision Authority and National Depository for Securities	(224 168)	(281 383)
Postal and telecommunication costs	(52 911)	(48 068)
Consulting fees	(65 574)	(60 398)
Cars, transport expenses, carriage of cash	(67 356)	(67 847)
Other external services	(104 616)	(94 130)
Stationery, cards, cheques etc.	(27 280)	(31 741)
Sundry taxes	(33 587)	(33 469)
Data transmission	(12 458)	(15 763)
KIR, SWIFT settlements	(28 480)	(26 242)
Security costs	(25 286)	(25 470)
Costs of repairs	(14 137)	(17 504)
Other	(25 719)	(23 224)
Total	(1 376 815)	(1 424 865)

In thousands of PLN

15. Other operating expenses

	01.01.2017- 31.12.2017	01.01.2016- 31.12.2016
Other operating expenses		
Charge of provisions for legal cases and other assets	(59 540)	(112 058)
Impairment loss on property, plant, equipment and intangible assets	(8 397)	(12 306)
Costs of purchased services	(8 177)	(2 775)
Other membership fees	(992)	(896)
Paid compensations, penalties and fines	(3 091)	(2 312)
Donations paid	(4 876)	(4 338)
Other	(28 976)	(20 587)
Total	(114 049)	(155 272)

16. Corporate income tax

	01.01.2017- 31.12.2017	01.01.2016- 31.12.2016
Corporate income tax		
Current tax charge	(801 991)	(874 323)
Deferred tax	(14 885)	127 976
Adjustments from previous years	169	8 385
Total	(816 707)	(737 962)

	01.01.2017- 31.12.2017	01.01.2016- 31.12.2016
Corporate total tax charge information		
Profit before tax	3 335 221	3 122 054
Tax rate	19%	19%
Tax calculated at the tax rate	(633 692)	(593 190)
Non-tax-deductible expenses	(20 954)	(34 690)
The fee to the Bank Guarantee Fund	(40 082)	(15 403)
Tax on financial institutions	(80 524)	(73 568)
Sale of receivables	(52 237)	(43 223)
Non-taxable income (dividends)	14 423	18 122
Non-tax deductible bad debt provisions	(10 970)	(8 023)
Adjustment of prior year tax	169	8 385
Tax effect of consolidation adjustments	5 045	6 834
Other	2 115	(3 206)
Total income tax expense	(816 707)	(737 962)

	31.12.2017	31.12.2016
Deferred tax recognised directly in equity		
Relating to equity securities available-for-sale	(130 950)	(122 523)
Relating to debt securities available-for-sale	(57 957)	35 033
Relating to cash flow hedging activity	20 508	25 251
Relating to valuation of defined benefit plans	(125)	(1 913)
Total	(168 524)	(64 152)

In thousands of PLN

17. Earnings per share

	01.01.2017- 31.12.2017	01.01.2016- 31.12.2016
Earnings per share		
Profit for the period attributable to ordinary shares	2 213 054	2 166 847
Weighted average number of ordinary shares	99 275 197	99 234 534
Earnings per share (PLN)	22,29	21,84
Profit for the period attributable to ordinary shares	2 213 054	2 166 847
Weighted average number of ordinary shares	99 275 197	99 234 534
Weighted average number of potential ordinary shares	187 456	155 947
Diluted earnings per share (PLN)	22,25	21,80

The weighted average number of potential ordinary shares takes into account the number of share options granted under the incentive scheme described in Note 52.

18. Cash and balances with central banks

	31.12.2017	31.12.2016
Cash and balances with central banks		
Cash	2 270 698	2 134 971
Current accounts in central banks	1 857 824	2 538 686
Term deposits	17 700	102 003
Total	4 146 222	4 775 660

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

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

19. Loans and advances to banks

	31.12.2017	31.12.2016
Loans and advances to banks		
Loans and advances	850 541	795 140
Current accounts	1 285 933	2 718 138
Total	2 136 474	3 513 278

Fair value of loans and advances to banks is presented in Note 43.

In thousands of PLN

20. Financial assets and liabilities held for trading

Financial assets and liabilities held for trading	31.12.2017		31.12.2016	
	Assets	Liabilities	Assets	Liabilities
Trading derivatives	1 226 551	1 237 704	1 859 361	1 728 931
Interest rate operations	307 344	275 046	970 357	898 100
Forward	-	68	6	20
Options	13 211	13 226	17 744	17 743
IRS	291 615	260 187	945 715	873 241
FRA	2 518	1 565	6 892	7 096
Transactions on equity instruments	6 053	6 053	12 032	12 032
Options	6 053	6 053	12 032	12 032
FX operations	913 154	956 605	876 972	818 799
CIRS	282 186	253 890	210 135	245 130
Forward	41 175	160 814	69 838	61 693
FX Swap	493 265	444 919	429 814	352 967
Spot	1 360	1 832	1 561	2 041
Options	95 168	95 150	156 718	156 718
Other	-	-	8 906	250
Debt and equity securities	2 189 557	-	1 321 624	-
Debt securities	2 174 096	-	1 312 589	-
Government securities:	2 170 048	-	612 233	-
- bonds	2 170 048	-	612 233	-
Central Bank securities:	-	-	699 883	-
- bills	-	-	699 883	-
Commercial securities:	4 048	-	473	-
- bonds	4 048	-	473	-
Equity securities:	15 461	-	9 035	-
- listed	15 461	-	9 035	-
Short sale	-	-	-	80 129
Total financial assets/liabilities	3 416 108	1 237 704	3 180 985	1 809 060

Financial assets and liabilities held for trading - trading derivatives include the change in the value of counterparty risk in the amount of PLN 190 k as at 31.12.2017 and PLN 9,525 k as at 31.12.2016.

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

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

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

Offsetting financial assets and financial liabilities

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

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

In thousands of PLN

Offsetting financial assets and financial liabilities	31.12.2017		31.12.2016	
	Financial assets	Financial liabilities	Financial assets	Financial liabilities
Fair value measurements of derivative instruments	1 226 551	1 237 704	1 916 422	3 690 509
Value of collateral accepted/provided	(373 184)	(268 306)	(232 591)	(2 131 485)
Assets and liabilities subject to set-offs under a mandate agreement	853 367	969 398	1 683 831	1 559 024
Maximum amount of potential set-off	(387 764)	(387 763)	(924 984)	(924 984)
Assets and liabilities subject to set-offs under a mandate agreement, taking into account the maximum amount of potential set-off	465 603	581 635	758 847	634 040

The table below presents derivatives' nominal values.

Derivatives' nominal values		31.12.2017	31.12.2016
1. Term derivatives (hedging)		25 301 383	32 810 487
a)	Single-currency interest rate swap	2 404 709	2 881 319
b)	Macro cash flow hedge -purchased (IRS)	1 575 000	2 242 000
c)	Macro cash flow hedge -purchased (CIRS)	10 430 903	12 714 713
d)	Macro cash flow hedge -sold (CIRS)	10 542 739	14 402 131
e)	FX Swap cash flow hedge -purchased (FX)	176 806	284 172
f)	FX Swap cash flow hedge-sold (FX)	171 226	286 152
2. Term derivatives (trading)		282 611 381	289 441 541
a)	Interest rate operations	168 569 058	170 149 579
	Single-currency interest rate swap	156 870 056	146 126 096
	FRA - purchased amounts	3 260 000	16 680 000
	Options	8 370 402	7 314 133
	Forward- purchased amounts	-	27 090
	Forward- sold amounts	68 600	2 260
b)	FX operations	114 042 323	119 291 962
	FX swap – purchased amounts	29 815 344	30 143 163
	FX swap – sold amounts	29 745 471	30 025 420
	Forward- purchased amounts	8 226 882	5 580 260
	Forward- sold amounts	8 393 420	5 620 242
	Cross-currency interest rate swap – purchased amounts	10 743 244	12 916 870
	Cross-currency interest rate swap – sold amounts	10 720 212	12 961 985
	FX options -purchased CALL	4 036 440	5 398 974
	FX options -purchased PUT	4 162 435	5 623 037
	FX options -sold CALL	4 036 440	5 398 974
	FX options -sold PUT	4 162 435	5 623 037
3. Currency transactions- spot		2 894 072	1 540 212
	Spot-purchased	1 446 853	769 621
	Spot-sold	1 447 219	770 591
4. Transactions on equity financial instruments		817 734	1 335 679
	Derivatives contract - purchased	401 987	664 431
	Derivatives contract - sold	415 747	671 248
Total		311 624 570	325 127 919

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

21. Hedging derivatives

Hedging derivatives	31.12.2017		31.12.2016	
	Assets	Liabilities	Assets	Liabilities
Derivatives hedging fair value	2 283	115 496	3 232	140 338
Derivatives hedging cash flow	215 778	463 302	64 413	1 883 006
Total hedging derivatives	218 061	578 798	67 645	2 023 344

In thousands of PLN

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

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

22. Loans and advances to customers

Loans and advances to customers	31.12.2017	31.12.2016
Loans and advances to enterprises	47 776 973	45 179 803
Loans and advances to individuals, of which:	57 822 414	56 291 404
<i>Home mortgage loans</i>	37 293 296	37 008 380
Finance lease receivables	6 848 960	6 098 499
Loans and advances to public sector	228 201	195 900
Other	9 479	181 813
Gross receivables	112 686 027	107 947 419
Allowance for impairment	(4 846 130)	(4 878 881)
Total	107 839 897	103 068 538

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

Finance lease receivables are presented in Note 46. Fair value of loans and advances to customers is presented in Note 43.

Movements on impairment losses on loans and advances to customers	31.12.2017	31.12.2016
Individual and collective impairment		
As at the beginning of the period	(4 187 798)	(4 471 467)
Individual and collective impairment acquired in a business combination	-	(11 548)
Charge/write back of current period	(668 164)	(828 170)
Write off/Sale of receivables	735 191	1 110 443
Transfer	(16 960)	26 631
F/X differences	30 137	(13 687)
Balance at the end of the period	(4 107 594)	(4 187 798)
IBNR		
As at the beginning of the period	(691 083)	(659 596)
IBNR acquired in a business combination	-	(1 947)
Charge/write back of current period	(65 420)	(27 015)
Sale of receivables	3 429	3 182
Transfer	940	558
F/X differences	13 598	(6 265)
Balance at the end of the period	(738 536)	(691 083)
Allowance for impairment	(4 846 130)	(4 878 881)

In September 2015, SCB securitized the instalment loan portfolio. The transaction was a traditional, revolving transaction and consisted in transferring the right to securitized receivables to SC Poland Consumer Sp. z o.o. 15-1 (SPV2), with its registered seat in Poland.

On the basis of the securitized assets, the aforesaid company issued bonds with a total value of PLN 1,051,125 k secured in the form of a registered pledge on the assets of SPV2. The bonds bear an interest rate comprising 1M WIBOR and margin. As a result of the securitization, SCB obtained financing in return for the right to future cash flows from the securitized credit portfolio. The latest redemption date is 19 August 2025, but in SCB estimation, the aforesaid bonds should be redeemed within two years from the transaction date.

In August 2016 SCB performed a transaction of securitization of cash loans portfolio. The concluded transaction is a traditional and revolving securitization including transfer of ownership rights to securitized receivables for the benefit of the special purpose vehicle, SC Poland Consumer 16-1 Sp. z o.o. (SPV3) with its registered seat in Poland.

This Company issued, on the basis of securitized assets, bonds of the total value of PLN 1,225,000 k, secured with a registered pledge on the property of SPV3. The bonds bear an interest rate comprising 1M WIBOR and margin. As a result of the securitization

In thousands of PLN

SCB obtained funding of its activity in exchange for giving rights to future flows arising from the securitized loans portfolio. The maximum period for redemption of the bonds is 16 September 2026 but SCB estimated that it shall take place within 3 years from the transaction date.

In the light of provisions of the IAS 39, the contractual terms and conditions of the securitization transaction do not require SCB to derecognize the securitized assets from its financial statements. Consequently, at 31 December 2017, SCB recognizes securitized assets under Loans and advances granted to clients in the net amount of PLN 2,136,690 k. The fair value of net securitized assets measured as of 31 December 2017 amounted respectively to PLN 2,145,065 k.

In May 2016 SCB finalized the transaction of securitization of car loans and instalment loans portfolios concluded in 2014. The transaction included transfer of ownership rights to securitized receivables for the benefit of the special purpose vehicle, SC Poland Auto 2014-1 Limited (SPV1) with its registered seat in Ireland. The transaction was finalized after redemption of all issued bonds and included exercising of the procedure specified in the agreement, so called redemption option. In the frame of realization of the procedure of datio in payment, SCB took over from the SPV the rights to remaining unpaid receivables which allowed total settlement of the transaction. The value of the net securitization portfolio as of the redemption moment was PLN 391,684 k.

The profit earned by all SPVs is zero because SPV absorbs all revenues and expenses of SPV1 and SPV2 are offset against the revenues and expenses of SCB. In this model SPV allocated all payments received from SCB to particular types of payments, including other settlements with SCB, according to a specified priority, in the sequence as agreed in the agreement.

23. Financial assets available for sale

Financial assets available for sale	31.12.2017	31.12.2016
Debt securities	27 494 933	28 423 828
Government securities:	24 025 353	23 429 089
- bonds	24 025 353	23 429 089
Central Bank securities:	1 379 839	2 849 694
- bills	1 379 839	2 849 694
Other securities:	2 089 741	2 145 045
-bonds	2 089 741	2 145 045
Equity securities	920 879	884 050
- listed	19 329	34 473
- unlisted	901 550	849 577
Total	28 415 812	29 307 878

As at 31.12.2017 fixed interest rate debt securities measured at fair value amount to PLN 17,640,329 k, variable interest rate securities amount to PLN 9,854,604 k.

As at 31.12.2016 fixed interest rate debt securities measured at fair value amount to PLN 19,649,445 k, variable interest rate securities amount to PLN 8,774,383 k.

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

Unlisted equity investments classified as available-for-sale for which no active market exists are recognized at cost and tested for impairment or their fair value is assessed based on valuation models. The Group 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 43.

In thousands of PLN

Movements on financial assets available for sale	Debt securities	Financial instruments	Total
		representing equity rights	
As at 1 January 2017	28 423 828	884 050	29 307 878
Additions	60 756 329	2 536	60 758 865
Disposals (sale and maturity)	(62 053 423)	(9 193)	(62 062 616)
Fair value adjustment	463 913	43 947	507 860
Movements on interest accrued	19 756	-	19 756
Allowances for impairment	-	(461)	(461)
F/X differences	(115 470)	-	(115 470)
As at 31 December 2017	27 494 933	920 879	28 415 812

Movements on financial assets available for sale	Debt securities	Financial instruments	Total
		representing equity rights	
As at 1 January 2016	23 463 634	1 158 444	24 622 078
Additions	49 889 981	80 284	49 970 265
Disposals (sale and maturity)	(44 608 851)	(17 749)	(44 626 600)
Fair value adjustment	(453 803)	(326 531)	(780 334)
Movements on interest accrued	80 715	-	80 715
Allowances for impairment	-	(10 398)	(10 398)
F/X differences	52 152	-	52 152
As at 31 December 2016	28 423 828	884 050	29 307 878

24. Investments in associates

Balance sheet value of associates	31.12.2017	31.12.2016
Polfund - Fundusz Poręczeń Kredytowych S.A.	43 570	43 216
BZ WBK - Aviva Towarzystwo Ubezpieczeń Ogólnych S.A. and BZ WBK - Aviva Towarzystwo Ubezpieczeń na Życie S.A.	845 802	828 275
Total	889 372	871 491

Movements on investments in associates	01.01.2017- 31.12.2017	01.01.2016- 31.12.2016
As at the beginning of the period	871 491	831 142
Share of profits	58 264	55 439
Dividends	(44 861)	(10 827)
Other	4 478	(4 263)
Balance at the end of the period	889 372	871 491

Fair value of "Investment in associates" is presented in Note 43.

The table below presents information regarding The Group's share in capital of associate:

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

In thousands of PLN

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

	BZ WBK - Aviva Towarzystwo Ubezpieczeń na Życie S.A.		BZ WBK - Aviva Towarzystwo Ubezpieczeń Ogólnych S.A.	
	2017 *	2 016	2017 *	2 016
Loans and advances to banks	67 377	44 635	69 888	30 857
Financial assets held for trading	12 079	19 457	1 256	1 230
Financial assets available for sale	318 393	260 392	373 978	348 360
Deferred tax assets	705	646	981	908
Net life insurance assets where the deposit (investment) risk is incurred by the insuring party	387 534	545 539	-	-
Other settlements	22 523	24 512	56 494	42 057
Prepayments	163 842	127 946	-	12 875
Other items	818	1 205	859	1 173
Total assets	973 271	1 024 332	503 456	437 460
Technical insurance provisions	733 747	851 318	164 235	172 589
Reinsurers' share in provisions	(7 444)	(7 322)	(143 055)	(113 294)
Estimated recourses and recoveries (negative value)	-	-	(1 003)	(602)
Other liabilities	136 678	85 565	157 253	105 488
Prepayments and accruals	6 641	2 458	94 618	69 198
Special funds	35	26	33	33
Total liabilities	869 657	932 045	272 081	233 412
Income	180 571	201 104	156 972	154 987
Profit (loss) for the period	45 011	37 849	73 173	72 372
Dividends paid to BZ WBK	19 142	10 827	25 719	-

*Data are based on estimates of companies.

2016 data are based on audit financial report of companies BZ WBK - Aviva Towarzystwo Ubezpieczeń na Życie S.A. and BZ WBK - Aviva Towarzystwo Ubezpieczeń Ogólnych S.A.

Data published in Annual Report 2016 were based on estimates of companies. Difference between estimates and real data are irrelevant.

In thousands of PLN

25. Intangible assets

Intangible assets Year 2017	Licences, patents etc.	Other	Expenditure on intangible assets	Total
Gross value - beginning of the period	1 387 288	429 893	195 384	2 012 565
Additions from:				
- purchases	-	-	174 088	174 088
- intangible assets taken for use	145 582	13 338	-	158 920
- transfers	13	-	-	13
- merger	2 890	-	-	2 890
Disposals from:				
- liquidation	(44 085)	(2 091)	(669)	(46 845)
- intangible assets taken for use	-	-	(158 920)	(158 920)
- transfers	(2)	-	(11 362)	(11 364)
- merger	(2 890)	-	-	(2 890)
Gross value - end of the period	1 488 796	441 140	198 521	2 128 457
Accumulated depreciation - beginning of the period	(1 174 777)	(351 026)	-	(1 525 803)
Additions/disposals from:				
- current year amortization	(136 738)	(30 798)	-	(167 537)
- liquidation, sale	44 085	2 090	-	46 175
- transfers	-	9 034	-	9 034
Write down/Reversal of impairment write down	-	-	-	-
Accumulated depreciation- end of the period	(1 267 430)	(370 700)	-	(1 638 131)
Balance sheet value				
Purchase value	1 488 796	441 140	198 521	2 128 457
Accumulated depreciation	(1 267 430)	(370 700)	-	(1 638 130)
As at 31 December 2017	221 366	70 440	198 521	490 327

In thousands of PLN

Intangible assets Year 2016	Licences, patents etc.	Other	Expenditure on intangible assets	Total
Gross value - beginning of the period	1 307 659	429 027	170 653	1 907 339
Intangible assets acquired in a business combination	745	-	-	745
Additions from:				
- purchases	-	-	159 181	159 181
- intangible assets taken for use	132 505	7 503	-	140 008
- transfers	335	3	6 173	6 511
Disposals from:				
- liquidation	(53 956)	(6 640)	(107)	(60 703)
- intangible assets taken for use	-	-	(140 009)	(140 009)
- transfers	-	-	(507)	(507)
Gross value - end of the period	1 387 288	429 893	195 384	2 012 565
Accumulated depreciation - beginning of the period	(1 122 378)	(319 274)	-	(1 441 652)
Accumulated depreciation acquired in a business combinations	(676)	-	-	(676)
Additions/disposals from:				
- current year amortization	(113 416)	(30 491)	-	(143 907)
- liquidation, sale	53 441	6 535	-	59 976
- transfers	8 145	(8 145)	-	-
Write down/Reversal of impairment write down	107	349	-	456
Accumulated depreciation- end of the period	(1 174 777)	(351 026)	-	(1 525 803)
Balance sheet value				
Purchase value	1 387 288	429 893	195 384	2 012 565
Accumulated depreciation	(1 174 777)	(351 026)	-	(1 525 803)
As at 31 December 2016	212 511	78 867	195 384	486 762

26. Goodwill

As at 31 December 2017 the goodwill covered the following items:

- PLN 1,688,516 k - goodwill arising from the merger of Bank Zachodni WBK and Kredyt Bank on 4 January 2013,
- PLN 23,540 k – goodwill arising from the fact that Bank Zachodni WBK holds 60% shares of Santander Consumer Bank, which, in turn, has 50% stake in PSA Finance Polska. Bank Zachodni WBK discloses non-controlling interests representing 70% of share capital and voting power at the General Meetings of PSA Finance Polska and, indirectly, PSA Consumer Finance Polska (for more information, see Note 50).

In the corresponding period, at 31 December 2016 the goodwill was PLN 1,688,516 k.

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

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

In 2017 and in the corresponding period, the Group conducted tests for impairment of goodwill arising from the merger with Kredyt Bank on 4 January 2013. The carrying amount as at 31 December 2017 was PLN 1,688,516 k (the same as at 31 December 2016).

Recoverable amount based on value in use

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

Taking into account the stability of Bank Zachodni WBK Group 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:

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

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

Financial projection

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

Discount rate

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

Growth rate in the period beyond the financial projections

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

Minimum solvency ratio imposed by the regulator

An increase in the required capital amount results in a decrease in the amount of capital available for distribution as part of the test. On 1 January 2018, the following legal provisions take effect: higher capital requirements for 50% profit distribution, additional capital requirements for risk attached to mortgage loans (0.54 p.p.), additional conservation buffer of 1.25 p.p., buffer of other systemically important institution of 0.5 p.p. (determined individually by the KNF) and systemic risk buffer of 3.0 p.p., increased by 1.5 p.p. In addition, banks are required to adjust dividend yield depending on the share of FX home loans in the credit portfolio. All the above factors have a negative impact on the capital available for distribution and, consequently, on the results of the goodwill impairment test.

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

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

Test for impairment of goodwill arising from the purchase of shares of PSA Finance Polska

The bank did not conduct the test for impairment of goodwill arising from the acquisition of shares of PSA Finance Polska and, indirectly, PSA Consumer Finance Polska by Santander Consumer Bank. Goodwill calculated as an excess of the value of non-controlling interests (70%) and the payment made over the carrying amount of the identified net assets is not significant.

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

In thousands of PLN

27. Property, plant and equipment

Property, plant & equipment Year 2017	Land and buildings	Equipment	Transportation means	Other fixed assets	Capital expenditures	Total
Gross value - beginning of the period	960 363	699 615	145 207	278 394	152 659	2 236 238
Additions from:						
- purchases	-	-	-	-	240 121	240 121
- leasing	-	-	9 062	-	-	9 062
- fixed assets taken for use	27 253	136 875	45 940	15 842	-	225 910
- transfers	-	146	2 436	10	2 280	4 872
- merger	28	381	-	53	-	462
Disposals from:						
- sale, liquidation, donation	(44 330)	(30 308)	(31 572)	(30 919)	(225)	(137 354)
- fixed assets taken for use	-	-	-	-	(225 910)	(225 910)
- transfers	-	-	(15 537)	(62)	(86)	(15 685)
- merger	(28)	(381)	-	(53)	-	(462)
Gross value - end of the period	943 286	806 328	155 536	263 265	168 839	2 337 254
Accumulated depreciation - beginning of the period	(621 431)	(468 323)	(32 154)	(236 032)	-	(1 357 940)
Additions/disposals from:						
- current year amortization	(36 634)	(77 772)	(22 934)	(14 056)	-	(151 396)
- sale, liquidation, donation	35 380	29 812	9 048	30 008	-	104 248
- transfers	17	32	6 568	239	-	6 856
Write down/Reversal of impairment write down	(8 304)	-	(1)	-	-	(8 305)
Accumulated depreciation- end of the period	(630 972)	(516 251)	(39 473)	(219 841)	-	(1 406 537)
Balance sheet value						
Purchase value	943 286	806 328	155 536	263 265	168 839	2 337 254
Accumulated depreciation	(630 972)	(516 251)	(39 473)	(219 841)	-	(1 406 537)
As at 31 December 2017	312 314	290 077	116 063	43 424	168 839	930 717

In thousands of PLN

Property, plant & equipment Year 2016	Land and buildings	Equipment	Transportation means	Other fixed assets	Capital expenditures	Total
Gross value - beginning of the period	985 451	625 042	120 374	310 922	132 927	2 174 716
Property, plant and equipment acquired in a business combination	429	1 740	1 722	997	-	4 888
Additions from:						
- purchases	-	-	-	-	194 802	194 802
- leasing	-	-	30 680	-	-	30 680
- fixed assets taken for use	26 243	101 509	30 435	11 541	-	169 728
- transfers	58	18 728	4 390	676	922	24 774
Disposals from:						
- sale, liquidation, donation	(51 314)	(46 520)	(13 041)	(27 014)	-	(137 889)
- fixed assets taken for use	-	-	-	-	(169 727)	(169 727)
- transfers	(504)	(884)	(29 353)	(18 728)	(6 265)	(55 734)
Gross value - end of the period	960 363	699 615	145 207	278 394	152 659	2 236 238
Accumulated depreciation - beginning of the period combinations	(613 329)	(433 400)	(34 664)	(262 830)	-	(1 344 223)
	(180)	(1 605)	(101)	(975)	-	(2 861)
Additions/disposals from:						
- current year amortization	(35 062)	(64 752)	(20 508)	(12 991)	-	(133 313)
- sale, liquidation, donation	39 433	46 508	6 878	25 517	-	118 336
- transfers	27	(15 074)	16 241	15 061	-	16 255
Write down/Reversal of impairment write down	(12 320)	-	-	186	-	(12 134)
Accumulated depreciation- end of the period	(621 431)	(468 323)	(32 154)	(236 032)	-	(1 357 940)
Balance sheet value						
Purchase value	960 363	699 615	145 207	278 394	152 659	2 236 238
Accumulated depreciation	(621 431)	(468 323)	(32 154)	(236 032)	-	(1 357 940)
As at 31 December 2016	338 932	231 292	113 053	42 362	152 659	878 298

In thousands of PLN

28. Net deferred tax assets

Deferred tax assets	31.12.2017	Changes to equity*	Changes to financial result	Changes in temporary differences	31.12.2016
Provisions for impairment of loans and advances	666 968	-	16 536	16 536	650 432
Valuation of derivative financial instruments	364 432	-	(353 780)	(353 780)	718 212
Cash flow hedges valuation	20 509	(4 743)	-	(4 743)	25 252
Other provisions	163 492	-	17 352	17 352	146 140
Deferred income	509 045	-	66 633	66 633	442 412
Differences between carrying and tax value of lease	373 662	-	76 007	76 007	297 655
Unrealised interest expenses on loans, deposits and securities	126 619	-	35 007	35 007	91 612
Other negative temporary differences	25 242	-	12 223	12 223	13 019
Total assets of deferred tax	2 249 969	(4 743)	(130 022)	(134 765)	2 384 734

Deferred tax liabilities	31.12.2017	Changes to equity*	Changes to financial result	Changes in temporary differences	31.12.2016
Revaluation of financial instruments available for sale	(188 908)	(101 417)	-	(101 417)	(87 491)
Provisions for retirement allowances	(126)	1 788	-	1 788	(1 914)
Valuation of derivative financial instruments	(261 617)	-	105 928	105 928	(367 545)
Unrealised interest income on loans, securities and interbank deposits	(179 373)	-	31 125	31 125	(210 498)
Prepayments regarding amortization of applied investment relief	(1 751)	-	125	125	(1 876)
Difference between balance sheet and taxable value of non-financial assets	8 466	-	3 340	3 340	5 126
Unrealised FX translation differences from b/s valuation of receivables and liabilities	(8 773)	-	509	509	(9 282)
Valuation of shares / interests in subsidiaries	(146 966)	-	816	816	(147 782)
Other positive temporary differences	(56 694)	-	(27 544)	(27 544)	(29 150)
Total liabilities deferred tax	(835 742)	(99 629)	114 299	14 670	(850 412)

Net deferred tax assets	1 414 227	(104 372)	(15 723)	(120 095)	1 534 322
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*The changes carried in equity do not reflect the deferred tax effect in relation to the item recognised in non-controlling interests.

As at 31.12.2017 the assets in the calculation of deferred tax assets do not include purchased receivables in the amount of gross PLN 5,114 k and provisions for loans that do not become tax expense in the amount of gross PLN 65,960 k.

Deferred tax assets	31.12.2016	Changes to equity*	Changes to financial result	Changes in temporary differences	31.12.2015
Provisions for impairment of loans and advances	650 432	-	41 699	41 699	608 733
Valuation of derivative financial instruments	718 212	-	(49 632)	(49 632)	767 844
Cash flow hedges valuation	25 252	(20 637)	-	(20 637)	45 889
Other provisions	146 140	-	3 215	3 215	142 925
Deferred income	442 412	-	35 685	35 685	406 727
Differences between carrying and tax value of lease	297 655	-	106 734	106 734	190 921
Unrealised interest expenses on loans, deposits and securities	91 612	-	1 715	1 715	89 897
Other negative temporary differences	13 019	-	(2 388)	(2 388)	15 407
Total assets of deferred tax	2 384 734	(20 637)	137 028	116 391	2 268 343

Deferred tax liabilities	31.12.2016	Changes to equity*	Changes to financial result	Changes in temporary differences	31.12.2015
Revaluation of financial instruments available for sale	(87 491)	140 283	-	140 283	(227 774)
Provisions for retirement allowances	(1 914)	(1 304)	-	(1 304)	(610)
Valuation of derivative financial instruments	(367 545)	-	56 063	56 063	(423 608)
Unrealised interest income on loans, securities and interbank deposits	(210 498)	-	(27 838)	(27 838)	(182 660)
Prepayments regarding amortization of applied investment relief	(1 876)	-	327	327	(2 203)
Difference between balance sheet and taxable value of non-financial assets	5 126	-	2 951	2 951	2 175
Unrealised FX translation differences from b/s valuation of receivables and liabilities	(9 282)	-	(790)	(790)	(8 492)
Valuation of shares / interests in subsidiaries	(147 782)	-	4 882	4 882	(152 664)
Other positive temporary differences	(29 150)	-	(8 451)	(8 451)	(20 699)
Total liabilities deferred tax	(850 412)	138 979	27 144	166 123	(1 016 535)

Net deferred tax assets	1 534 322	118 342	164 172	282 514	1 251 808
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*The changes carried in equity do not reflect the deferred tax effect in relation to the item recognised in non-controlling interests.

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.

In thousands of PLN

Movements on net deferred tax	31.12.2017	31.12.2016
As at the beginning of the period	1 534 322	1 251 808
Changes on net deferred tax in a business combination	-	35 387
Changes recognised in income statement	(14 885)	127 976
Changes recognised in other comprehensive income	(104 372)	118 342
Transfer	(838)	809
Balance at the end of the period	1 414 227	1 534 322

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

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

The impact of IFRS 9 implementation on the deferred tax effect is presented in Note 2.2.

29. Assets classified as held for sale

Assets classified as held for sale	31.12.2017	31.12.2016
Land and buildings	8	608
Other fixed assets	95	21
Total	103	629

30. Other assets

Other assets	31.12.2017	31.12.2016
Interbank settlements	142 701	106 829
Sundry debtors	756 662	443 476
Prepayments	128 892	125 164
Repossessed assets	103	24 567
Settlements of stock exchange transactions	31 711	21 385
Other	4 999	4 293
Total	1 065 068	725 714
of which financial assets*	931 074	571 690

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

31. Deposits from banks

Deposits from banks	31.12.2017	31.12.2016
Term deposits	64 023	98 531
Loans from other banks	1 994 759	1 945 101
Current accounts	724 301	517 649
Total	2 783 083	2 561 281

As at 31.12.2017 fair value adjustment for hedged deposit totaled PLN nil (as at 31.12.2016 – PLN nil).

Fair value of "Deposits from banks" is presented in Note 43.

In thousands of PLN

Movements in loans received from banks	31.12.2017	31.12.2016
As at the beginning of the period	1 945 101	574 693
Increase (due to):	985 114	1 911 927
- drawing of loans	953 810	1 849 792
- interest on loans	31 304	21 348
- FX differences and other	-	40 787
Decrease (due to):	(935 456)	(541 519)
- repayment of loans	(841 644)	(522 731)
- interest repayment	(31 700)	(18 788)
- FX differences and other	(62 112)	-
As at the end of the period	1 994 759	1 945 101

32. Deposits from customers

Deposits from customers	31.12.2017	31.12.2016
Deposits from individuals	64 987 719	63 547 942
Term deposits	21 911 544	23 711 846
Current accounts	42 948 226	39 650 731
Other	127 949	185 365
Deposits from enterprises	42 170 092	45 709 065
Term deposits	17 486 056	22 608 733
Current accounts	20 481 778	18 464 132
Loans	3 552 388	4 075 897
Other	649 870	560 303
Deposits from public sector	4 323 324	3 265 450
Term deposits	2 085 917	1 504 136
Current accounts	2 233 410	1 747 709
Other	3 997	13 605
Total	111 481 135	112 522 457

As at 31.12.2017 deposits held as collateral totaled PLN 271,147 k (as at 31.12.2016 - PLN 289,695 k).

Fair value of "Deposits from customers" is presented in Note 43.

Movements in loans received from other financial institutions	31.12.2017	31.12.2016
As at the beginning of the period	4 075 897	3 002 047
Increase (due to):	483 022	1 572 132
- drawing of loans	466 860	1 425 007
- interest on loans	16 162	14 165
- FX differences and other	-	132 960
Decrease (due to):	(1 006 531)	(498 282)
- repayment of loans	(726 764)	(486 245)
- interest repayment	(16 513)	(12 037)
- FX differences and other	(263 254)	-
As at the end of the period	3 552 388	4 075 897

In thousands of PLN

33. Subordinated liabilities

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

Movements in subordinated liabilities	31.12.2017	31.12.2016
As at the beginning of the period	440 457	526 634
Increase (due to):	1 133 436	31 671
- interest on subordinated loan	33 564	18 919
- FX differences	-	12 752
- reclassification *	1 099 872	-
Decrease (due to):	(85 291)	(117 848)
- subordinated loans repayment	-	(100 000)
- interest repayment	(27 528)	(17 848)
- FX differences	(57 763)	-
Subordinated liabilities - as at the end of the period	1 488 602	440 457
Short-term	11 257	1 604
Long-term (over 1 year)	1 477 345	438 853

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

Other details on these liabilities are disclosed in Note 5.

34. Debt securities in issue

Issuance of debt securities in 2017 (non-matured securities)	Nominal value	Currency	Redemption date
Series F bank securities	750 000	PLN	19.02.2018
Series A	700 000	PLN	18.04.2018
SCB00038	300 000	PLN	09.08.2021
SCB00039	252 100	PLN	09.10.2020
SCB00040	261 400	PLN	07.10.2022
SCB00041	60 000	PLN	07.10.2022

Issuance of debt securities in 2016 (non-matured securities)	Nominal value	Currency	Redemption date
Series D	185 000	PLN	26.02.2017
Series C bank securities	100 000	PLN	17.02.2017
Series E	120 000	EUR	03.12.2026
SCB00031	40 000	PLN	23.02.2018
SCB00032	20 000	PLN	26.08.2019
SCB00037	40 000	PLN	02.12.2019
SCB00033	50 000	PLN	26.02.2020
SCB00034	140 000	PLN	05.05.2020
SCB00035	82 000	PLN	29.05.2020
SCB00036	100 000	PLN	10.08.2020
Securitized bonds Float sale	1 225 000	PLN	16.09.2026

In thousands of PLN

Movements in debt securities in issue	31.12.2017	31.12.2016
As at the beginning of the period	5 529 187	4 320 891
Increase (due to):	3 745 653	2 894 670
- debt securities in issue	3 562 288	2 762 880
- interest on debt securities in issue	167 135	131 790
- FX differences	16 230	-
Decrease (due to):	(3 379 026)	(1 686 374)
- debt securities redemption	(2 095 000)	(1 554 700)
- reclassification*	(1 099 872)	-
- FX differences	(21 786)	-
- interest repayment	(162 368)	(131 674)
As at the end of the period	5 895 814	5 529 187

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

35. Provisions

Provisions	31.12.2017	31.12.2016
Provisions for off-balance sheet credit facilities	50 652	50 746
Provisions for legal claims	99 463	74 396
Provisions for restructuring *	3 019	4 986
Total	153 134	130 128

* Provisions for restructuring acquired as a result of the acquisition of control over Santander Consumer Bank on July 1, 2014 in the amount of PLN 15,547 k (as at 31.12.2017 in the amount of PLN 3,019 k) referred to:

- restructuring of employment in the bank PLN 3,323 k (as at 31.12.2017 in the amount of PLN 955 k),
- liquidation of branches PLN 12,224 k. (as at 31.12.2017 in the amount of PLN 2,064 k).

The restructuring is related to the business reorganisation plan for Santander Consumer Finance (SCF) in Poland which was adopted by the Group in 2010. The plan was adopted after SCF Group had taken control over AIG Bank Polska S.A. and in the wake of subsequent restructuring actions carried out in the years 2013-2014 (amongst others, restructuring of the business transferred from Santander Consumer Finance Sp z o.o.). Provision has also been associated with the implementation of the Operational Excellence Programme in 2015.

Change in provisions 31.12.2017	Provisions for legal claims	Provisions for off balance sheet credit facilities	Provisions for restructuring	Total
As at the beginning of the period	74 396	50 746	4 986	130 128
Provision charge	63 742	77 447	4 754	145 943
Utilization	(12 142)	(517)	-	(12 659)
Write back	(26 533)	(77 024)	(6 721)	(110 278)
Other changes	-	-	-	-
Balance at the end of the period	99 463	50 652	3 019	153 134
Short-term	99 463	43 693	3 019	146 175
Long-term	-	6 959	-	6 959

In thousands of PLN

Change in provisions 31.12.2016	Provisions for legal claims	Provisions for off balance sheet credit facilities	Provisions for restructuring	Total
As at the beginning of the period	48 582	75 340	8 648	132 570
Provision charge	93 280	93 586	377	187 243
Utilization	(66 157)	835	-	(65 322)
Write back	(1 309)	(119 015)	(4 000)	(124 324)
Other changes	-	-	(39)	(39)
Balance at the end of the period	74 396	50 746	4 986	130 128
Short-term	74 396	41 752	4 986	121 134
Long-term	-	8 994	-	8 994

36. Other liabilities

Other liabilities	31.12.2017	31.12.2016
Settlements of stock exchange transactions	25 851	25 314
Interbank settlements	952 192	585 606
Employee provisions	407 722	375 959
Other provisions	3 300	3 300
Sundry creditors	511 537	512 010
Other deferred and suspended income	249 880	250 059
Public and law settlements	84 971	86 298
Accrued liabilities	532 117	436 249
Finance lease related settlements	99 306	72 901
Other	1 898	866
Total	2 868 774	2 348 562
of which financial liabilities *	2 532 025	2 011 339

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

Change in provisions 31.12.2017	Employee provisions	Other provisions	Total
	<i>of which: Provisions for retirement allowances</i>		
As at the beginning of the period	375 959	60 397	3 300
Provision charge	330 771	14 270	-
Utilization	(232 256)	-	-
Write back	(66 675)	(1 941)	-
Other changes	(77)	-	-
Balance at the end of the period	407 722	72 726	3 300
Short-term	334 996	-	3 300
Long-term	72 726	72 726	-

In thousands of PLN

Change in provisions 31.12.2016	Employee provisions	Other provisions	Total
	<i>of which: Provisions for retirement allowances</i>		
As at the beginning of the period	380 724	63 209	384 030
Provision acquired in a business combination	747	46	747
Provision charge	327 004	1 046	327 004
Utilization	(269 233)	-	(269 239)
Write back	(63 543)	(319)	(63 543)
Other changes	260	(3 585)	260
Balance at the end of the period	375 959	60 397	379 259
Short-term	315 562	-	318 862
Long-term	60 397	60 397	60 397

Employee related provisions and accruals consists of items outlined in Note 51.

37. Share capital

31.12.2017

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

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

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

In thousands of PLN

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%.

38. Other reserve capital

Other reserve capital	31.12.2017	31.12.2016
General banking risk fund	649 810	649 810
Share premium	7 035 424	7 035 424
Other reserves of which:	9 234 895	8 106 321
<i>Reserve capital</i>	8 953 176	7 879 974
<i>Supplementary capital</i>	937 954	890 172
<i>Adjustment to equity from acquisition/loss of controlling interest in subsidiaries</i>	(656 234)	(663 825)
Total	16 920 129	15 791 555

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

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

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

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

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

In thousands of PLN

39. Revaluation reserve

Revaluation reserve 31.12.2017	Total gross	Deferred tax adjustment	Total nett
Opening balance, of which:	340 856	(64 763)	276 093
Debt and equity securities	465 234	(88 396)	376 838
Valuation related to cash flow hedge	(134 282)	25 514	(108 768)
Actuarial gains/losses on retirement allowances	9 904	(1 881)	8 023
Change in valuation of debt and equity securities available for sale	549 139	(104 336)	444 802
Decrease in revaluation reserve related to sale of investments	(23 503)	4 465	(19 037)
Change of cash flow hedges valuations	24 931	(4 737)	20 193
Change of actuarial gains/losses on retirement allowances	(9 365)	1 779	(7 586)
Closing balance, of which:	882 058	(167 592)	714 466
Debt and equity securities	990 870	(188 267)	802 603
Valuation related to cash flow hedge	(109 351)	20 777	(88 574)
Actuarial gains/losses on retirement allowances	539	(102)	437

Revaluation reserve 31.12.2016	Total gross	Deferred tax adjustment	Total nett
Opening balance, of which:	959 153	(182 239)	776 914
Debt and equity securities	1 197 303	(227 489)	969 814
Valuation related to cash flow hedge	(241 359)	45 859	(195 500)
Actuarial gains/losses on retirement allowances	3 209	(609)	2 600
Change in valuation of debt and equity securities available for sale	(459 368)	87 280	(372 088)
Decrease in revaluation reserve related to sale of investments	(272 701)	51 813	(220 888)
Change of cash flow hedges valuations	131 726	(25 028)	106 698
Decrease in revaluation reserve related to sale of cash flow hedges	(24 649)	4 683	(19 966)
Change of actuarial gains/losses on retirement allowances	6 695	(1 272)	5 423
Closing balance, of which:	340 856	(64 763)	276 093
Debt and equity securities	465 234	(88 396)	376 838
Valuation related to cash flow hedge	(134 282)	25 514	(108 768)
Actuarial gains/losses on retirement allowances	9 904	(1 881)	8 023

In thousands of PLN

40. Non - controlling interests

Name of the subsidiary	Country of incorporation and place of business	Percentage share of non-controlling interests in share capital / voting rights		Net profit for the period attributable to non-controlling interests		Accumulated non-controlling interests	
		31.12.2017	31.12.2016	31.12.2017	31.12.2016	31.12.2017	31.12.2016
BZ WBK Towarzystwo Funduszy Inwestycyjnych S.A.	Poland	50,00	50,00	33 252	24 634	42 507	46 802
BZ WBK Asset Management S.A.	Poland	-	50,00	-	1 763	-	-
Santander Consumer Bank S.A.	Poland	40,00	40,00	272 208	190 848	1 393 902	1 190 847
Total				305 460	217 245	1 436 409	1 237 649

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

	BZ WBK Towarzystwo Funduszy Inwestycyjnych S.A.					
	BZ WBK Towarzystwo Funduszy Inwestycyjnych S.A.		BZ WBK Asset Management S.A.		Santander Consumer Bank S.A.	
	31.12.2017	31.12.2016	31.12.2017	31.12.2016	31.12.2017	31.12.2016
Loans and advances to banks	79 045	86 904	-	-	130 022	111 871
Loans and advances to customers	-	-	-	-	13 891 179	13 370 604
Investments in subsidiaries	-	-	-	-	154 775	157 552
Financial assets available for sale	-	-	-	-	2 608 443	2 959 214
Net deferred tax assets	2 234	1 573	-	-	468 338	425 644
Other items	36 352	29 457	-	-	394 257	357 384
Total assets	117 631	117 934	-	-	17 647 014	17 382 269
Deposits from banks	-	-	-	-	152 739	73 339
Deposits from customers	-	-	-	-	10 846 837	10 889 396
Sell-buy-back transactions	-	-	-	-	1 171 179	1 632 613
Debt securities in issue	-	-	-	-	1 676 559	1 466 769
Other items	32 617	24 331	-	-	609 633	615 118
Total liabilities	32 617	24 331	-	-	14 456 947	14 677 235
Income	314 031	258 932	-	8 648	1 944 552	1 735 893
Profit (loss) for the period	66 503	49 267	-	3 525	649 136	451 408
Dividends paid to non-controlling interests	37 546	29 847	-	22 344	73 416	173 834

41. Hedge accounting

Bank Zachodni WBK Group uses hedging strategies within hedge accounting in line with the risk management principles set out in note 4 to the consolidated financial statements.

Fair value hedges

Bank Zachodni WBK Group uses fair value hedge accounting in relation to the following classes of financial instruments:

- Debt securities with a fixed interest rate in PLN and denominated in EUR;
- Loans with a fixed interest rate granted by the Bank in PLN;
- Loans with a fixed interest rate taken out by BZ WBK Leasing.

To hedge the fair value, Bank Zachodni WBK uses Interest Rate Swaps and Overnight Indexed Swaps, for which the Bank pays a fixed interest rate and receives a variable interest rate. The hedged risk is the change in the fair value of an instrument or a portfolio resulting from changes in market interest rates. The transactions do not hedge against fair value changes relating to 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.

In thousands of PLN

The tables below contain details about individual groups of hedge transactions as at 31.12.2017 and 31.12.2016:

31.12.2017	Bonds	Loans
Nominal value of hedging position	1 979 709	425 000
Measurement to fair value of hedging instrument	(104 434)	3 763
Fair value adjustment of hedged instrument due to hedged risk asset/(liability)	107 005	(3 817)
Hedged risk	Interest rate risk	Interest rate risk
Period over which the instruments have an impact on the bank's results	up to 2025	up to 2021

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

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

In December 2015, Bank Zachodni WBK S.A. 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 terms originally agreed for individual hedging relationships. PLN 1,199 k was recognised in the income statement for 2017 and PLN 262 k will be reflected in the income statement by the end of 2018.

As at 31.12.2017, BZ WBK Leasing had three derivative instrument - IRS (Interest Rate Swap), designated to hedge accounting of cashflows, which hedges the company against the risk of credit margin and the risk of credit interest rate. The nominal value of the transaction is PLN 905,172 k.

Transactions were made to hedge the interest rate risk and the credit margin risk arising from three loans raised with international financial institutions - with fixe interest rates. These loans finance lease agreements based on 1M EURIBOR – hence the need to match the moment of revaluation of liabilities and the moment of revaluation of assets.

There was 1 such transaction of PLN 599,079 k in BZ WBK Leasing's financial statements as at 2016 year-end. The fair value (including the accrued interest) totals PLN (365) k as at the balance sheet day.

Details of the hedging transaction of BZ WBK Leasing S.A. as at 31.12.2017 and 31.12.2016 are presented in tables below:

31.12.2017	BZ WBK Leasing S.A.
Nominal value of hedging position	905 172
Measurement to fair value of hedging instrument	(3 422)
Fair value adjustment of hedged instrument due to hedged risk asset/(liability)	3 422
Hedged risk	Interest rate risk
Period over which the instruments have an impact on the BZ WBK Leasing results	up to 2022

31.12.2016	BZ WBK Leasing S.A.
Nominal value of hedging position	599 079
Measurement to fair value of hedging instrument	(392)
Fair value adjustment of hedged instrument due to hedged risk asset/(liability)	392
Hedged risk	Interest rate risk
Period over which the instruments have an impact on the BZ WBK Leasing results	up to 2022

Cash flow hedging

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

The Group's hedging strategies are designed to protect the Group'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.

In thousands of PLN

Hedging relationships are created using Interest Rate Swaps, FX 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 December 2017, the nominal value of the hedging item was PLN 12,117,739 k (31 December 2016 – PLN 16,644,130 k). Measurement to fair value of the hedging instrument was PLN (109,351) k (31 December 2016 – PLN (134,281) k); the same amount, less deferred tax, is recognised in comprehensive income and accumulated in the Bank's equity under revaluation reserve and are presented in note 39. Hedging instruments have been concluded for a period of time until 2028.

The non-effective portion of measurement of the cash flow hedge was PLN (10,703) k as of 31.12.2017 and PLN 11,170 k as of 31.12.2016. It was taken to the 'Net trading income and revaluation' line of the profit and loss account.

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

The Group 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 Group's balance sheet portfolio.

	31.12.2017	31.12.2016
	Balance sheet value	Balance sheet value
Liabilities valued at amortised cost (contains sell-buy-back)	2 650 846	1 632 613
Fair value of securities held as collateral for sell-buy-back/repo transactions	2 990 774	1 827 329
Sell-buy-back transactions	31.12.2017	31.12.2016
Sell-buy-back transactions from banks	986 398	1 632 613
Sell-buy-back transactions from customers	1 664 448	-
Total	2 650 846	1 632 613

The foregoing items are not removed from the balance sheet, because the Group 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.

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 Group, as well as power to dispose them.

The Group 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 Group does not retain any rewards or risks attaching to these assets.

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

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

In thousands of PLN

43. Fair value

Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date.

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

Assets	31.12.2017		31.12.2016	
	Book Value	Fair Value	Book Value	Fair Value
Cash and balances with central banks	4 146 222	4 146 222	4 775 660	4 775 660
Loans and advances to banks	2 136 474	2 136 474	3 513 278	3 513 278
Financial assets held for trading	3 416 108	3 416 108	3 180 985	3 180 985
Hedging derivatives	218 061	218 061	67 645	67 645
Loans and advances to customers	107 839 897	108 488 102	103 068 538	102 882 533
Financial assets available for sale	28 415 812	28 415 812	29 307 878	29 307 878
Investments in associates	889 372	889 372	871 491	871 491
Liabilities				
Deposits from banks	2 783 083	2 783 083	2 561 281	2 561 281
Hedging derivatives	578 798	578 798	2 023 344	2 023 344
Financial liabilities held for trading	1 237 704	1 237 704	1 809 060	1 809 060
Subordinated liabilities	1 488 602	1 500 989	440 457	564 402
Deposits from customers	111 481 135	111 496 805	112 522 457	112 548 047

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 Group has financial instruments which in accordance with the IFRS are not carried at fair value in the consolidated financial statements. 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 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 Group 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 Group 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 31.12.2017 and in the comparable periods the Group 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 Group allocates to this level fixed-rate State Treasury bonds, treasury bills, shares of listed companies and WIG 20 futures.

Level II (the measurement methods based on market-derived parameters): This level includes derivative instruments. Derivative instruments are measured using discounted cash flow models based on the discount curve derived from the inter-bank market.

Level III (measurement methods using material non-market parameters): This 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 and debt securities.

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

Valuation of major capital investments classified to Level III:

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

are made semi-annually by specialized units of the Bank using income methods based on discounted cash flows, where the most important variables of the model are the level of forecasted dividends and the risk free rate. During the reporting period revaluation of above equity investments has been made in the total amount of 33.8 million PLN and recognized in the revaluation reserve.

As at 31.12.2017 and in the comparable periods the Group classified its financial instruments to the following fair value levels:

31.12.2017	Level I	Level II	Level III	Total
Financial assets				
Financial assets held for trading	2 189 110	1 226 551	447	3 416 108
Hedging derivatives	-	218 061	-	218 061
Financial assets available for sale - debt securities	27 462 401	-	32 532	27 494 933
Financial assets available for sale- equity securities	19 328	-	901 551	920 879
Total	29 670 839	1 444 612	934 530	32 049 981
Financial liabilities				
Financial liabilities held for trading	-	-	-	-
Hedging derivatives	-	1 237 704	-	1 237 704
Total	-	1 816 502	-	1 816 502

31.12.2016	Level I	Level II	Level III	Total
Financial assets				
Financial assets held for trading	282 769	2 897 965	251	3 180 985
Hedging derivatives	-	67 645	-	67 645
Financial assets available for sale - debt securities	16 025 497	12 360 090	38 240	28 423 827
Financial assets available for sale- equity securities	34 473	-	849 578	884 051
Total	16 342 739	15 325 700	888 069	32 556 508
Financial liabilities				
Financial liabilities held for trading	80 129	1 728 931	-	1 809 060
Hedging derivatives	-	2 023 344	-	2 023 344
Total	80 129	3 752 275	-	3 832 404

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 assets available for sale - debt securities	Financial assets available for sale - equity securities	Financial liabilities held for trading
31.12.2017				
Beginning of the period	251	38 240	849 578	-
Profits or losses	-	-	-	-
<i>recognised in income statement (unrealised)</i>	(29)	-	-	-
<i>recognised in equity</i>	-	-	68 337	-
Purchase	1 057	-	2 036	-
Sale	(832)	-	(18 400)	-
Transfer between levels	-	(5 708)	-	-
At the period end	447	32 532	901 551	-

Level III	Financial assets			Financial liabilities
	Financial assets held for trading	Financial assets available for sale - debt securities	Financial assets available for sale - equity securities	Financial liabilities held for trading
31.12.2016				
Beginning of the period	1 839	-	1 115 212	-
Profits or losses	81	-	3 920	-
<i>recognised in income statement (unrealised)</i>	81	-	63 651	-
<i>recognised in equity</i>	-	-	(59 731)	-
Purchase	340	-	9 900	-
Sale	(2 009)	-	(279 454)	-
Transfer between levels	-	38 240	-	-
At the period end	251	38 240	849 578	-

44. Contingent liabilities

Significant court proceedings

As at 31.12.2017 no proceedings were instituted by court or by state administration agencies with relation to any claims made by or against the Bank or its subsidiaries amounting to a minimum of 10% of the Group's equity.

The value of all litigation amounts to PLN 1,080,768 k, which is ca 4.63% of the Group's equity. This amount includes PLN 717,617k claimed by the Group, PLN 359,362 k in claims against the Group and PLN 3,789 k of the Group's receivables due to bankruptcy or arrangement cases.

On 20.10.2017, Bank Zachodni WBK received a notice of a class action instituted by the borrowers who had loans indexed to the CHF, originated by the former Kredyt Bank. The total value of the claim, estimated as at the reporting date, is PLN 32.3 m. However, this amount is very likely to be changed as new borrowers join the class action.

As at 31.12.2017 the amount of significant court proceedings which had been completed amounted to PLN 532,519 k.

As at 31.12.2017, the value of provisions for legal claims was PLN 99,463 k. In 10 cases against the Bank, where the claim value was high, a provision of PLN 40,983 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 35.

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 or its subsidiaries amounting to a minimum of 10% of the Group's equity.

In thousands of PLN

The value of all litigation amounts to PLN 780,750 k, which is ca 3.71% of the Group's equity. This amount includes PLN 518,256 k claimed by the Group, PLN 221,634 k in claims against the Group and PLN 40,860 k of the Group's receivables due to bankruptcy or arrangement cases. In 2016, there was a significant year-on-year increase in the amount claimed by the Group (from PLN 256,443 k to PLN 518,256 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.

As at 31.12.2016 the amount of significant court proceedings which had been completed amounted to PLN 451,697 k.

As at 31.12.2016, the value of provisions for legal claims was PLN 74,396 k, including for significant 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.

Off-balance sheet liabilities

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

Contingent liabilities - sanctioned	31.12.2017	31.12.2016
Liabilities sanctioned		
- financial	24 642 271	23 243 064
- credit lines	20 279 546	19 134 360
- credit cards debits	3 730 667	3 419 031
- import letters of credit	624 207	655 624
- term deposits with future commencement term	7 851	34 049
- guarantees	4 885 661	4 182 758
Allowance for impairment	(50 652)	(50 746)
Total	29 477 280	27 375 076

45. 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 and Santander Consumer Bank applied 0.55% (i.e. the same rate as in 2016) of funds deposited in all accounts with the bank, being the basis for calculating the obligatory reserve.

As at 31.12. 2017, assets allocated to that end totalled PLN 605,429 k compared with PLN 597,789 k a year before.

In 2016, deposits opened with financial institutions to secure the value of transactions totalled PLN 772,961 k (PLN 2,190,757k as at 31.12. 2016).

In 2017, the Group accepted PLN 500,105 k worth of deposits securing transactions (vs. PLN 232,670 k in 2016).

Other assets pledged and liabilities accepted as collateral are disclosed in Notes 32 and 42.

46. Finance and operating leases

Finance leases

Lease agreements where the Group acts as a lessor

Bank Zachodni WBK Group operates on the leasing market through leasing companies which specialise in funding vehicles, machines and equipment for businesses and personal customers and property.

The item "Loans and advances to customers" contains the following amounts relating to the finance lease obligations:

In thousands of PLN

Finance leases gross receivables - maturity	31.12.2017	31.12.2016
less than 1 year	2 724 540	2 340 974
between 1 and 5 years	4 452 169	4 041 964
over 5 years	115 819	128 190
Total	7 292 528	6 511 128

Present value of minimum lease payments - maturity	31.12.2017	31.12.2016
less than 1 year	2 751 560	2 257 106
between 1 and 5 years	4 011 195	3 749 807
over 5 years	86 205	91 586
Total	6 848 960	6 098 499

Reconciliation between the gross investment and the present value of minimum lease payments	31.12.2017	31.12.2016
Finance lease gross receivables	7 292 528	6 511 128
Unearned finance income	(443 568)	(412 629)
Impairment of finance lease receivables	(84 140)	(76 416)
Present value of minimum lease payments, net	6 764 820	6 022 083

Lease agreements where the Group acts as a lessee

The BZ WBK Group companies also avail of lease arrangements as lessees, however as the leases are between related entities they were eliminated from the consolidated statement of financial position and profit and loss account.

Operating leases

Lease agreements where the Group acts as a lessee

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 Group. In 2017 and 2016 rentals totalled PLN 234,684 k and PLN 236,412 k, respectively. These payments are presented in the profit and loss account under "operating expenses".

The majority of lease agreements signed by SCB were concluded for a definite period of time ranging from three to five years. As regards the premises for mobile units, the lease agreements were entered for an indefinite period subject to one up to three months' notice.

PSA Finance Polska Sp. z o.o., acting together with its subsidiary PSA Consumer Finance Polska Sp. z o.o., leases mainly office space under the agreement renegotiated in 2016 and valid until 2021. The PSA Finance Polska sp. z o.o. and PSA Consumer Finance Polska sp. z o.o. Companies lease from Banque PSA Finance SA printers/scanners for a standard period of 4 years, laptops for 3 years and dekstop workstations for 4 years.

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

Payments - maturity	31.12.2017	31.12.2016
less than 1 year	208 032	235 737
between 1 and 5 years	474 185	494 489
over 5 years	384 471	467 632
Total	1 066 688	1 197 858

Lease agreements where the Group acts as a lessor

The table below shows future minimum lease fees due to irrecoverable operating lease.

Future minimum lease fees due to irrecoverable operating lease	31.12.2017	31.12.2016
less than 1 year	9 301	8 534
between 1 and 5 years	9 160	6 802
over 5 years	-	-
Total	18 461	15 336

In thousands of PLN

47. Consolidated statement of cash flows- additional information

The table below specifies components of cash balances of BZ WBK Group.

Cash and cash equivalents	31.12.2017	31.12.2016
Cash and balances with central banks	4 146 222	4 775 660
Receivables from interbank deposits*	2 136 307	3 513 206
Debt securities held for trading*	-	699 883
Debt securities available for sale*	1 379 839	2 849 694
Cash acquired	-	356
Total	7 662 368	11 838 799
The impact of changes in currency exchange rates during the financial year on cash and cash equivalents	(89 445)	84 951

* financial assets with initial maturity below three months.

Bank Zachodni WBK and Santander Consumer Bank have restricted cash in the form of a mandatory reserve held on account with the Central Bank.

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

Interests received and interests paid	01.01.2017- 31.12.2017	01.01.2016- 31.12.2016
Interests received, including:	6 542 339	6 214 338
- operating activities	5 875 868	5 595 969
- investing activities	666 471	618 369
Interests paid, including:	(1 231 416)	(1 267 431)
- operating activities	(993 307)	(1 087 084)
- financing activities	(238 109)	(180 347)

48. Related parties

The tables below present intercompany transactions. They are effected between associates and parent entity. Most of the transactions are banking transactions made as part of ordinary business activities and mainly include loans, deposits, guarantees and leases. Intercompany transactions effected by the bank and its subsidiaries have been eliminated during the consolidation process. In the case of internal Group transactions, a documentation is prepared in accordance with requirements of tax regulations for transfer pricing.

Transactions with associates	31.12.2017	31.12.2016
Assets	93	70
Other assets	93	70
Liabilities	120 382	78 706
Deposits from customers	90 102	78 414
Sell-buy-back transactions	30 044	-
Other liabilities	236	292
INCOME	14 223	18 393
Fee and commission income	14 223	18 393
Expenses	6 654	10 924
Interest expenses	1 806	1 313
Fee and commission expenses	3 020	3 230
Operating expenses incl.:	1 828	6 381
<i>General and administrative expenses</i>	<i>1 828</i>	<i>6 381</i>

In thousands of PLN

Transactions with Santander Group	with the parent company		with other entities	
	31.12.2017	31.12.2016	31.12.2017	31.12.2016
Assets	598 411	981 961	9 854	3 674
Loans and advances to banks, incl:	308 691	594 042	9 831	274
<i>loans and advances</i>	95 993	353 911	-	-
<i>current accounts</i>	212 698	240 131	9 831	274
Financial assets held for trading	282 036	387 727	-	3 371
Hedging derivatives	7 469	-	-	-
Other assets	215	192	23	29
LIABILITIES	403 807	633 941	86 720	262 160
Deposits from banks incl.:	62 996	271 312	23 539	174 617
<i>current accounts</i>	62 996	271 312	23 539	3 683
<i>Loans from other banks</i>	-	-	-	170 934
Hedging derivatives	-	54 503	-	-
Financial liabilities held for trading	322 933	308 126	-	7 365
Deposits from customers	-	-	52 577	71 079
Other liabilities	17 878	-	10 604	9 099
Income	14 914	16 747	411	294
Interest income	11 321	14 268	95	28
Fee and commission income	3 593	2 096	299	239
Other operating income	-	-	17	27
Net trading income and revaluation	-	383	-	-
Expenses	84 818	1 721	76 712	28 899
Interest expenses	1 050	446	2 298	2 211
Fee and commission expenses	1 171	1 106	205	281
Net trading income and revaluation	64 720	-	57 672	2 420
Operating expenses incl.:	17 877	169	16 537	23 987
<i>Bank's staff, operating expenses and management costs</i>	17 877	-	16 529	23 987
<i>Other operating expenses</i>	-	169	8	-
Contingent liabilities	-	10 706	-	-
Sanctioned:	-	10 706	-	-
<i>financial</i>	-	10 706	-	-
Derivatives' nominal values	51 859 866	57 761 351	-	634 312
Cross-currency interest rate swap – purchased amounts	3 478 300	5 645 125	-	-
Cross-currency interest rate swap – sold amounts	3 414 864	5 424 101	-	-
Single-currency interest rate swap	18 298 033	16 517 900	-	633 412
Options	8 001 216	7 285 846	-	-
FX swap – purchased amounts	4 719 697	5 363 317	-	-
FX swap – sold amounts	4 762 299	5 344 715	-	-
FX options -purchased CALL	2 010 291	2 643 269	-	-
FX options -purchased PUT	1 950 686	2 798 804	-	-
FX options -sold CALL	2 026 149	2 755 705	-	-
FX options -sold PUT	2 211 749	2 824 233	-	-
Spot-purchased	162 894	162 456	-	-
Spot-sold	163 182	162 876	-	-
Forward- purchased amounts	138 027	101 365	-	-
Forward- sold amounts	135 771	74 665	-	900
Capital derivatives contract - purchased	386 708	656 974	-	-

Transactions with Members of Management and Supervisory Boards

Remuneration of Bank Zachodni WBK Management Board Members, Supervisory Board Members and key management BZ WBK Group's.

Loans and advances made by the Banks to the key management personnel

As at 31.12.2017 and 31.12.2016 members of the Management Board were bound by the non-compete agreements which remain in force after they step down from their function. If a Member of the Management Board is removed from their function or not appointed for another term, he/she is entitled to a once-off severance pay. The severance pay does not apply if the person accepts another function in the Bank.

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

In thousands of PLN

Remuneration of Management Board Members and Key Management	Management Board Members		Key Management	
	2017	2016	2017	2016
Remuneration	12 774	10 162	40 903	40 600
Additional benefits (e.g among others, life insurance cover without pension option, medical cover, accommodation, travel expenses and school fees)	1 136	894	1 062	1 061
The awards paid in 2017 and 2016 *	8 186	6 910	16 587	12 669
Equivalent paid for unused annual leave	125	199	130	155
Additional compensation for termination of the contract and the non-competition clause	-	1 092	-	-
Loans and advances made by the Bank to the Members of the Management Board/Key Management	11 054	7 158	22 693	25 697
Deposits from The Management Board and their relatives/Key management	17 328	13 312	13 106	14 199
Provisions for unused holidays	797	567	2 651	2 902
The number of conditional rights to shares	34 670	17 671	41 194	31 415

* included part of the award for 2016, 2015, 2014, 2013 and 2012 which was conditional and deferred in time

The category of key management personnel includes the persons covered by the principles laid down in the "Policy on variable components of remuneration paid to the individuals holding managerial positions at Bank Zachodni WBK", and in the case of subsidiaries – by the principles laid down in their respective internal regulations.

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

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

In 2017, the total remuneration paid to the Supervisory Board Members of Bank Zachodni WBK totalled PLN 1,556 k (PLN 1,712 k in 2016). Mr John Power received remuneration for the supervision over acquisition of a carve-out business of Deutsche Bank Poland by BZ WBK in the amount of PLN 84.0 k. Mr John Power received remuneration of PLN 28.7 k from subsidiaries for his membership in their Supervisory Boards (PLN 35 k in 2016).

49. Acquisitions and disposals of investments in subsidiaries and associates

Agreement on the acquisition of a carve-out of Deutsche Bank Polska by Bank Zachodni WBK

On 14 December 2017, Bank Zachodni WBK and Banco Santander signed a transaction agreement with Deutsche Bank AG (DB AG) to purchase a part of Deutsche Bank Polska (DBPL) business, consisting of retail banking, private banking, SME banking and DB Securities. DBPL's corporate and investment banking business and foreign-currency mortgage portfolio are excluded from the transaction and will remain in DBPL (retained business).

On the same day, the bank signed a pre-demerger agreement with DBPL and DB AG setting out the terms of cooperation between the bank and DBPL to finalise the transaction.

Pursuant to the transaction agreement, DBPL's branch network and external sales channels (agents and intermediaries) are to be integrated with the bank's structures. Asset management contracts will also be transferred along with the carve-out, which will enable the transfer of open-ended investment funds.

Before the demerger, Bank Zachodni WBK will buy DBPL's shares from DB AG, representing 10% of votes at the DBPL's General Meeting of Shareholders. Next, the bank and DBPL will file requests for the registration of the demerger with relevant registry courts.

The demerger will be effected on the following terms:

- DBPL will be a demerged company and BZ WBK will be an acquiring company;
- The share capital of DBPL will be decreased by at least an equivalent of the total nominal value of the shares purchased by Bank Zachodni WBK. On the date of the registration of such capital decrease, all the shares purchased by the bank will cease to exist and DB AG will become the sole shareholder of DBPL;

In thousands of PLN

- In exchange for the transfer of the carved-out business to Bank Zachodni WBK, DB AG will receive a stated number of BZ WBK shares (demerger shares) on the demerger date, calculated based on the agreed formula which will be used to determine a share exchange ratio in the demerger plan. The demerger will be effective as of the date of registration of the bank's capital increase by way of the issuance of demerger shares;
- On the demerger date, the carved-out business will be transferred to the bank and the business which is not subject to the transaction will remain in DBPL. DBPL's assets and liabilities will be allocated between the carved-out business and the retained business based on the terms specified in the transaction agreement and the demerger plan;

The preliminary purchase price is PLN 1,289,799,000 and has been calculated on the basis of a capital requirement for carved-out risk weighted assets (excluding DB Securities' shares), determined using financial projections as at the date close to the execution of the transaction agreement. The portion of the preliminary purchase price related to the value of DB Securities' shares has been calculated on the basis of the company's net asset value.

The consideration for the transaction will be paid in:

- cash, through the payment of a price for the purchased shares (20% of the preliminary purchase price);
- newly issued shares of the bank representing approx. 2.7% of the bank's share capital (80% of the preliminary purchase price).

Once the transaction agreement is executed, the preliminary purchase price will be adjusted to reflect changes in relevant assets and liabilities that have taken place between the transaction agreement date and the demerger date.

The transaction is subject to regulatory approvals, including consents from the Polish Financial Supervision Authority (KNF) and the President of the Office of Competition and Consumer Protection (UOKiK), as well as resolutions of the General Meetings of Shareholders of BZ WBK and DBPL, signing of the demerger plan and fulfilment of certain operational conditions. The transaction is expected to close in Q4 2018. The migration of IT systems is planned to be completed immediately after closing.

Conclusion of the agreement will not lead to a take-over of control or significant influence over Deutsche Bank Polska S.A., nor will it give rise to any obligations that would need to be disclosed.

Contribution in kind of BZWBK F24 S.A. (formerly BZ WBK Nieruchomości S.A.) shares to BZWBK Finanse sp. z o.o

On 24.11.2017, BZ WBK S.A. made contribution in kind of BZWBK F24 S.A. (formerly BZ WBK Nieruchomości S.A.) shares to BZWBK Finanse sp. z o.o. to cover the acquisition of BZWBK Finanse sp. z o.o. shares by BZWBK S.A. In the second half of 2017, BZ WBK F24 S.A. changed its business model. The main profile of the business activity focused around financing of consumer car purchase – the company was registered by the Polish Financial Supervision Authority (KNF) as a lending institution.

The changed ownership structure will allow to limit the cost of business management and it is consistent with the strategy of extending the business activity of BZ WBK Group whereby BZ WBK F24 S.A. will offer financial products addressed to personal customers (consumers) on the market of so-called "light vehicles".

On 12.01.2018, in the Nation Court Register was registered increase of share capital BZWBK Finanse sp. z o.o to PLN 1,630 k. Share capital was fully paid.

Liquidation of AKB Marketing Services sp. z o.o.

On 28.03.2017, AKB Marketing Services sp. z o.o. , a subsidiary of Santander Consumer Bank S.A., was liquidated.

The subsidiary's assets and liabilities were finally accounted for. Profit on liquidation of PLN 3,757 k was presented in the consolidated income statement under 'Net gains/(losses) on subordinated entities'.

AKB Marketing Services sp. z o.o. in liquidation carried out ancillary business operations in respect of banking services. On 20.11.2017, the company AKB Marketing Services sp. z o.o. was deleted from the National Court Register.

Merger of BZWBK Leasing S.A. and BZWBK Lease S.A.

On 28.02.2017, BZ WBK Leasing S.A. and BZ WBK Lease S.A. merged.

The companies merged by way of absorption of BZ WBK Lease S.A. (the absorbed entity) by BZ WBK Leasing S.A. (the absorbing entity). All the assets of BZ WBK Lease S.A. were transferred to BZ WBK Leasing S.A. In connection with the merger, BZ WBK Lease S.A. ceased to exist legally, while BZ WBK Leasing S.A., being the absorbing entity, assumed, under the law, all the rights and obligations of the absorbed entity. As a result, BZ WBK Leasing S.A. continues business operations which previously were carried out by BZ WBK Lease S.A. and assumed, under the law, all the rights and obligations of absorbed BZ WBK Lease S.A.

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

In thousands of PLN

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.

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

Description the transaction

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 October 2016, Santander Consumer Bank took over control over PSA Finance Polska sp. z o.o. (PSA Finance Polska) and indirectly over PSA Consumer Finance Polska sp. z o.o. (PSA Consumer Finance Polska).

The change of control took place as a result of purchase (for a final price of PLN 58,849,775 paid in cash) of 50% shares in PSA Finance Polska and indirectly in PSA Consumer Finance Polska, representing 50% of total votes at the companies' General Meeting. The fair value of the price paid is 50% of the companies' fair value determined on the basis of the reference carrying amount.

Difference in the amount of PLN 2 503 k the amount presented above between the initial purchase price in the amount PLN 61 353 k and the price paid for the shares results from the final settlement of the transaction.

Santander Consumer Bank recognises PSA Finance Polska and PSA Consumer Finance Polska as subsidiaries due to the fact that it has control over their key areas which influence the companies' financial results (notably the risk and funding areas). As a result, Santander Consumer Bank is a shareholder which is exposed to a higher risk and can derive greater benefits due to the consequences of the decisions relating to the financial activities of the two companies.

Due to the fact that Bank Zachodni WBK has a 60% stake in Santander Consumer Bank, which in turn has a 50% stake in PSA Finance Polska, the bank has disclosed non-controlling interests of 70% in the share capital and the number of votes at the General Meeting of PSA Finance Polska and, indirectly, PSA Consumer Finance Polska.

Cancellation of shares in PSA Finance Polska

On 5 April 2017, an agreement was signed whereby Santander Consumer Bank sold 10% of its shares in PSA Finance Polska to the latter company for the purpose of their cancellation, which took place on the basis of a resolution of the General Meeting of Shareholders of PSA Finance Polska. The resolution provided for reduction of the company's share capital by PLN 30,000 k and a voluntary cancellation of the company's shares PLN 12,266 k. The initial purchase price and the price paid for the shares were adjusted by the value of the above cancellation.

The Management Board of PSA Finance Polska acquired own shares, with the intention of their cancellation, from both shareholders in equal proportions, as a result of which the company's ownership structure remained the same.

In thousands of PLN

Assets and liabilities recognised at the merger date

In the financial year ended 31 December 2017 a final settlement was made of the acquisition of control over PSA Finance Polska and PSA Consumer Finance Polska.

The table below presents the fair value of assets and liabilities acquired by Santander Consumer Bank.

	as at 31.12.2017	PSA Finance sp. z o.o.	PSA Consumer Finance sp. z o.o.
ASSETS			
Cash and balances with central bank		1	5
Loans and advances to banks		317	33
Loans and advances to customers		735 482	141
Intangible assets		66	3
Property, plant and equipment		2 027	-
Net deferred tax assets		35 386	1
Other assets		11 828	13
Total assets		785 107	196
LIABILITIES			
Deposits from banks		(476 864)	-
Deposits from customers		(96 731)	-
Current income tax liabilities		(6 060)	-
Other liabilities		(87 948)	-
Total liabilities		(667 603)	-
Fair value of identifiable net assets		117 504	196

No intangible fixed assets or contingent liabilities that would meet the criteria of being recognised as balance sheet assets were identified in the assets and liabilities acquired.

Non-controlling interests

As a result of the take-over of control by Bank Zachodni WBK, non-controlling interests were recognised, representing indirect 70% of the share capital and the number of votes at the General Meeting of PSA Finance Polska and indirectly PSA Consumer Finance Polska. They result from the recognition of non-controlling shares both at the level of the acquired companies, and at the level of the shareholders of Santander Consumer Bank. The carrying amount of the shares was PLN 82,390 k using the proportional share in the identified net assets method.

The goodwill arising on acquisition represents the excess of the value of non-controlling shares (70%) and the payment made over the book value of the identified net assets, determined as at the date of final settlement of the purchase price.

Goodwill calculation

Data presented in the consolidated financial statements for 2017 are different than in the financial statements for 2016 due to the final settlement of the transaction.

	as at	31.12.2017
Goodwill		
Total consideration		58 850
Non-controlling interests		82 390
Less: fair value of identifiable net assets		(117 700)
Total		23 540

The goodwill arising as at the merger date results from the possibility of achieving additional benefits from the expected synergies and an increase in revenues and market share. These benefits were not recognised separately from the goodwill as they did not meet the criteria for recognition as intangible assets.

The goodwill arising on acquisition was not treated as tax deductible.

In thousands of PLN

51. 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 companies of the BZ WBK Group create 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 are stated in the amount of the probable payment without discounting.

Provisions for retirement allowances

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

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

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

The amount of the retirement benefits and death-in-service benefits is dependent on length of service and amount of remuneration. The expected present value of the benefits is calculated, taking into account the financial discount rate and the probability of an individual 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 Group 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 December 2017 are as follows:

- the discount rate at the level of 3.3% (3.6% as at 31 December 2016),
- the future salary growth rate at the level of 2.0% (2,0% as at 31 December 2016),
- the probable number of leaving employees calculated on the basis of historical data concerning personnel rotation in the Group,
- 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.

In thousands of PLN

	31.12.2017	31.12.2016
As at the beginning of the period	60 397	63 209
Provision acquired in a business combination	-	747
Current service cost	308	1 073
Interest expense	2 611	2 228
Actuarial (gains) and losses	9 410	(6 860)
Balance at the end of the period	72 726	60 397

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 December 2017.

Defined benefit plan obligations	1 percent increase	1 percent decrease
Discount rate	9,00%	-9,78%
Future salary growth rate	-9,91%	7,04%

The following table presents how the impact on the defined benefits obligations would have increased (decreased) as a result of a change in the respective actuarial assumptions by one percent as at 31 December 2016.

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

Other staff-related provisions

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

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

Provisions	31.12.2017	31.12.2016
Provisions for unused holidays	58 392	63 948
Provisions for employee bonuses	257 986	237 745
Provisions for retirement allowances	72 726	60 397
Other staff-related provisions	18 618	13 869
Total	407 722	375 959

Detailed information about movements on staff-related provisions is available in additional Note 36.

52. Share based incentive scheme

The fifth edition of the BZWBK incentive scheme vested as at 30.06.2017. The vesting level is 63% for participants having significant impact on the Group's risk profile and at the level of 67% for participants not having significant impact on the Group's risk profile. Its realization through issuance of new shares and their allocation to individual accounts of entitled individuals was processed in Q3 2017.

On 17.05.2017, Annual General Meeting of the Shareholders of Bank Zachodni WBK S.A. approved three-year Incentive Scheme no. VI which participants are employees of the Bank Zachodni WBK Group (including Members of the Management Board), however not more than 250 individuals. On 26.06.2017 the Supervisory Board approved the list of entitled individuals ("grant date").

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

In thousands of PLN

In every single year annual award not exceeding one third on total award will be considered. Shares will vest on a linear pattern between 25% and 100% contingent on profit after tax (PAT) growth and on RORWA ratio growth. The range of the scale requires PAT growth between "lower level" set to 80% of assumed level of realization in 2017 and "upper level" of nominal growth at 17,8% in first year and between "lower level" set to 80% of assumed level of realization in 2018 and 2019 and "upper level" of nominal growth at 13,4% in second and third year of duration of scheme. The range of the scale requires RORWA ratio growth between "lower level" set to 80% of assumed level of realization in 2017 and "upper level" of nominal growth at 2,24% in first year, between "lower level" set to 80% of assumed level of realization in 2018 and "upper level" of nominal growth at 2,37% in second year and between "lower level" set to 80% of assumed level of realization in 2019 and "upper level" of nominal growth at 2,5% in third year of duration of scheme.

Additionally the qualitative factors will be taken into account – participants are entitled to annual award depending on the level of an external customer satisfaction and engagement survey results (an internal customer). The level of customer satisfaction will be met when in the peer group Bank will be on second place in first and second year and on the first place in third year of duration of the scheme. The engagement survey results will not be lower than 50% in first year, 60% in second year and 70% in third year of duration of scheme.

Additionally, after 3 years cumulative award will be considered. Shares will vest on a linear pattern between 25% and 100% contingent on PAT compound annual growth rate in 3 years' time between 11,7% and 15% and on average value of RORWA ratio in 3 years' time between 1,9% and 2,38%. If number of shares resulting from cumulative assessment will be higher than sum of annual awards vested to date, additional shares will be allocated to individuals up to the amount resulting from cumulative assessment.

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

Share based payments granted in 2017:

	2017
Number of share based payments	131 262
Share price (PLN)	350,00
Exercise price	10
Vesting period	3 years
Expected volatility of share prices	30,07%
Award life	3 years
Discounted risk free rate	2,12%
Fair value per award	323,36 zł
Dividend yield	1,71%

The following table summarizes the share based payments activity:

	12 months of 2017 based payments	12 months of 2016 based payments
Outstanding at 1 January	157 254	168 784
Granted	131 912	-
Exercised	(100 233)	-
Forfeited	(3 958)	(11 530)
Expired	(55 176)	-
Outstanding at 31 December	129 799	157 254
Exercisable at 31 December	-	-

The expired rights presented in the table for 12 months of 2017 represent the lower level of the vested rights for the Incentive Scheme V.

For the share based payments outstanding as at 31.12.2017 and 31.12.2016 the average remaining contractual life is approximately 2,5 years and 0,5 year respectively.

The expenses of sixth edition of equity settled share-based payments scheme recognized in profit and loss account for 12 months of 2017 amounts to PLN 7 173 k.

In thousands of PLN

The table below presents information about the number of conditional rights to shares vested in BZ WBK Management Board members under the 5th Incentive Scheme and the 6th Incentive Scheme launched in 2017.

No. of awards	2017	2016
Outstanding at 1 January	17 671	17 918
Granted	35 687	1 253
Expired	(6 053)	-
Exercised	(10 541)	-
Resignation from the function	(2 094)	(1 500)
As at 31 December	34 670	17 671

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

No. of awards	2017	2016
Outstanding at 1 January	31 415	30 350
Granted	44 134	1 065
Expired	(9 484)	-
Exercised	(19 616)	-
Resignation from the function	(5 255)	-
As at 31 December	41 194	31 415

53. Dividend per share

As of the date of publication of this report, the Management Board of Bank Zachodni WBK SA has not finalised its analysis in respect of recommendation on dividend payout for 2017.

On 17.05.2017 Annual General Meeting of Bank Zachodni WBK S.A. adopted a resolution on dividend payment.

It was decided to allocate PLN 535,866 k from the Bank's undivided net profit for 2014 and 2015 to dividend for shareholders.

Dividend per share was PLN 5.40.

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

Issuance of own bonds by Bank Zachodni WBK

The Management Board of Bank Zachodni WBK S.A. informed that on 7.02.2018, it adopted a resolution approving the issuance by the Bank of subordinated bonds with a total nominal value not higher than PLN 1,000,000 k, to be qualified as Tier II instruments of the Bank subject to the consent from the Polish Financial Supervision Authority.

The Bonds will be offered solely on the territory of Poland. The Bonds may be issued in one or several series. The Bank plans to carry out the issuance by 30.06.2018. Details of the issuance will be communicated at a later date.


Signatures of Members of the Management Board

Date	Name	Function	Signature
12.02.2018	Michał Gajewski	President	
12.02.2018	Andrzej Burliga	Vice-President	
12.02.2018	Michael McCarthy	Vice-President	
12.02.2018	Juan de Porras Aguirre	Vice-President	
12.02.2018	Miroslaw Skiba	Vice-President	
12.02.2018	Feliks Szyszkowiak	Vice-President	
12.02.2018	Artur Chodacki	Member	
12.02.2018	Carlos Polaino Izquierdo	Member	
12.02.2018	Marcin Prell	Member	
12.02.2018	Arkadiusz Przybył	Member	
12.02.2018	Maciej Reluga	Member	
12.02.2018	Dorota Strojowska	Member	

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

Date	Name	Function	Signature
12.02.2018	Wojciech Skalski	Financial Accounting Area Director	