Annual report of Santander Bank Polska for 2018

Dear Sir/Madame,

2018 was a momentous year for Santander Bank Polska S.A. (previously Bank Zachodni WBK S.A.). The implemented strategic projects and the "Bank As You Want It" idea, which we put to work in our daily business reality, have consolidated our position in the Polish market.

We have successfully carried out the rebranding process, which reaffirmed our long-standing membership of Santander Group, one of the biggest financial institutions in the world and the biggest bank in the eurozone in terms of market capitalisation. In this way, we can even better project our image as a secure, responsible and innovative organisation. Drawing on our prior achievements and tradition, and leveraging the potential of Santander Group, we have set new standards for building relationships with customers and creating innovative products and services. Security and innovation are at the heart of our activities – we cannot ignore the fact that the modern world is characterised by many cyber threats, which is becoming a challenge not only for banks and their customers, but also for the entire economic ecosystem. For this reason, investing in cyber security for the protection of our customers is a priority for us.

Last year, we actively participated in shaping the landscape of the Polish financial sector through consolidation processes, notably as Santander Bank Polska S.A. incorporated the demerged part of Deutsche Bank Polska S.A.

The growth of Santander Bank Polska S.A. and the whole sector was also driven by the strong economy in Poland and elsewhere in Europe.

The increasing competition from fintechs compels the sector players to change and quickly adapt their business models to new requirements to ensure the best possible service for customers. This competition has a stimulating effect, although we would wish to see a level playing field for all, with regulatory requirements applying across the board to all financial sector entities.

The positive results and the significant strengthening of the position of Santander Bank Polska S.A. among the top tier of the domestic financial institutions are a testimony to our development strategy.

Sector and Santander Bank Polska S.A.

Last year was good for the Polish banking sector, despite the continued low interest rate environment and the higher tax and regulatory burden. Net profit of commercial banks increased, clearly exceeding the forecasts that had appeared earlier in the year and pointed to a mere several percent growth. The downturn and turmoil in the capital market stifled the net fee and commission income. On the other hand, last year's profit of the banking sector was buoyed by further improvement in net interest income (which resulted from an increase in margins and better-than-expected credit volumes, especially in retail banking), better cost control and only a slight increase in the cost of risk, despite the transition to the new financial reporting standard IFRS 9.

In 2018, the sector consolidation process accelerated – two acquisitions were completed, including one by Santander Bank Polska S.A., with another transaction pending in 2019. Throughout the year, the issue of foreign currency loans, including the risk of statutory regulation in this area, was very much present in discussions within the sector.

Last year, Santander Bank Polska S.A. incorporated the demerged part of Deutsche Bank Polska S.A., including retail banking, private banking and the SME segment. The transaction also included the acquisition of 100% shares of DB Securities S.A. This brokerage house was subsequently renamed as Santander Securities S.A.

We were the first financial institution in the Polish market to successfully carry out a pioneering project – a parallel legal and operational merger, combined with the branch network rebranding. As a result, Santander Bank Polska S.A. acquired almost 400,000 customers, who immediately gained access to the full range of the bank's products and services. The transaction strengthened the bank's growth potential in the private banking segment, increasing the number of customers served. According to internal estimates, Santander Bank Polska S.A. is currently the preferred banker for customers who have liquid assets above PLN 1 million.

As a result of organic growth helped by the acquisition effects, in 2018, Santander Bank Polska S.A. posted attributable profit of PLN 2.2 billion. Gross loans and advances to customers increased by 28,5% YoY, and deposits grew by 36.5% YoY. The bank's assets increased significantly to PLN 183 billion. At present, the bank serves nearly 5 million customers.

Security and innovation

Through the "Bank As You Want It" strategy, Santander Bank Polska S.A. aspires to be not only the best bank for customers, but also an innovator whose primary goal is to increase satisfaction and loyalty of the bank's customers and business partners alike. The business transformation is focused on creating a business model geared towards creating a positive customer experience, simplifying the product offer, streamlining processes and building a flexible distribution strategy.

We invest in new technologies which ensure a convenient and intuitive access to financial services, both through our extensive branch network and remote channels.

Innovation may not exist without security. We use modern technologies in our daily work to protect the most valuable assets – the data and resources of our customers. We are developing cyber security systems, running educational projects and investing in technologies so that our customers know that security is now Santander Bank Polska S.A.

One of the key focus areas for Santander Bank Polska S.A. is the development of payment solutions that create huge potential for increasing customer satisfaction and loyalty. For this reason, the bank was the first in Poland to offer customers all forms of digital payments, including payments by mobiles equipped with the Santander app, BLIK, Apple Pay, Google Pay, Fitbit Pay and Garmin Pay. Our customers, users of the flagship "Account As I Want It", who numbered more than 1 million at the year-end, were offered free instant transfers in the Express ELIXIR and the BlueCash systems.

We also invest in the development of payments for business customers. In 2018, we were the first institution in the domestic market to introduce SWIFT global payments innovation standard (SWIFT gpi), a system which guarantees near-real time processing of international payments.

One of the most spectacular payment features introduced last year was Santander One Pay FX, the first quick payment service based on blockchain technology for retail and business customers. Santander was the first bank in the world to offer such a solution, which was launched in four markets: Spain, the United Kingdom, Brazil and Poland.

In 2018, we also continued efforts on introducing innovations and improvements in other areas of our business. Our key initiatives included digitalisation and robotisation of processes; further growth of CRM; Big Data analysis, and development of Internet and mobile channels, as well as expanding cooperation with the fintech sector. In addition, we were the first to use chatbots for recruitment, a process we started in August 2018.

The digital transformation covered retail, SME and corporate banking. We have launched eKsięgowość, an accounting and financial service for business customers, operated via the online banking system. International companies were offered Santander Cash Nexus, a global platform with a complete set of transactional solutions for different countries available via direct electronic communication.

Last year, we thoroughly reorganised our corporate business. We have implemented a new sales model and a new quality strategy. The purpose of these changes is to accelerate our market expansion in the corporate segment. It will be a continuation of the previous acquisition strategy in strategic sectors, where revenues in 2018 increased by 16%, and in the group of companies operating in foreign markets, where the bank's income from trade finance products and services increased by 15% YoY.

The transformation of Santander Bank Polska S.A. is focused on improving customer service and offering end-to-end solutions available to customers in all channels anytime and anywhere. The growing number of our loyal customers is proof that we are going in the right direction.

Our Responsibility

I trust that 2019 will be the time for discussion about responsible banking and responsible business. Big economic groups and banks, such as our organisation, are required to comply with higher standards, and the onus is on us to start this discussion. As institutions of public trust, we can play a major role here, and our voice should be heard.

Responsibility is one of the principles on which the operations of Santander Bank Polska S.A. are founded. This is why we initiate and actively participate in CSR projects. Last year, Santander Bank Polska S.A. was awarded Ambassador for Ethical Standards (Rzecznik Standardu Etyki) by Global Compact Network Poland.

Our mission is to help people and businesses prosper. But it is not about finances only. We want to be wherever we need to be and where we may truly impact on the lives of our stakeholders. We make sure our services are adapted to the needs of people with various disabilities. For years, we have been doing our Barrier-Free Banking Programme, and last year, the Santander mobile application received recognition from customers with visual disabilities.

We believe that mutual trust and respect are the foundations for effective, innovative and responsible business. The loyalty and satisfaction of our stakeholders ensure a sustainable profit, which strengthens the bank's credibility among shareholders and allows us to continue investing in the development of products, services, new technologies, as well as in local communities and environmental protection.

We care about our employees. We deliver many global and local leadership and talent development programmes and create the best working environment. We increase the engagement of employees by catering to their needs at each stage of their professional life. Santander Bank Polska S.A. received the Top Employer Poland and Top Employer Europe awards, and was honoured as the Employer of Choice in the banking services market.

Santander Bank Polska S.A. publishes regular CSR reports. We show that corporate social responsibility is a permanent fixture of the bank's strategy and an important and integral part of our daily activities.

In 2018, Santander Bank Polska S.A. carried out social projects under the following programmes: How's Your Driving, Santander Orchestra, Santander Universidades and Barrier-Free Banking, as well as through the Foundation of Santander Bank Polska S.A. and corporate volunteering activities, in which 1,300 employees were involved.

Commitment to Stakeholders

Relying on our prior achievements and the experience and best practices of Santander Group, in 2018, we consistently implemented the “Bank As You Want It” strategy, building loyalty and satisfaction of our customers and employees.

The effectiveness of our activities is evidenced by the “Bank of the Year in Poland” award conferred on Santander Bank Polska S.A. by The Banker magazine in one of the most prestigious competitions in the sector. The bank received this award in recognition of its activities, supported by a strong increase in profits and the innovative nature of its products and services. The Awards Judging Panel also underlined the bank’s significant progress in its strategic development and its position as the leader in the private banking segment. The recognition makes us the more proud as we received it in one of the most intensive periods in the history of our organisation. Santander Bank Polska S.A. was also honoured as the Best Bank in the prestigious CIJ Awards Poland competition, which recognises projects, companies and leaders in the real estate financing segment.

We are looking ahead to new challenges and new goals. In 2019, we will increase the use of artificial intelligence, robots and deep machine learning. In addition to the automation of processes, this will allow us to consolidate and analyse big data sets. In this way, we will be able to offer customers solutions tailored to their expectations, increase the speed of service and improve cybersecurity. Day in, day out we will work with energy and passion to realise our vision to be the best retail and commercial bank in Poland, earning the lasting loyalty of people, customers, shareholders and communities. This is a good moment to fulfil our brand promise: to be the Bank As You Want It.

Michał Gajewski

President of the Management Board of Santander Bank Polska S.A.

FINANCIAL HIGHLIGHTS		PLN k		EUR k	
		31.12.2018	31.12.2017	31.12.2018	31.12.2017
	Stand alone financial statement				
I	Net interest income	4 063 056	3 785 549	952 227	891 830
II	Net fee and commission income	1 616 903	1 726 648	378 941	406 777
III	Profit before tax	2 658 064	2 515 330	622 950	592 581
IV	Profit for the period	2 167 161	1 916 156	507 901	451 423
V	Total net cash flows	10 271 700	(4 048 528)	2 407 298	(953 784)
VI	Total assets	183 038 564	132 863 268	42 567 108	31 854 820
VII	Deposits from banks	1 039 979	1 414 448	241 856	339 123
VIII	Deposits from customers	139 469 776	102 155 522	32 434 832	24 492 441
IX	Total liabilities	159 178 207	112 024 431	37 018 188	26 858 575
X	Total equity	23 860 357	20 838 837	5 548 920	4 996 245
XI	Number of shares	102 088 305	99 333 481	-	-
XII	Net book value per share in PLN/EUR	233,72	209,79	54,35	50,30
XIII	Capital ratio	18,04%	18,95%	-	-
XIV	Profit per share in PLN/EUR	21,73	19,30	5,09	4,55
XV	Diluted earnings per share in PLN/EUR	21,69	19,27	5,08	4,54
XVI	Declared or paid dividend per share in PLN/EUR*	3,10	5,40	0,73	1,27

* Detailed information are described in Note 52.

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

- for balance sheet items – average NBP exchange rate as at 31.12.2018: EUR 1 = PLN 4.3000 and as at 29.12.2017: EUR 1 = PLN 4.1709
- for profit and loss items – as at 31.12.2018 - the rate is calculated as the average of NBP exchange rates prevailing as at the last day of each month in 2018: EUR 1 = PLN 4.2669; 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 = PLN 4.2447.

As at 31.12.2018, FX denominated balance sheet positions were converted into PLN in line with the NBP FX table no. 252/A/NBP/2018 dd. 31.12.2018.

Financial Statement of Santander Bank Polska for 2018

In thousands of PLN

I. Income statement of Santander Bank Polska

		01.01.2018-31.12.2018	01.01.2017-31.12.2017
Interest income and similar to interest		**5 174 209**	**4 703 187**
Interest income on financial assets measured at amortised cost		4 401 909	-
Interest income on financial assets measured at fair value through other comprehensive income		683 986	-
Income similar to interest - financial assets measured at fair value through profit or loss		88 314	-
Interest expenses		**(1 111 153)**	**(917 638)**
Net interest income	Note 5	**4 063 056**	**3 785 549**
Fee and commission income		1 900 245	1 997 881
Fee and commission expenses		(283 342)	(271 233)
Net fee and commission income	Note 6	**1 616 903**	**1 726 648**
Dividend income	Note 7	492 607	299 518
Net gains/(losses) on subordinated entities		(65)	(288)
Net trading income and revaluation	Note 8	153 564	183 229
Gains (losses) from other financial securities	Note 9	40 522	44 614
Other operating income	Note 10	154 335	83 763
Gain on acquisition of enterprise	Note 49	364 765	-
Impairment losses on loans and advances	Note 11	(777 511)	(540 375)
Operating expenses incl.:		(3 023 043)	(2 679 341)
-Staff,Operating expenses and management costs	Note 12,13	(2 590 275)	(2 323 197)
-Depreciation/amortisation		(280 350)	(274 954)
-Other operating expenses	Note 14	(152 418)	(81 190)
Tax on financial institutions		(427 069)	(387 987)
Profit before tax		**2 658 064**	**2 515 330**
Corporate income tax	Note 15	(490 903)	(599 174)
Profit for the period		**2 167 161**	**1 916 156**
Net earnings per share (PLN/share)	Note 16		
Basic earnings per share		21,73	19,30
Diluted earnings per share		21,69	19,27

Notes presented on pages 10 – 156 constitute an integral part of this Financial Statement.

In thousands of PLN

II. Statement of comprehensive income of Santander Bank Polska

for reporting period:	01.01.2018-31.12.2018	01.01.2017-31.12.2017
Profit for the period	**2 167 161**	**1 916 156**
Other comprehensive income which can be transferred to the profit and loss account:	**331 641**	**438 053**
Available-for sale financial assets valuation gross	-	515 926
Deferred tax	-	(98 026)
Valuation of cash flow hedging instruments gross	30 274	24 880
Deferred tax	(5 752)	(4 727)
Valuation of debt securities measured at fair value through other comprehensive income gross	379 159	-
Deferred tax	(72 040)	-
Other comprehensive income which can't be transferred to the profit and loss account:	**18 865**	**(7 504)**
Valuation of equity securities measured at fair value through other comprehensive income gross	10 412	-
Deferred tax	(1 978)	-
Profit on sale of equity securities measured at fair value through other comprehensive income gross	(142)	-
Current tax	12	-
Provision for retirement allowances – actuarial gains/losses gross	13 038	(9 264)
Deferred tax	(2 477)	1 760
Other comprehensive income for the period net of income tax	**350 506**	**430 549**
TOTAL COMPREHENSIVE INCOME FOR THE PERIOD	**2 517 667**	**2 346 705**

Notes presented on pages 10 – 156 constitute an integral part of this Financial Statement.

In thousands of PLN

III. Statement of financial position of Santander Bank Polska

	as at:	31.12.2018	31.12.2017
ASSETS			
Cash and balances with central banks	Note 17	8 841 902	4 114 801
Loans and advances to banks	Note 18	2 859 479	2 012 118
Financial assets held for trading	Note 19	9 776 705	3 421 547
Hedging derivatives	Note 20	52 554	146 724
Loans and advances to customers incl.:	Note 21	117 492 490	90 537 003
- measured at amortised cost		116 056 599	-
- measured at fair value through other comprehensive income		366 751	-
- measured at fair value through profit or loss		1 069 140	-
Buy-sell-back transactions	Note 41	177 482	-
Financial assets available for sale		-	25 784 029
Investment securities incl.:	Note 22	36 372 113	-
- debt securities measured at fair value through other comprehensive income		35 439 836	-
- debt securities measured at fair value through profit and loss		131 005	-
- equity securities measured at fair value through other comprehensive income		801 272	-
Investments in subsidiaries and associates	Note 23	2 396 937	2 377 037
Intangible assets	Note 24	775 908	459 976
Goodwill	Note 25	1 688 516	1 688 516
Property, plant and equipment	Note 26	870 686	821 532
Net deferred tax assets	Note 27	950 886	709 867
Assets classified as held for sale	Note 28	11 123	8
Other assets	Note 29	771 783	790 110
Total assets		**183 038 564**	**132 863 268**
LIABILITIES AND EQUITY			
Deposits from banks	Note 30	1 039 979	1 414 448
Hedging derivatives	Note 20	903 170	578 798
Financial liabilities held for trading	Note 19	1 238 002	1 263 859
Deposits from customers	Note 31	139 469 776	102 155 522
Sell-buy-back transactions	Note 41	8 233 994	1 479 667
Subordinated liabilities	Note 32	2 543 940	1 488 602
Debt securities in issue	Note 33	3 311 969	1 240 244
Current income tax liabilities		186 769	61 143
Provisions for off balance sheet credit facilities	Note 34	58 143	25 384
Other provisions	Note 35	83 644	57 216
Other liabilities	Note 36	2 108 821	2 259 548
Total liabilities		159 178 207	112 024 431
Equity			
Share capital	Note 37	1 020 883	993 335
Other reserve capital	Note 38	18 150 998	16 176 183
Revaluation reserve	Note 39	1 030 661	712 303
Retained earnings		1 490 654	1 040 860
Profit for the current period		2 167 161	1 916 156
Total equity		23 860 357	20 838 837
Total liabilities and equity		**183 038 564**	**132 863 268**

Notes presented on pages 10 – 156 constitute an integral part of this Financial Statement.

In thousands of PLN

IV. Statement of changes in equity

Statement of changes in equity	Share capital	Other reserve capital	Revaluation reserve	Retained earnings and profit for the period	Total
Note	37	38	39		
Equity as at 31.12.2017	**993 335**	**16 176 183**	**712 303**	**2 957 016**	**20 838 837**
Impact of the implementation of IFRS 9	-	-	(32 278)	(200 527)	(232 805)
Equity as at 1.01.2018 (restated)	**993 335**	**16 176 183**	**680 025**	**2 756 489**	**20 606 032**
Coverage of negative impact of IFRS 9 implementation*	-	-	-	218 466	218 466
Total comprehensive income	-	-	350 506	2 167 161	2 517 667
Profit for the period	-	-	-	*2 167 161*	*2 167 161*
Other comprehensive income	-	-	*350 506*	-	*350 506*
Issue of shares **	27 548	-	-	-	27 548
Agio	-	1 004 291	-	-	1 004 291
Profit on sale of equity securities measured at fair value through other comprehensive income	-	-	130	(130)	-
Profit allocation to other reserve capital	-	958 078	-	(958 078)	-
Profit allocation to dividends	-	-	-	(307 627)	(307 627)
Profit allocation to cover negative impact of IFRS 9 implementation*	-	-	-	(218 466)	(218 466)
Share scheme charge	-	12 446	-	-	12 446
As at 31.12.2018	**1 020 883**	**18 150 998**	**1 030 661**	**3 657 815**	**23 860 357**

*On 16.05.2018 General Meeting of Santander Bank Polska SA decided to allocate part of the retained earnings to cover the negative impact of the implementation of IFRS 9.

** On 9.11.2018, Santander Bank Polska SA was informed that on 9.11.2018 the amendments to the Statute of Santander Bank Polska SA resulting in Bank's share capital increase related to acquisition of a demerged part of Deutsche Bank Polska SA was registered by the District Court for the Capital City of Warsaw in Warsaw, XII Commercial Division of the National Court Register. The amendments to the Bank's Statute were adopted by the Extraordinary General Meeting on 29.05.2018. The registered amendment to the Statutes includes an increase in the capital of Santander Bank Polska SA. The share capital of Bank was increased from PLN 993,334,810 to PLN 1,020,883,050 i.e. by PLN 27,548,240. Shares in the increased share capital have been allocated to Deutsche Bank AG in connection with the finalised acquisition of a demerged part of Deutsche Bank Polska SA by Santander Bank Polska SA.

As at the end of the period revaluation reserve in the amount of PLN 1,030,661 k comprises of debt securities and equity shares of PLN 544,394 k and PLN 542,290 k respectively and additionally cash flow hedge activities of PLN (66,906) k and accumulated actuarial gains - provision for retirement allowances of PLN 10,883 k.

In thousands of PLN

Statement of changes in equity	Share capital	Other reserve capital	Revaluation reserve	Retained earnings and profit for the period	Total
Note	37	38	39		
Equity as at 1.01.2017	**992 345**	**15 132 993**	**281 754**	**2 622 428**	**19 029 520**
Total comprehensive income	-	-	430 549	1 916 156	2 346 705
Profit for the period	-	-	-	*1 916 156*	*1 916 156*
Other comprehensive income	-	-	*430 549*	-	*430 549*
Issue of shares *	990	-	-	-	990
Profit allocation to other reserve capital	-	1 045 702	-	(1 045 702)	-
Profit allocation to dividends	-	-	-	(535 866)	(535 866)
Share scheme charge	-	(2 512)	-	-	(2 512)
As at 31.12.2017	**993 335**	**16 176 183**	**712 303**	**2 957 016**	**20 838 837**

*On 3.08.2017, Santander Bank Polska SA was informed that on 3.08.2017, the District Court for Wrocław-Fabryczna, VI Commercial Division of the National Court Register, entered into the National Court Register the changes to the Bank's statute adopted by the Annual General Meeting of the shareholders of the Bank held on 17.05.2017. Given the above, the Bank's share capital was increased from PLN 992,345,340 to PLN 993,334,810, i.e. by PLN 989,470. The shares acquired in the increased share capital were paid up in full.
This increase of the share capital took place within the private placement with the exclusion of the pre-emptive rights of the present shareholders in respect of the shares of the M series ordinary bearer shares covered by Incentive Scheme V participants.

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

In thousands of PLN

V. Statement of cash flows of Santander Bank Polska

for reporting period:	01.01.2018-31.12.2018	01.01.2017-31.12.2017
Profit before tax	**2 658 064**	**2 515 330**
Total adjustments:		
Depreciation/amortisation	280 350	274 954
Gain on acquisition of enterprise	(364 765)	-
Profit from investing activities	(78 408)	(58 698)
Impairment losses (reversal)	13 054	8 342
	2 508 295	**2 739 928**
Changes in:		
Provisions	21 523	16 255
Trading portfolio financial instruments	(6 369 088)	(1 469 353)
Hedging derivatives	418 542	(1 462 967)
Loans and advances to banks	(99 654)	(273)
Loans and advances to customers	(8 366 572)	(3 434 613)
Deposits from banks	(4 164 926)	201 824
Deposits from customers	23 435 073	(636 987)
Buy-sell/ Sell-buy-back transactions	6 754 327	1 479 667
Other assets and liabilities	(355 130)	278 379
	11 274 095	**(5 028 068)**
Interest accrued excluded from operating activities	(516 747)	(522 528)
Dividends	(491 480)	(298 972)
Paid income tax	(580 950)	(411 583)
Net cash flows from operating activities	**12 193 213**	**(3 521 223)**
Inflows	**5 638 949**	**3 934 371**
Sale of investments in subsidiaries	35	-
Sale/maturity of financial assets available for sale	-	3 012 773
Sale/maturity of investment securities	4 383 747	-
Sale of intangible assets and property, plant and equipment	73 277	22 226
Dividends received	491 480	298 972
Interest received	690 410	600 400
Outflows	**(10 411 044)**	**(3 818 079)**
Acquisition of demerged part of Deutsche Bank Polska SA net of cash acquired	(186 482)	-
Acquisition of subordinated entities net of cash acquired	(19 990)	-
Purchase of financial assets available for sale	-	(3 491 908)
Purchase of investment securities	(9 728 225)	-
Purchase of intangible assets and property, plant and equipment	(476 347)	(326 171)
Net cash flows from investing activities	**(4 772 095)**	**116 292**
Inflows	**5 659 259**	**2 031 978**
Debt securities in issue	4 290 794	1 988 788
Proceeds from issuing/shares	-	990
Drawing of loans	1 368 465	42 200
Outflows	**(2 808 677)**	**(2 675 575)**
Debt securities buy out	(1 235 000)	(1 430 000)
Repayment of loans	(1 173 101)	(630 728)
Dividends and other payments to shareholders	(307 627)	(535 866)
Interest paid	(92 949)	(78 981)
Net cash flows from financing activities	**2 850 582**	**(643 597)**
Total net cash flows	**10 271 700**	**(4 048 528)**
Cash and cash equivalents at the beginning of the accounting period	**7 506 027**	**11 554 555**
Cash and cash equivalents at the end of the accounting period	**17 777 727**	**7 506 027**

Cash, cash equivalents and other additional information regarding the statement of cash flows are presented in Note 46. Information regarding liabilities arising from financial activities in loans received, subordinated liabilities and the issue of debt securities were presented respectively in notes 30-33.

Notes presented on pages 10 – 156 constitute an integral part of this Financial Statement.

VI. Additional notes to financial statement of Santander Bank Polska

1. General information about issuer

Santander Bank Polska S.A. is a bank seated in Poland, 00-854 Warszawa, al. Jana Pawła II 17, National Court Registry under 0000008723 number, TIN 896-000-56-73, National Official Business Register number (REGON) 930041341.

On 7.09.2018, the District Court for Wrocław-Fabryczna in Wrocław, VI Economic Unit of the National Court Register, entered into the register of entrepreneurs changes in the Bank's statute resulting in, among others, the change of the Bank's name from the Bank Zachodni WBK SA to Santander Bank Polska SA.

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

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

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

2. Basis of preparation of the financial statement

2.1. Statement of compliance

Unconsolidated annual financial statement of Santander Bank Polska S.A. was prepared in accordance with the International Financial Reporting Standards (IFRS) adopted by the European Union, which are applied on a consistent basis, as at 31 December 2018 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 2018, item 395) 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 the Act of 29 July 2005 on Public Offering, on Conditions for the Introduction of Financial Instruments to the Organized Trading System and on Public Companies.

These Unconsolidated financial statements have been approved for publication by Santander Bank Polska Management Board on 21 February 2019.

Unconsolidated financial statement of Santander Bank Polska S.A. is published on the same date as the consolidated report of Santander Bank Polska S.A. Group.

In thousands of PLN

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

IFRS	Nature of changes	Effective from	Influence on Santander Bank Polska S.A.
Conceptual Framework for Financial Reporting	The IASB issued the Conceptual Framework in March 2018. It sets out a comprehensive set of concepts for financial reporting, standard setting, guidance for preparers in developing consistent accounting policies and assistance to others in their efforts to understand and interpret the standards. The Conceptual Framework includes some new concepts, provides updated definitions and recognition criteria for assets and liabilities and clarifies some important concepts. It is arranged in eight chapters, as follows: • Chapter 1 – The objective of financial reporting • Chapter 2 – Qualitative characteristics of useful financial information • Chapter 3 – Financial statements and the reporting entity • Chapter 4 – The elements of financial statements • Chapter 5 – Recognition and derecognition • Chapter 6 – Measurement • Chapter 7 – Presentation and disclosure • Chapter 8 – Concepts of capital and capital maintenance The Conceptual Framework is accompanied by a Basis for Conclusions. The Board has also issued a separate accompanying document, Amendments to References to the Conceptual Framework in IFRS Standards, which sets out the amendments to affected standards in order to update references to the Conceptual Framework. In most cases, the standard references are updated to refer to the Conceptual Framework. There are exemptions in developing accounting policies for regulatory account balances for two standards, namely, IFRS 3 Business Combinations and for those applying IAS 8 Accounting Policies, Changes in Accounting Estimates and Errors.	Effective immediately for the IASB and the IFRS IC. For preparers who develop accounting policies based on the Conceptual Framework, it is effective for annual periods beginning on or after 1 January 2020.	The amendment will not have a significant impact on financial statement.
Amendment to IFRS 9 Financial Instruments Prepayment right with negative compensation	Amendments to IFRS 9 introduce the statements with reference to contractual prepayment feature, when the lender could be forced to accept the prepayment amount that is substantially less than unpaid amounts of principal and interest. Such a prepayment amount would be a payment to the borrower from the lender, instead of compensation from the borrower to the lender. Such a financial asset would be eligible to be measured at amortized cost or fair value through other comprehensive income (subject to an assessment of the business model in which they are held), however, the negative compensation must be reasonable compensation for early termination of the contract.	1 January 2019	The amendment will not have a significant impact on financial statement.
IFRS 16 Leases	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. 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.	1 January 2019	Standard's implementation progress is described below.

In thousands of PLN

Amendments to IAS 28 Long-term Interests in Associates and Joint Ventures *	The amendments clarify that an entity applies IFRS 9 Financial Instruments to long-term interests in an associate or joint venture to which the equity method is not applied but that, in substance, form part of the net investment in the associate or joint venture (long-term interests). This clarification is relevant because it implies that the expected credit loss model in IFRS 9 applies to such long-term interests. The Board also clarified that, in applying IFRS 9, an entity does not take account of any losses of the associate or joint venture, or any impairment losses on the net investment, recognised as adjustments to the net investment in the associate or joint venture that arise from applying IAS 28 Investments in Associates and Joint Ventures. To illustrate how entities apply the requirements in IAS 28 and IFRS 9 with respect to long-term interests, the Board also published an illustrative example when it issued the amendments.	1 January 2019	The amendment will not have a significant impact on financial statement.
Improvements to IFRS 10 and IAS 28 *	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 assests 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.	The International Accounting Standards Board has not establised the validity date of the amended regulations.	The amendment will not have a significant impact on financial statement.
IFRS 17 Insurance Contracts*	IFRS 17 defines a new approach to the recognition, valuation, presentation and disclosure of insurance contracts. The main purpose of IFRS 17 is to guarantee the transparency and comparability of insurers' financial statements. In order to meet this requirement the entity will disclose a lot of quantitative and qualitative information enabling the users of financial statements to assess the effect that insurance contracts within the scope of IFRS 17 have on the financial position, financial performance and cash flows of the entity. IFRS 17 introduces a number of significant changes in relation to the existing requirements of IFRS 4. They concern, among others: aggregation levels at which the calculations are made, methods for the valuation of insurance liabilities, recognition a profit or loss over the period the entity provides insurance coverage, reassurance recognition, separation of the investment component and presentation of particular items of the balance sheet and profit and loss account of reporting units including the separate presentation of insurance revenues, insurance service expenses and insurance finance income or expenses.	1 January 2021	The standard will not have a significant impact on financial statement.
IFRIC 23 Uncertainty over Income Tax Treatments*	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. IFRIC Interpretation 23 addresses, in particular, when there is uncertainty over income tax treatments, whether an entity considers uncertain tax treatments separately, what assumptions an entity makes about the examination of tax treatments by taxation authorities, how an entity determines taxable profit (tax loss), tax bases, unused tax losses, tax rates and how an entity considers changes in facts and circumstances. 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.	1 January 2019	The amendment will not have a significant impact on financial statement.
IAS 19, Plan Amendment, Curtailment or Settlement*	Amendments to IAS 19 specifies how an entity determines pension expenses when changes to a defined benefit pension plan occur. IAS 19 'Employee Benefits' specifies how an entity accounts for a defined benefit plan. When a change to a plan – an amendment, curtailment or settlement- takes place, IAS 19 requires an entity to remeasure its net defined benefit liability or asset. The amendments require an entity to use the updated assumptions from this remeasurement to determine current service cost and net interest for the remainder of the reporting period after the change to the plan. By requiring the use of updated assumptions, the amendments are expected to provide useful information to users of financial statements.	1 January 2019	The amendment will not have a significant impact on financial statement.

In thousands of PLN

2015-2017 Cycle	Following is a summary of the amendments from the 2015-2017 annual improvements cycle: **IFRS 3 Business Combinations** - Previously held Interests in a joint operation • The amendments clarify that, when an entity obtains control of a business that is a joint operation, it applies the requirements for a business combination achieved in stages, including remeasuring previously held interests in the assets and liabilities of the joint operation at fair value. • In doing so, the acquirer remeasures its entire previously held interest in the joint operation. • An entity applies those amendments to business combinations for which the acquisition date is on or after the beginning of the first annual reporting period beginning on or after 1 January 2019. Earlier application is permitted. **IFRS 11 Joint Arrangements** - Previously held Interests in a joint operation • A party that participates in, but does not have joint control of, a joint operation might obtain joint control of the joint operation in which the activity of the joint operation constitutes a business as defined in IFRS 3. The amendments clarify that the previously held interests in that joint operation are not remeasured. • An entity applies those amendments to transactions in which it obtains joint control on or after the beginning of the first annual reporting period beginning on or after 1 January 2019. Earlier application is permitted.	1 January 2019	The amendment will not have a significant impact on financial statement.
2015-2017 Cycle	Following is a summary of the amendments from the 2015-2017 annual improvements cycle: **IAS 12 Income Taxes** - Income tax consequences of payments on financial instruments classified as equity • The amendments clarify that the income tax consequences of dividends are linked more directly to past transactions or events that generated distributable profits than to distributions to owners. Therefore, an entity recognises the income tax consequences of dividends in profit or loss, other comprehensive income or equity according to where the entity originally recognised those past transactions or events. • An entity applies those amendments for annual reporting periods beginning on or after 1 January 2019. Earlier application is permitted. When an entity first applies those amendments, it applies them to the income tax consequences of dividends recognised on or after the beginning of the earliest comparative period. **IAS 23 Borrowing Costs** - Borrowing costs eligible for capitalisation • The amendments clarify that an entity treats as part of general borrowings any borrowing originally made to develop a qualifying asset when substantially all of the activities necessary to prepare that asset for its intended use or sale are complete. • An entity applies those amendments to borrowing costs incurred on or after the beginning of the annual reporting period in which the entity first applies those amendments. • An entity applies those amendments for annual reporting periods beginning on or after 1 January 2019. Earlier application is permitted.	1 January 2019	The amendment will not have a significant impact on financial statement.
Amendments to IFRS 3 Business combinations	As a result of the amendments to IFRS 3, the definition of a "business" has been modified. The definition has been narrowed down and is likely to result in more acquisitions being classified as a purchase of assets.	1 January 2020	The amendment will not have a significant impact on financial statement.
IAS 1 Presentation of financial statements and IAS 8 Accounting principles (policy), changes in estimates and correction of errors	The IASB has published a new definition of 'material'. Amendments to IAS 1 and IAS 8 clarify the definition and increase consistency across standards	1 January 2020	The amendment will not have a significant impact on financial statement.

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

IFRS 16 Leases

Description of changes

IFRS 16 Leases was published by the International Accounting Standards Board on 13 January 2016 and approved by 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 to 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: licenses 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.

IFRS 16 adapts the control model for the identification of leases by differentiating between leases and service agreements depending on the existence of an asset controlled by the lessee.

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

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

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

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

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 lessors the substantive right to substitute the asset do not meet the criteria of IFRS 16 and are 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.

As a general rule, at inception of a lease the lessee recognises 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) in relation to all lease contracts. At the same time, reporting entities have the right to use two simplifications for short-term leases and leases of low-value assets:

- Short-term leases. 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.

- Leases for which the underlying asset is of low value. IFRS 16 does not require lessees to recognise lease assets or liabilities in relation to low-value assets such as tablets, personal computers, telephones or office furniture with a low value when new. As recommended by IASB, an exemption may be applied to any standalone item worth less than USD 5,000 when new. To determine whether the leased asset is of low value, the lessee assesses the value of the asset when it is new, regardless of the actual age or wear and tear of the asset being leased.

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-of-use asset reflects:

- 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. The discount rate used by the lessee to determine the present value of lease payments 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.

Implementation

Pursuant to IFRS 16 Leases, Santander Bank Polska S.A. adopted uniform reporting principles which require lessees to recognise assets and liabilities in relation to all lease contracts, subject to the exceptions specified in the standard.

The IFRS 16 implementation project was launched by Santander Bank Polska S.A. in H2 2017 and was divided into two stages:

- gap analysis; and
- operational implementation of changes in documents, policies, internal procedures, accounting schemes and IT systems identified during the first stage of the project which are necessary to meet all the requirements arising from the new standard.

At the release date of this report, the implementation of the standard was completed.

The project participants included representatives of departments responsible for the accounting policy, property management, administration of contracts with suppliers, operating accounting, reporting, capital adequacy, taxes and cost management. The Management Board member in charge of the Financial Accounting and Control Division supervised the project in terms of timely delivery and quality.

In 2018, Santander Bank Polska S.A.:

- took measures to ensure complete identification of assets used under lease or rental contracts or other innominate contracts under which the lessor grants Santander Bank Polska S.A., the lessee, the right to use an identified asset for a period of time in exchange for a fee or a series of fees;
- analysed the lease term to be adopted for the measurement of the right-of-use asset and its corresponding financial liability, taking into account extension and termination options and the likelihood that the parties to the lease use those options;
- developed an approach to the calculation of the incremental borrowing rate;

- identified the necessary changes in the existing processes, procedures, chart of accounts and contract registers maintained by Santander Bank Polska S.A.;
- developed and implemented an effective internal control environment to ensure appropriate differentiation between service contracts and lease contracts, including contracts that contain a lease component;
- analysed reporting requirements and provisions regulating capital adequacy assessment and implemented solutions in line with new disclosure and reporting requirements.

The adoption of IFRS 16 required Santander Bank Polska S.A. to analyse data and make certain estimates which affect the measurement of lease liabilities and right-of-use assets.

Most importantly, Santander Bank Polska S.A. needed to determine whether a given contract is a lease contract or includes a lease component, or whether it is a service contract. In relation to that assessment, Santander Bank Polska S.A. elected to apply grandfather assessments regarding whether a contract existing at the date of initial application contains a lease.

As a result, the following groups of lease, rental or usufruct contracts or other innominate contracts under which the lessor grants Santander Bank Polska S.A., as the lessee, the right to use an identified asset for a period of time in exchange for a fee or a series of fees were classified as lease contracts subject to IFRS 16:

- lease of branch and regional office premises and buildings used for administrative purposes such as Business Support Centres and Corporate Banking Centres as well as buildings used for other purposes;
- lease and usufruct of land and premises where the following are located: commercial units, parking lots integral to branches, Business Support Centre or banking centres, ATMs and other self-service devices;
- operating lease of cars.

The groups of assets identified by Santander Bank Polska S.A. as assets subject to IFRS 16 did not include any assets which would meet the definition of a lease of an investment property.

For lease contracts and contracts that contain a lease component, Santander Bank Polska S.A. made estimates which affect the value of right-of-use assets and their corresponding lease liabilities. The following items were estimated:

- a lease term; and
- an interest rate used for the purpose of discounting future cash flows.

Lease term

Santander Bank Polska S.A. determined the lease term as the non-cancellable period of a lease, together with:

1. periods covered by an option to extend the lease if Santander Bank Polska S.A., the lessee, is reasonably certain to exercise that option; and
2. periods covered by an option to terminate the lease if Santander Bank Polska S.A., the lessee, is reasonably certain not to exercise that option.

In assessing whether Santander Bank Polska S.A., the lessee, is reasonably certain to exercise an option to extend a lease, or not to exercise an option to terminate a lease, Santander Bank Polska S.A. considered all relevant facts and circumstances that create an economic incentive for Santander Bank Polska S.A. to exercise the option to extend the lease, or not to exercise the option to terminate the lease.

For fixed-term contracts, Santander Bank Polska S.A. assumed the lease term equal to the term of the lease contract, unless Santander Bank Polska S.A. was aware of circumstances indicating that an extension or termination option would be exercised. For contracts made for an indefinite period, the lease term typically equals three years, unless a given property is subject to redevelopment. In such a case, the lease term does not exceed five years. In the case of right-of-use assets which are accessory to the underlying asset, the lease term is determined as the term of lease of the underlying asset, e.g. commercial premises where the branch is located.

Where an underlying asset is subleased by Santander Bank Polska S.A., the head lessee (“intermediate lessor”), to a third party, and the lease (“head lease”) between the head lessor and lessee remains in effect, the term of the sublease contract does not exceed the term of the head lease contract.

Incremental borrowing rate

The discount rate equals Santander Bank Polska S.A. incremental borrowing rate at the time of the initial application of IFRS 16. The rate is the sum of:

1. risk-free rate
2. credit spread.

In thousands of PLN

Average weighted incremental borrowing ra tes applied for lease liabilities as at the first application date for individual currencies are as follows:

- PLN: 3.84%
- USD: 4.14%
- EUR: 1.87%

Impact of IFRS 16 on the assets and financial position of Santander Bank Polska S.A.

IFRS 16 Leases has a significant impact on the financial statements of Santander Bank Polska S.A.

In 2019, the classification of expenses in the income statement will change (lease rents will be replaced by amortisation/depreciation and interest expenses), as will the timing of their recognition (under the new model, lease expenses will be recognised relatively earlier compared to the current model for recognition of operating lease expenses) and the balance sheet total will increase.

The table below presents the value of each class of right-of-use assets:

Class of right-of-use assets	Land	Buildings and structures	Vehicles	Other	TOTAL
TOTAL	**20 412**	**621 143**	**2 267**	**4 128**	**647 950**

As at the initial application of IFRS 16, all assets indicated above, which are the subjects of lease contracts, were recognised separately from other assets under “Right-of-use assets”. Such contracts were classified as operating lease in accordance with IAS 17. Consequently, during the term of the contract, the related fees were recognised in operating expenses under “General and administrative expenses”.

Total liabilities arising from irrevocable operating leases of Santander Bank Polska S.A. is presented in Note 45.

The table below presents the difference between future fees under operating leases payable by Santander Bank Polska S.A. and disclosed at the end of 2018 in accordance with IAS 17 and lease liabilities recognised in the statement of financial position as at initial application of IFRS 16:

Description	Value
Total liabilities arising from irrevocable operating leases of Santander Bank Polska S.A. as at 31 December 2018	772 809
Discount based on the incremental borrowing rate of Santander Bank Polska S.A. as the lessee	(93 016)
Lease liabilities classified as finance lease before initial application of IFRS 16	190 953
Value of contractual liabilities considering extension and termination options	11 963
Exclusion – short-term leases	(17 685)
Exclusion – leases of low-value assets	(3 291)
Lease liabilities as per IFRS 16 as at 1 January 2019 – TOTAL	**861 732**

The value of right-of-use assets does not equal the value of lease liabilities to the fact that Santander Bank Polska S.A.:

- determined the provisions for onerous leases as an alternative to performing an impairment review. The use of this expedient entailed 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 and totalling PLN 8 397k.
- adjusted the carrying amount of the right-of-use asset by assets and liabilities recognized in respect of business combination in line with IFRS 3 “Business combinations” relating to favourable and unfavourable terms of opertating leases acquired as part of a business combination in amount PLN 21 578k,
- decommisioning provision. As regards the lease contracts providing for the obligation of Santander Bank Polska S.A. to reinstate the leased asset to its original condition after termination of the lease, Santander Bank Polska S.A. recognised decommissioning assets and corresponding provisions mainly in connection with the lease of buildings and structures. Decommissioning costs are incurred in relation to the right-of-use asset and amortised over the estimated economic life. The fair value of decommissioning costs is estimated by Santander Bank Polska S.A. on the basis of average historical costs of asset reinstatement for the last 12 months. As at 1 January 2019, the present value of provisions for reinstatement

In thousands of PLN

of assets to their original condition is PLN 7 146 k and will be presented in the statement of financial position under "Other provisions".

The table below presents right-of-use assets reconciliations with lease liabilities:

Description	Value
Right-of-use assets as per IFRS 16 as at 1 January 2019 , including:	647 950
- lease liabilities as per IFRS 16 as at 1 January 2019	670 779
- provisions for onerous contracts	(8 397)
- assets' adjustment related to assets and liabilities recognized in applying IFRS 3	(21 578)
- decommissioning provision	7 146

Lease liabilities were measured at the present value of the lease payments not paid as at 1 January 2019, including net fixed payments.

Lease liabilities do not include:

- variable lease payments that do not depend on an index or a rate;
- amounts expected to be payable by the lessee under residual value guarantees;
- the exercise price of a purchase option.

It is due to the fact that contracts do not provide for such types of payments, and in the case of the purchase option, it is not reasonably certain whether the lessee will exercise that option.

There are no variable payments that depend on external factors such as sales generated on the leased premises.

Santander Bank Polska S.A. applied the two exemptions regarding:

- short-term leases (with a term up to 12 months and no purchase options); and
- low-value assets (assets with the initial value of PLN 20k or less)

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

For the purpose of the initial application of the standard, Santander Bank Polska S.A. used a modified retrospective approach and measured right-of-use assets at the amount of lease liabilities adjusted for any prepayments or accrued lease payments relating to leases only, recognised in the statement of financial position directly before the date of initial application, and avoided the obligation to restate comparative data.

At the date of initial application of the standard, Santander Bank Polska S.A. decided to use additional expedients available for first-time adopters, other than those specified above, specifically:

- 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);
- determine the provisions for onerous leases as an alternative to performing an impairment review.

For contracts that contain a lease component and one or more additional lease or non-lease components and not showing how the remuneration is divided into lease and non-lease elements, Santander Bank Polska S.A. used the expedient provided under IFRS 16 and did not allocate the consideration in the contract to each lease component on the basis of the relative stand-alone price of the lease component and the aggregate stand-alone price of the non-lease components. As a practical expedient, Santander Bank Polska S.A. elected not to separate non-lease components from lease components, and instead accounts for each lease component and any associated non-lease components as a single lease component.

Santander Bank Polska S.A. was not required under IFRS 16 to make any adjustments on transition for leases where it is the lessor. However, as the intermediate lessor, the reassessed subleases that were classified as operating leases applying IAS 17 and are ongoing at the date of initial application. As a result of assessment of subleases, Santander Bank Polska S.A. continued to classify all sublease contracts as operating leases.

In thousands of PLN

2.3. Standards and interpretations or changes to existing standards or interpretations which were applied for the first time in the accounting year 2018

IFRS	Nature of changes	Effective from	Influence on Santander Bank Polska S.A.
IFRIC 22 Foreign Currency Transactions and Advance Consideration *	IFRIC Interpretation 22 clarify the date of the transaction for the purpose of determining the exchange rate to use on initial recognition of the related asset, expense or income when an entity has received or paid advance consideration in a foreign currency. The Interpretation relates to the situation when the transaction is in foreign currency and the entity pays or receives consideration in advance in a foreign currency before the recognition of the related asset, expense or income.	1 January 2018	The amendment does not have a significant impact on financial statements.
IFRS 9 Financial Instruments	The standard introduces one model under which financial assets are classified into two categories: those measured at fair value and those measured at amortised cost. Assets are classified at initial recognition, depending on the financial instrument management model adopted by an entity and the characteristics of contractual cash flows from such instruments. IFRS 9 introduces a new model for determining impairment allowances: the expected credit loss model. The IFRS 9 requirements for the classification and measurement of financial liabilities are substantially unchanged from IAS 39. The key difference is that entities are required to present in other comprehensive income the effects of changes in the credit risk of financial liabilities designated as measured at fair value through profit or loss. Changes to hedge accounting were meant to better align hedge accounting with risk management activities.	1 January 2018	Impact is described below.
IFRS 15 - Revenue from Contracts with Customers	The rules set out in IFRS 15 will apply to all contracts that generate revenue. The core principle is that an entity will recognise revenue as goods or services are transferred to customers, in an amount that reflects the transaction price. Any separately identifiable goods or services sold as a bundle should be recognised on a standalone basis, and any discounts or rebates applicable to the transaction price should be, in principle, allocated to individual elements of the bundle. Where a contract provides for variable consideration, any such amounts will be included in the revenue only if it is highly probable that their inclusion will not result in a revenue reversal in the future following the remeasurement. 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.	1 January 2018	Impact 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	Impact is described below.
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 2018 for improvements to IFRS 1 and IAS 28	The amendment does not have a significant impact on financial statement.

In thousands of PLN

Improvements to IAS 40 'Investment Property' *	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.	1 January 2018	The amendment does not have a significant impact on financial statement.
Amendments to IFRS 2: Classification and measurement share-based payment transactions *	Changes relate to the following areas: • 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 does not have a significant impact on financial statement.
Improvements to IFRS 4: Applying IFRS 9 'Financial Instruments' with IFRS 4 'Insurance Contracts'	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.	1 January 2018	The amendment does not have a significant impact on financial statement.

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

The section below presents the impact of implementation of IFRS 9 Financial Instruments and IFRS 15 Revenue from Contracts with Customers.

IFRS 9 Financial instruments

Santander Bank Polska S.A. applied new accounting principles regarding the classification and measurement of financial instruments as of 1 January 2018.

IFRS 9 Financial Instruments was published by the International Accounting Standards Board on 24.07.2014 and approved by Commission Regulation (EU) 2016/2067/EU 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 1.01.2018, except for insurers which may apply the standard starting from 1.01.2021. 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.

The impact of changes in the classification and measurement of financial assets and impairment for expected credit losses resulting from the implementation of IFRS 9 is described below.

Classification and measurement of financial instruments

Santander Bank Polska S.A. carried out a detailed analysis of its business models in the area of financial asset management as well as an analysis of cash flow characteristics resulting from the agreements in force. As a result of the analysis, changes in the classification and measurement of financial assets were made and the comparison of the category of valuation and balance sheet value of financial assets as at 1 January 2018 in accordance with IAS 39 and IFRS 9 is as follows:

In thousands of PLN

Standalone financial statement's line for 2017	Measurement category - IAS 39	Carrying amount	Measurement category - IFRS 9	Carrying amount
		Financial assets		
Cash and balances with central banks	Amortized cost (loans and advances)	4 114 801	Amortized cost	4 114 801
Loans and advances to banks	Amortized cost (loans and advances)	2 012 118	Amortized cost	2 012 118
Financial assets held for trading	Fair value through profit and loss	3 421 547	Fair value through profit and loss	3 421 547
Hedging derivatives	Hegde accounting	146 724	Hegde accounting	146 724
Loans and advances to customers	Amortized cost (loans and advances)	90 412 680	Amortized cost	89 157 480
Loans and advances to customers	Amortized cost (loans and advances)	1 151 239	Fair value through profit and loss	1 135 519
Financial asstes available for sale - Debt instruments	Fair value through other comprehensive income	24 889 479	Fair value through other comprehensive income	24 889 479
Financial asstes available for sale - Equity instruments	Fair value through other comprehensive income	756 229	Fair value through other comprehensive income - option	756 229
Financial asstes available for sale - investment in VISA Inc.	Fair value through other comprehensive income	90 175	Fair value through profit and loss	90 175
Financial asstes available for sale - Equity instruments	Historical cost	48 146	Fair value through other comprehensive income - option	32 428
Other assets	Amortized cost (loans and advances)	790 110	Amortized cost	790 110
TOTAL		**127 833 248**		**126 546 610**

The table above illustrates changes in the classification and measurement of financial assets as at the effective date of IFRS9, taking into account the reclassification of the credit card portfolio to the portfolio of financial assets measured at fair value through profit or loss applied retrospectively in the second quarter of 2018 and effective as of 1 January 2018. The impact of the reclassification of credit cards totalling PLN3,202 k including reversal of PLN 36,291 k of allowances for expected credit losses and fair value measurement of the portfolio at PLN 33,089 k was taken to the current period profit.

In thousands of PLN

The comparison of the category of valuation and the carrying amount of liabilities as at 1.01.2018 is as follows:

Standalone financial statement's line for 2017	Measurement category	Carrying amount	Measurement category	Carrying amount
		Liabilities		
Deposits from banks	Amortized cost	1 414 448	Amortized cost	1 414 448
Hedging derivatives	Hegde accounting	578 798	Hegde accounting	578 798
Financial liabilities held for trading	Fair value through profit and loss	1 263 859	Fair value through profit and loss	1 263 859
Deposits from customers	Amortized cost	102 155 522	Amortized cost	102 155 522
Sell-buy-back transactions	Amortized cost	1 479 667	Amortized cost	1 479 667
Subordinated liabilities	Amortized cost	1 488 602	Amortized cost	1 488 602
Debt securities in issue	Amortized cost	1 240 244	Amortized cost	1 240 244
Provisions for off-balance sheet credit facilities	IAS 37	25 384	IFRS 9	49 873
Other liabilities	Amortized cost	2 259 548	Amortized cost	2 259 548
TOTAL		**111 906 072**		**111 930 561**

As a result of the reclassification of the credit card portfolio, the carrying amount of liabilities did not change as the off-balance sheet portion of credit cards continues to be measured at amortised cost for the purpose of calculation of provisions for off-balance sheet liabilities subject to credit risk.

The reconciliation of the items of the statement of financial position, whose value has changed due to the change in the valuation category after the transition from IAS 39 to IFRS 9, which took place on 1.01. 2018, is presented below.

In thousands of PLN

The table below presents the impact of IFRS 9 implementation on assets as at 1.01.2018:

No.	Reference to change description	Item	Carrying amount 01.01.2018 before amendments	Change of measurement category	Valuation update: Classification and measurement	Valuation update: Impairment	Carrying amount 01.01.2018 after amendments
		Financial assets measured at amortised cost					
1		**Loans and advances to customers**					
		Closing balance	90 537 003	-	-	-	-
	Adjustment 1a	ECL allowance	-	-	-	(199 978)	-
	Adjustment 2	Change of recognition of interest income	-	-	-	(28 306)	-
	Adjustment 3	Presentation adjustment – adjustment to impairment interest	-	-	26 565	(26 565)	-
	Adjustment 1b and 4	Reclassification to the category of financial assets measured at fair value through profit or loss	-	(1 151 239)	-	-	-
		Closing balance after amendments	-	-	-	-	89 157 480
		Financial assets measured at amortised cost – TOTAL	**90 537 003**	**(1 151 239)**	**26 565**	**(254 849)**	**89 157 480**
		Financial assets measured at fair value through other comprehensive income					
2		**Financial assets available for sale**					
		Closing balance	25 784 029	-	-	-	-
	Adjustment 6	Reclassification to the category of debt investment financial assets measured at fair value through other comprehensive income	-	(24 889 479)	-	-	-
	Adjustment 6	Reclassification to the category of equity investment financial assets measured at fair value through other comprehensive income	-	(804 375)	-	-	-
	Adjustment 7	Reclassification of investment in VISA Inc. to debt investment financial assets measured at fair value through profit or loss	-	(90 175)	-	-	-
		Closing balance after amendments	-	-	-	-	-
3		**Investment securities, including:**					
		Closing balance					
		– debt investment financial assets measured at fair value through other comprehensive income	-	24 889 479	-	-	-
		– equity investment financial assets measured at fair value through other comprehensive income – option	-	756 229	-	-	-
	Adjustment 5	– equity investment financial assets measured at fair value through other comprehensive income – option	-	48 146	(17 702)	1 984	-
	Adjustment 7	Reclassification of investment in VISA Inc. to debt investment financial assets measured at fair value through profit or loss	-	90 175	-	-	-
		Closing balance after amendments	-	-	-	-	25 768 311
		Financial assets measured at fair value through other comprehensive income – TOTAL	**25 784 029**	**-**	**(17 702)**	**1 984**	**25 768 311**
		Financial assets measured at fair value through profit or loss					
4		**Loans and advances to customers**					
		Closing balance	-	-	-	-	-
	Adjustment 1a and 4	Reclassification from the category of financial assets measured at amortised cost	-	124 323	(80 729)	61 807	-
	Adjustment 1b	Change in measurement category of credit cards' portfolio recorded in current year's income	-	1 026 916	(33 089)	36 291	-
		Closing balance after amendments	-	-	-	-	1 135 519
		Financial assets measured at fair value through profit or loss – TOTAL	**-**	**1 151 239**	**(113 818)**	**98 098**	**1 135 519**
		Deferred tax assets, net					
		Deferred tax assets, net					
		Closing balance	709 867	-	-	-	-
		Valuation update - retained earnings	-	-	18 702	35 907	-
		Valuation update - current's year income statement			6 287	(6 895)	
		Closing balance after amendments	-	-	-	-	763 868
		Deferred tax assets, net – TOTAL	**709 867**	**-**	**24 989**	**29 012**	**763 868**
		TOTAL ASSETS	**117 030 899**	**-**	**(79 966)**	**(125 755)**	**116 825 178**

The value of other 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 equity components and liabilities as at 1.01.2018:

No.	Reference to change description	Item	Carrying amount 01.01.2018 before amendments	Change of measurement category	Valuation update: Classification and measurement	Valuation update: Impairment	Carrying amount 01.01.2018 after amendments
		Equity					
1		**Revaluation reserve**					
		Closing balance	712 303	-	-	-	-
	Adjustment 8	Impact of implementing IFRS 9 – gross	-	-	(17 702)	-	-
		Impact of implementing IFRS 9 – deferred tax	-	-	3 363	-	-
	Adjustment 7	Reclassification of investment in VISA Inc.	-	-	(17 939)	-	-
		Closing balance after amendments	-	-	-	-	680 025
		Revaluation reserve - TOTAL	**712 303**	**-**	**(32 278)**	**-**	**680 025**
2		**Retained earnings**					
		Closing balance	1 040 860	-	-	-	-
	Adjustment 8	Impact of implementing IFRS 9 – gross	-	-	(80 729)	(188 982)	-
		Impact of implementing IFRS 9 – deferred tax	-	-	15 339	35 907	-
	Adjustment 7	Reclassification of investment in VISA Inc.	-	-	17 939	-	-
		Closing balance after amendments	-	-	-	-	840 334
		Retained earnings - TOTAL	**1 040 860**	**-**	**(47 451)**	**(153 075)**	**840 334**
		Profit for the period					
		Closing balance	-	-	-	-	-
	Adjustment1b	Impact of implementing IFRS 9 – gross	-	-	(33 089)	36 291	-
		Impact of implementing IFRS 9 – deferred tax	-	-	6 287	(6 895)	-
		Closing balance after adjustments	-	-	-	-	2 594
		Profit for the period - TOTAL	**-**	**-**	**(26 802)**	**29 396**	**2 594**
		Equity – TOTAL	**1 753 163**	**-**	**(106 531)**	**(123 679)**	**1 522 953**
		Provisions					
3		**Provisions**					
		Closing balance	25 384	-	-	-	-
	Adjustment 1a	Reclassification to “Provisions for off-balance sheet liabilities subject to credit risk”	-	(25 384)	-	-	-
		Closing balance after amendments	-	-	-	-	-
		Provisions – TOTAL	**25 384**	**(25 384)**	**-**	**-**	**-**
		Provisions for off-balance sheet liabilities subject to credit risk					
4		**Provisions for off-balance sheet liabilities subject to credit risk**					
		Closing balance	-	-	-	-	-
		Reclassification from “Provisions”	-	25 384	-	-	-
	Adjustment 1a	Valuation update	-	-	-	24 489	49 873
		Closing balance after amendments	-	-	-	-	-
		Provisions for off-balance sheet liabilities subject to credit risk – TOTAL	**-**	**25 384**	**-**	**24 489**	**49 873**
		TOTAL LIABILITIES AND EQUITY	**1 778 547**	**-**	**(106 531)**	**(99 190)**	**1 572 826**

The value of other liabilities and equity components presented in the unconsolidated statement of financial position did not change significantly as a result of implementation of IFRS 9

Compared to the disclosure of the impact of IFRS 9 implementation in the annual consolidated financial statements for 2017, Santander Bank Polska S.A. has made the following changes:

- impact of the change in the method of recognition of interest income for financial assets classified to stage 1 and 2 in the amount of PLN (28,306)k was presented as part of changes resulting from the implementation of impairment instead of classification and valuation;
- changes in the presentation of the impairment interest adjustment for stage 3: Santander Bank Polska S.A. following the guidelines contained in the ITG document of 11.12.2015 (IFRS Transition Resource Group for the Impairment of Financial Instruments: "Measurement of the loss allowance for credit-impaired financial assets") presents the adjustment of interest income, which reduces interest income for exposures classified to stage 3 to the level of recoverable value of PLN 26,565k as part of impairment for expected credit losses,
- change related to the presentation of impairment losses on purchased or originated financial assets that were affected by credit losses (POCI assets) existing at the time of initial application of IFRS 9. For the purposes of preparing the financial statement for 2018 Santander Bank Polska SA made on January 1, 2018 a presentational compensation of the gross carrying amount and loss allowances for purchased or originated credit-impaired financial assets in the amount of PLN 492 417 k.

The adjustments did not affect, in comparison to the 2017 disclosure, the net value of "Loans and advances to customers".

Changes in the classification and measurement of financial assets presented in the tables above result from following reasons.

- Adjustment 1a: Allowances for expected credit losses (ECL). The total value of additional impairment charges recognised in retained earnings for previous years is PLN 162,660 k, without the deferred tax effect, of which PLN 199,978k relates to balance sheet items, PLN 24,489k the increase in provisions for off-balance sheet liabilities presented in “Provisions for off balance sheet liabilities subject to credit risk” and the reclassifications of financial instruments from the category of assets measured at amortised cost to the category of assets measured at fair value through profit or loss, triggered reversal of allowances of PLN 61,807k.
- Adjustment no. 1b: in H2 2018, Santander Bank Polska S.A. completed the analysis of the credit card portfolio, widely discussed in the banking sector, in terms of the portfolio passing the contractual cash flow test. The analysis resulted in the change of the classification and measurement of selected credit card portfolios due to implementation of IFRS 9. The change concerned credit cards sold until 1 August 2016 whose contractual structure of interest rate was based on four times the NBP Lombard rate and the contractual clauses did not include a direct reference to the Polish Civil Code in terms of the maximum statutory interest at which interest income was recognised. The above-mentioned credit card portfolio was measured at fair value and classified in the statement of financial position as “Loans and advances to customers measured at fair value through profit or loss”. The interest income from such instruments was presented in “Interest-like income from assets measured at fair value through profit or loss”. Santander Bank Polska S.A. ceased to recognise impairment allowances on such portfolio and the assessment of credit risk for such products is now an integral part of measurement at fair value.
- Adjustment 2: Change in interest revenue 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 1.01.2018 it is calculated at the gross carrying amount of the exposure. IFRS 9 provides for two exceptions from this rule:
  - 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.
  - 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, Santander Bank Polska S.A. recognised an interest income adjustment of PLN (28,306)k without deferred tax effect.
- Adjustment 3: changes in the presentation of the impairment interest adjustment for stage 3. Until the end of 2017 Santander Bank Polska S.A. treated the impairment interest adjustment as the element of exposure’s gross carrying amount. Santander Bank Polska S.A. following the guidelines contained in the ITG document of 11.12.2015 (IFRS Transition Resource Group for the Impairment of Financial Instruments: "Measurement of the loss allowance for credit-impaired financial assets") presents the correction of interest income, which reduces interest income for exposures classified to stage 3 to the level of recoverable value in the amount of PLN 26,565 k PLN as part of impairment for expected credit losses.

- Adjustment 4: reclassification of financial instruments that do not meet the contractual cash flow test to the category of financial assets at fair value through profit or loss. Santander Bank Polska S.A. identified in assets' portfolio financial instruments:
  - containing profit sharing clauses which are not compliant with contractual cash flow test criteria. The indicated clauses were identified in some tranches of debt financial instruments entitling the Santander Bank Polska S.A. to obtain additional cash flows, other than solely payments of principal and interest, in the form of a contractually agreed share in the client's financial result. The existence of such contractual clauses has resulted in mandatory valuation of tranches at fair value through profit or loss. The adjustment to the fair-value measurement has been set at PLN (64,726)k, without the deferred tax effect.
  - whose contractual cash flows are not payments of principal and interest due to the interest rate construction. This applies to debt instrument 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 Santander Bank Polska S.A. will be calculated on the nominal price so these cash flows do not represent interest payments as defined in IFRS 9. Due to the failure to meet the contractual cash flow test criteria, the instruments described were mandatory measured at fair value. 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.
- Adjustment 5: equity instruments' valuation at fair value. IFRS 9 significantly limited the ability to measure non-listed equity instruments classified as available for sale 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, Santander Bank Polska S.A. took an irrevocable decision to designate strategic equity investments from the portfolio of financial assets other than those held for trading as instruments measured at fair value through other comprehensive income. The equity investments for which Santander Bank Polska S.A. chose the option of fair value measurement through other comprehensive income were acquired to be maintained in the investment portfolio for a long term and strategically, without the intention to make a profit on selling them in the short or medium term. If the equity instrument designated to be measured at fair value through other comprehensive income is sold, the gain (loss) on the transaction is not recycled to profit or loss at the time of the sale.

  The adjustment to the fair-value measurement of equity instruments has been set at PLN (17,702) k and amount of reversed impairment charges at PLN 1,984 k, without the deferred tax effect.
- Adjustment 6: as the category of financial assets available for sale has been removed and replaced with the category of investment financial assets, Santander Bank Polska S.A. reclassified debt instruments and equity instruments available for sale to the category of investment financial assets. This was merely a presentation change with not impact on the balance sheet total.
- Adjustment 7: Reclassification of preference shares of VISA Inc. Santander Bank Polska S.A. has revised the classification of its preference shares of VISA Inc. As a result of the revision, the investment has been reclassified from equity instruments to debt instruments. Due to the failure to meet the contractual cash flow test for the planned settlement (through allocation of own shares of Visa Inc.), the shares were classified as debt instruments measured at fair value through profit or loss. The adjustment has no impact on the value of equity and relates only to the presentation of financial instruments in these financial statements. As a result of the reclassification, the cumulative change in fair value, exchange rate differences from the balance sheet valuation in the total value of PLN 22,147k and corresponding deferred income tax in the amount of PLN 4,208k was transferred from revaluation capital to retained earnings.
- Adjustment 8: impact of IFRS 9 adoption on the equity of Santander Bank Polska S.A. As at 1.01. 2018, the total value of the impact of IFRS 9 implementation PLN (284,211) k, and the deferred tax effect in the form of deferred net tax asset increase PLN 54,001 k decreased the balance of retained earnings and revaluation reserve by the amount of PLN (232,804) k and, due to the credit cards portfolio reclassification made in 2018, profit of the period in amount PLN 2,594 k.

In thousands of PLN

Additionally, the specification of the impact of individual titles on equity items is presented below:

No.	Equity item	Value as at 01/01/2018 before IFRS 9 implementation	Gross impact	Deferred tax impact	Value taking into account the impact of implementing IFRS 9
	Revaluation reserve				
	Revaluation reserve as at 1 January 2018 before IFRS 9	**712 303**			
1	Reclassification of available-for-sale equity instruments measured at fair value through other comprehensive income – the effect of remeasuring to fair value	-	(17 702)	3 363	-
2	Reclassification of the cumulative change in the fair value of the investment in VISA Inc. to retained earnings in connection with the classification of the instrument as a debt instrument not meeting the contractual cash flow test	-	(22 147)	4 208	-
	Revaluation reserve as at 1 January 2018 taking into account the impact of implementing IFRS 9 – TOTAL	**712 303**	**(39 849)**	**7 571**	**680 025**
	Retained earnings				
	Retained earning as at 1 January 2018 before IFRS 9 implementation	**1 040 860**			
1	Recognition of ECL allowances on financial assets and off-balance sheet liabilities subject to credit risk	-	(199 978)	37 996	-
2	Making a fair value adjustment for financial assets reclassified from the category of financial assets measured at amortised cost to the category of assets obligatorily measured at fair value through profit or loss	-	(80 729)	15 339	-
3	Reversal of allowances for financial assets reclassified from the category of financial assets measured at amortised cost to the category of assets obligatorily measured at fair value through profit or loss	-	61 807	(11 743)	-
4	Reclassification of available-for-sale equity instruments measured at fair value through other comprehensive income – reversal of impairment allowances for shares in other entities	-	1 984	(377)	-
5	Change in the presentation of interest income for the stage 1 and stage 2 exposures which had IBNR allowance calculated until the end of 2017	-	(28 306)	5 378	-
6	Recognition of ECL allowances on off-balance sheet liabilities subject to credit risk	-	(24 489)	4 653	-
7	Reclassification of the cumulative change in the fair value of the investment in VISA Inc. to retained earnings in connection with the classification of the instrument as a debt instrument not meeting the contractual cash flow test	-	22 147	(4 208)	-
	Retained earnings taking into account the impact of implementing IFRS 9 – TOTAL	**1 040 860**	**(247 564)**	**47 038**	**840 334**
	Current period profit or loss				
	Current period profit or loss as at 1 January 2018: before implementation of IFRS 9				
	Change in measurement category of credit cards' portfolio recorded in current year's income statement		3 202	(608)	2 594
	Current period profit or loss as at 1 January 2018 including impact of IFRS 9 – TOTAL		**3 202**	**(608)**	**2 594**
	Impact of implementing IFRS 9 on Santander Bank Polska S.A. Group's equity – TOTAL	**1 753 163**	**(284 211)**	**54 001**	**1 522 953**

As at 1.01.2018 Santander Bank Polska S.A. has not identified any financial assets which it would intend to designate 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. Santander Bank Polska S.A. has not chosen the option of measuring financial liabilities at fair value. Should this option be chosen, changes in the fair value arising from changes in Santander Bank Polska S.A. credit risk will be taken to other comprehensive income, and once a financial liability is derecognised, the value previously recognised in other comprehensive income will not be recycled to profit or loss.

In thousands of PLN

Reconciliation of impairment allowance balance from IAS 39 to IFRS 9

The following table reconciles the prior period's closing impairment allowance, both for performing and non-performing exposures, measured in accordance with the IAS 39 incurred loss model to the new impairment allowance measured in accordance with the IFRS 9 expected loss model at 1.01.2018 taking into account the reclassification of the credit card portfolio.

Measurement category	Loss allowance under IAS 39/Provisions IAS 37	Reclassification	Remeasurement	Change in presentation in interest impaired adjustment	ECL impairment charge reversal due to change in measurement category of credit cards' portfolio	Loss allowance under IFRS 9
Loans and receivables (IAS 39)/Financial assets at amortized cost (IFRS 9)						
Loans and advances from customers	3 032 126	(61 807)	199 978	26 565	(36 291)	3 160 571
Loans and receivables (IAS 39)/Financial assets at amortized cost (IFRS 9) - TOTAL	**3 032 126**	**(61 807)**	**199 978**	**26 565**	**(36 291)**	**3 160 571**
Provisions for off-balance sheet credit facilities (IAS 37)/Loss allowance for expected credit losses (IFRS 9)						
Provisions for off-balance sheet credit facilities (IAS 37)/Loss allowance for expected credit losses (IFRS 9)	25 384	-	24 489	-	-	49 873
Provisions for off-balance sheet credit facilities (IAS 37)/Loss allowance for expected credit losses (IFRS 9)	**25 384**	**-**	**24 489**	**-**	**-**	**49 873**
TOTAL	**3 057 510**	**(61 807)**	**224 467**	**26 565**	**(36 291)**	**3 210 444**

The above reconciliation does not take into account introduced in 2018 change related to the presentation of impairment losses on purchased or originated financial assets that were affected by credit losses (POCI assets) existing at the time of initial application of IFRS 9. For the purposes of preparing the financial statement for 2018 Santander Bank Polska SA made on January 1, 2018 a presentational compensation of the gross carrying amount and loss allowances for purchased or originated credit-impaired financial assets in the amount of PLN 492 417 k.

The application of the new guidelines in accordance with IFRS 9 contributed to the increase in impairment losses in the Santander Bank Polska S.A. The total value of additional impairment charges recognised in retained earnings for previous years is PLN 162,660 k, without the deferred tax effect, of which PLN 199,978 k relates to balance sheet items, PLN 24,489k the increase in provisions for off-balance sheet liabilities presented in the line „Provisions for off balance sheet credit facilities" and the reclassifications of financial instruments from the category of assets measured at amortised cost to measure at fair value through profit or loss triggered impairment charge reversal in the amount of PLN 61,807 k.

The balance sheet value of allowances for expected credit losses has changed, in comparison to previous periods, due to the reclassification of credit cards and reversal of allowances for expected credit losses.

Impact of IFRS 9 on capital adequacy

On 12.12.2017, 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 1.01.2018. 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:

1. 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, reporting entity 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

In thousands of PLN

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.

2. The multipliers that can be applied in consecutive years of the transitional period are as follows: 95%, 85%, 70%, 50%, 25%.
3. If reporting entity 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.
4. Reporting entity should decide whether to apply those transitional arrangements and inform the KNF accordingly.
5. During the transitional period, reporting entity 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.
6. Reporting entities that decide to apply transitional arrangements should be required to adjust the calculation of regulatory items which are directly affected by expected credit loss provisions to ensure that they do not receive inappropriate capital relief. For example, the specific credit risk adjustments by which the exposure value is reduced under the standardised approach for credit risk should be reduced by a factor which has the effect of increasing the exposure value. This would ensure that an institution would not benefit from both an increase in its Common Equity Tier 1 capital due to transitional arrangements as well as a reduced exposure value.

Having analysed Regulation No. 2017/2395, Santander Bank Polska 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 Santander Bank Polska.

Below, Santander Bank Polska S.A. has disclosed own funds, capital ratios, as well as the leverage ratio, both including and excluding application of transitional solutions stemming from Article 473a of Regulation (EU) No 575/2013:

	Available capital (amounts)	**31.12.2018**
1	Common Equity Tier 1 (CET1) capital	18 234 902
2	Common Equity Tier 1 (CET1) capital as if IFRS 9 or analogous ECLs transitional arrangements had not been applied	18 059 952
3	Tier 1 capital	18 234 902
4	Tier 1 capital as if IFRS 9 or analogous ECLs transitional arrangements had not been applied	18 059 952
5	Total capital	20 755 203
6	Total capital as if IFRS 9 or analogous ECLs transitional arrangements had not been applied	20 572 495
	Risk-weighted assets (amounts)	
7	Total risk-weighted assets	115 080 775
8	Total risk-weighted assets as if IFRS 9 or analogous ECLs transitional arrangements had not been applied	114 918 604
	Capital ratios	
9	Common Equity Tier 1 (as a percentage of risk exposure amount)	15,85%
10	Common Equity Tier 1 (as a percentage of risk exposure amount) as if IFRS 9 or analogous ECLs transitional arrangements had not been applied	15,72%
11	Tier 1 (as a percentage of risk exposure amount)	15,85%
12	Tier 1 (as a percentage of risk exposure amount) as if IFRS 9 or analogous ECLs transitional arrangements had not been applied	15,72%
13	Total capital (as a percentage of risk exposure amount)	18,04%
14	Total capital (as a percentage of risk exposure amount) as if IFRS 9 or analogous ECLs transitional arrangements had not been applied	17,90%
	Leverage ratio	
15	Leverage ratio total exposure measure	191 431 869
16	Leverage ratio	9,53%
17	Leverage ratio as if IFRS 9 or analogous ECLs transitional arrangements had not been applied	9,44%

IFRS 15 Revenue from Contracts with Customers

IFRS 15 Revenue from Contracts with Customers was published on 28.05.2014 by the International Accounting Standards Board and applies to annual reporting periods beginning on or after 1.01.2018.

IFRS 15 introduces 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 has been introduced to harmonise the rules used by enterprises and to eliminate inconsistencies with previous standards.

As of 1.01.2018, IFRS 15 replaces the following standards and interpretations:

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

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

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

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

IFRS 15 has introduced a single, five-step revenue recognition model, replacing the previous three separate models of revenue recognition. The new model will apply to all transactions, enterprises and industries. This model is 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 Santander Bank Polska S.A. 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.

As part of the analysis of the impact of IFRS 15 on the Santander Bank Polska S.A., the following types of revenues have been identified, which in principle should be recognized in accordance with IFRS 15:

- commission income excluding revenues for issuing guarantees and sureties,
- income due to advisory services,
- income from the sale of fixed operating assets taken over for debts, which are presented together with the cost of fixed assets as a profit on sales in the line "Other operating income",
- loyalty programs,
- so called "success fee" - where success fee agreements are understood by Santander Bank Polska S.A. as agreements where Santander Bank Polska S.A. has no guaranteed remuneration or when it is insignificant during the lifetime of the agreement until a condition is fulfilled (for example in the form of finalization of a contractually agreed transactions), when Santander Bank Polska S.A. receives a remuneration of a significant value covering the effort put into the performance of the agreements in a longer, preceding time,
- income from asset management and

In thousands of PLN

- income from the sale of insurance products showing a connection with financial instruments to an extent not covered by separate standards.

For the purpose of analyzing the impact of the implementation of IFRS 15, Santander Bank Polska S.A. took the advantage of the practical application of the portfolio approach to the analysis of contracts with clients under paragraph 4 of IFRS 15. This was due to the reasonable expectations of Santander Bank Polska S.A. that the impact on the financial statements, in connection with the standard application in the portfolio will not significantly differ from the standard applied in relation to individual contracts (or performance obligations) within this portfolio. Santander Bank Polska S.A. applied the portfolio approach in the majority of the identified revenue categories indicated above.

Santander Bank Polska S.A. applied the modified retrospective method referred to in paragraph C3 point b) of IFRS 15, reflecting the potential effect of the first application of IFRS 15 as an adjustment to retained earnings in the annual reporting period starting from 01.01.2018. As part of this interim method, Santander Bank Polska S.A. applied IFRS 15 retrospectively only to contracts that are not terminated as at the day of first application.

The implementation of IFRS 15 does not have significant impact on the financial standing and equity of Santander Bank Polska S.A. because revenue derived from financial instruments offered by Santander Bank Polska S.A. such as loans or leases is recognised using an effective interest rate and the recognition method for revenue and corresponding cost will not change in the context of contractual provisions.

2.4. Comparability with the results from the previous periods

The changes presented below may have impact on comparability of financial data.

1. The use of IFRS 9 required 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 Santander Bank Polska S.A.

Santander Bank Polska S.A. elected to use the IFRS 9 provisions which provide for exemption of the obligation to restate comparative information for prior periods in relation to the changes arising from classification, measurement and impairment. Differences in the carrying amount of financial assets and liabilities resulting from the application of IFRS 9 are reported in retained earnings in equity and in revaluation reserve as at 1.01.2018.

2. The application of IFRS15 did not require significant changes to the presentation.

3. As a result of the analysis in 2018, on 1 January 2018, the bank changed the method of presentation of discounts or reduction connected with electronic services, in relation to fee and commission income and costs.

These items were previously presented as fee and commission income in “eBusiness and payments” and as fee and commission expenses in “eBusiness and payments”, “Insurance fees” and “Other fees”. These changes were applied by the Bank to the data for 2017 to make them comparable.

Since 1 January 2017, these items have been netted and presented as fee and commission income in “eBusiness and payments”.

The table below shows the impact of the presentation change on comparative data.

	31.12.2017 before conversion	Change of presentation method	31.12.2017 converted
Fee and commission income:	**627 961**	**50 605**	**577 356**
eBusiness & payments	627 961	50 605	577 356
Fee and commission expenses:	**(286 412)**	**50 605**	**(235 807)**
eBusiness & payments	(225 491)	21 404	(204 087)
Insurance commissions	(7 924)	2 752	(5 172)
Other	(52 997)	26 449	(26 548)

The above changes are for presentation purposes only.

In thousands of PLN

2.5. Basis of preparation of financial statement

Unconsolidated financial statement is presented in PLN, rounded to the nearest thousand.

The financial statement of Santander Bank Polska S.A. has been prepared in accordance with the International Financial Reporting Standards (IFRS) adopted in the European Union.Santander Bank Polska S.A. prepared the consolidated financial statement in accordance with the historical cost principle, except for the items specified below:

Item	Balance sheet valuation rules
Held-for-trading financial instruments	Fair value through profit or loss
Loans and advances to customers which do not meet the contractual cash flows test (since 01.01.2018)	Fair value through profit or loss
Financial instruments measured at fair value through other comprehensive income (since 01.01.2018)	Fair value through other comprehensive income
Financial assets available for sale (until 31.12.2017)	Fair value through other comprehensive income
Share-based payment transactions	According to IFRS 2 "Share-based payment" requirements
Equity investment securities (since 01.01.2018)	Fair value through other comprehensive income – an option
Non-current assets held for sale and groups of non-current assets designated as held for sale	Are recognised at the lower of their carrying amount and their fair value less costs of disposal.

Santander Bank Polska S.A. applied the same accounting principles as in the preparation of the consolidated financial statements for the year ended 31.12.2017, excluding the changes resulting from the implementation of IFRS 9 "Financial Instruments" starting from 1.01.2018 and IFRS 15 "Revenue from contracts with customers" described later in the financial statement.

2.6. Use of estimates

Preparation of financial statement in accordance with the IFRS requires the management to make subjective judgements, estimations and assumptions, which affects the applied accounting principles as well as presented assets, liabilities, revenues and expenses.

The estimates and assumptions are based on historical experience and various other factors that are believed to be reasonable under the circumstances, the results of which form the basis of making the judgments about carrying amounts 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.

Main estimates made by Santander Bank Polska S.A.

Impairment allowances for expected credit losses in respect of financial assets applicable since 1 January 2018

Allowances for credit losses under IFRS 9

IFRS 9 introduces a new approach to the estimation of allowances for credit losses. The approach is based on estimation of the expected credit loss (ECL), in contrast to the previous IAS 39 model, which is based on the concept of incurred loss. ECL allowances reflect an unbiased and probability-weighted amount that is determined by evaluating a range of possible outcomes, the time value of money; and reasonable and supportable information that is available without undue cost or effort at the reporting date about past events, current conditions and forecasts of future economic conditions. ECL allowances are measured at an amount equal to a 12-month ECL or the lifetime ECL, when it is deemed there has been a significant increase in credit risk since initial recognition. Accordingly, the ECL model gives rise to measurement uncertainty, especially in relation to:

- measurement of a 12-month ECL or the lifetime ECL;
- determination of when a significant increase in credit risk occurred;
- determination of any forward-looking events reflected in ECL estimation, and their likelihood.

As a result, ECL allowances are estimated using the adopted model developed using many inputs and statistical techniques.

Structure of the models that are used for the sake of ECL estimation consider models for the following parameters:

- PD - Probability of Default, i.e. the estimate of the likelihood of default over a given time horizon (12-month or lifetime);
- LGD - Loss Given Default, i.e. the fraction of the exposure amount that would be lost in the event of default;
- EAD – Exposure at Default, i.e. expectation for the amount of exposure in case of default event in a given horizon 12-month or lifetime.

Changes in these estimates and the structure of the models may have a significant impact on ECL allowances, which might be higher than losses arising from materialisation of credit risk as part of the existing portfolio of financial instruments.

In accordance with IFRS 9, the recognition of expected credit losses will depend on changes in risk after recognition of the exposure. The standard introduces 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 will be 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 will be recognised.
- Stage 3: exposures for which the risk of default has materialised (indications of impairment have been identified). For such exposures, lifetime expected credit losses will be recognised.

ECL is caclucalted using the individual (for individually significant exposures in Stage 3) or collective approach (for remaining exposures in Stage 3 as well as for all exposures in Stage 1 and 2).
For the purpose of the collective evaluation of ECL, financial assets are grouped on the basis of similar credit risk characteristics that were indicative of the debtors' ability to pay all amounts due according to the contractual terms (for example, on the basis of the Santander Bank Polska SA credit risk evaluation or the Santander Bank Polska S.A. grading process that considered asset type, industry, geographical location, collateral type, past-due status and other relevant factors). The characteristics chosen were 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/scoring systems have been internally developed and were continually being enhanced, e.g. externally benchmarked to help underpin the aforementioned factors which determine the estimates of impairment charges.
In the individual approach, the ECL charge was 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 were 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.

Lifetime expected losses are recognised also for the exposures classified as POCI (purchased or originated credit-impaired).

A credit-impaired assets

Credit-impaired assets are classified as stage 3 or POCI. The rules for the determination of impairment under IFRS 9 remained the same as under IAS 39. A financial asset or a group of financial assets are impaired if, and only if, there was objective evidence of impairment as a result of one or more events that occurred after the initial recognition of the asset or asset was recognized as POCI and that impairment event (or events) had an impact on the estimated future cash flows of the financial asset or group of financial assets that could 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. Objective evidence that a financial asset or group of assets was impaired includes observable data:

- significant financial difficulty of the issuer or debtor;
- a breach of contract, such as a default or delinquency in interest or principal payments;
- the Santander Bank Polska S.A. , for economic or legal reasons relating to the debtor's financial difficulty, granting to the debtor a concession that the Santander Bank Polska S.A. would not otherwise consider;
- it becoming probable that the debtor will enter bankruptcy, recovery, arrangement or other financial reorganisation;

- the disappearance of an active market for that financial asset because of financial difficulties; or
- observable data indicating that there was 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 could not yet be identified with the individual financial assets, including:
  - (i) adverse changes in the payment status of debtors in the Santander Bank Polska S.A., or
  - (ii) national or local economic conditions that correlated with defaults on the assets in the Santander Bank Polska S.A..

A significant increases in credit risk

One of the key aspects of implementation of IFRS 9 is to work out a definition of a significant increase in credit risk that determines the classification of an exposure into Stage 2. Santander Bank Polska has developed detailed criteria for identifying a significant increase in risk based on the following main assumptions:

- Qualitative assumptions:
  - Implementing dedicated monitoring strategies for the customer following the identification of early warning signals that indicate a significant increase in credit risk
  - Restructuring actions connected with making concessions to the customers as a result of their difficult financial standing
  - Delay in payment as defined by the applicable standard, i.e. 30 days past due combined with the materiality threshold consistent with classification into stage 3.
- Quantitative assumptions:
  - A risk buffer method based on the comparison of curves illustrating the probability of default over the currently remaining lifetime of the exposure based on the risk level assessment at exposure recognition and at reporting date, Risk buffer is set in relative terms for every single exposure based on its risk assessment resulting from internal models and other parameters of exposure impacting assessment of the Bank whether the increase might have significantly increased since initial recognition of the exposure (such parameters considered types of the products, term structure as well as profitability). Risk buffer methodology was prepared internally and is based on the information gathered in course of the decisioning process as well as in process of transactions structuring.

ECL measurement

Another key feature introduced by IFRS 9 is the approach to the estimation of risk parameters. For the purpose of estimating allowances for expected losses, Santander Bank Polska uses its own estimates of risk parameters that are based on internal models. However, necessary modifications were made in the context of IFRS 9 requirements (such as estimating the parameters over the lifetime of the exposure or taking into account future macroeconomic conditions). The Bank has developed a methodology for models' parameters and built models compliant with IFRS 9. Expected credit losses are equal to the estimated PD parameter multiplied by the estimated LGD and EAD parameters. The final value of expected credit losses is the sum of expected losses from all periods (depending on the stage, either in 12 months or in the entire lifetime) discounted using the effective interest rate. The estimated parameters are adjusted for macroeconomic scenarios in accordance with the assumptions of IFRS 9. To this end, the bank determines the factors which affect individual asset classes to estimate an appropriate evolution of risk parameters. The bank uses internally developed scenarios, which are updated at least every six months. The models and parameters generated for the needs of IFRS 9 are subject to model management process and periodic calibration and validation.

Determination of forward-looking events and their likelihood

Forward-looking events are reflected both in the process of estimating ECL and when determining a significant increase in credit risk, by developing appropriate macroeconomic scenarios and then reflecting them in the estimation of parameters for each scenario. The final parameter value and the ECL is the weighted average of the parameters weighted by the likelihood of each scenario. The bank uses three scenario types: the baseline scenario and two alternative scenarios, which reflect the probable alternative options of the baseline scenario: best case and worst case. The tables below present the key economic indicators arising from the respective scenarios as at 1 January 2018 and 31 December 2018.

In thousands of PLN

Scenario as at 31 December 2018		Baseline		Best case		Worst case	
Likelihood		60%		20%		20%	
		2019	average, next 3 years	2019	average, next 3 years	2019	average, next 3 years
GDP	YoY	3,70%	3,20%	4,60%	4,30%	2,80%	2,00%
3M WIBOR	average	1,80%	2,50%	1,90%	3,20%	1,70%	1,80%
unemployment rate	% active	2,80%	2,30%	2,80%	1,80%	3,20%	5,20%
CPI	YoY	2,10%	2,90%	2,30%	3,50%	1,90%	2,20%
EURPLN	period-end	4,25	4,23	4,18	4,06	4,32	4,37

Scenario as at 1 January 2018		Baseline		Best case		Worst case	
Likelihood		60%		20%		20%	
		2018	average, next 3 years	2018	average, next 3 years	2018	average, next 3 years
GDP	YoY	3,60%	3,00%	4,40%	3,80%	2,20%	2,00%
3M WIBOR	average	1,70%	2,40%	1,80%	3,00%	1,60%	1,60%
unemployment rate	% active	3,80%	3,50%	3,30%	2,50%	4,30%	5,70%
CPI	YoY	2,10%	2,50%	2,50%	2,60%	1,60%	1,90%
EURPLN	period-end	4,22	4,18	4,09	4,01	4,35	4,34

Scenarios are based on the forecasts prepared before reporting date to allow preparation of allowances parameters calibration which is reflected in reporting date book values.

Potential variability – Santander Bank Polska SA

Changes in the estimates referred to above may have significant one-off effects on the value allowances.

The adoption of estimated parameters only at the level of the worst case scenario will cause impairment allowances to increase by PLN 19.3m, while in the best case scenario only, allowances would be lower by PLN 13.2m. The above estimates include the portfolio and scenarios as at 31 December 2018 (excluding SCB) and represent a theoretical estimate of the change in the level of parameters, without considering any potential migrations between stages when scenarios change.

Major variability in the income statement might be caused by transfers from stage 2 to stage 1. Theoretically, if 1% of exposures in each type of assets with the highest 12 months PD are transferred from stage 1 to stage 2, for each type of exposure, this would cause allowances to increase by PLN 47.1m, given the value of the portfolio as at 31 December 2018 (excluding SCB).

The above estimates show that as a result of implementation of IFRS 9, a higher variability may be expected as a result of transfers between stage 1 and stage 2, resulting in material changes in the degree to which exposures are covered with allowances in respect of different ECL horizons. Another essential factor which affects the variability of estimates is the application of macroeconomic forecasts in the ECL calculation.

Santander Bank Polska S.A. regularly reviewed the methodologies and assumptions underpinning estimation of cash flows and periods of time in which they occured; in particular Santander Bank Polska S.A. compares estimated and actual cash flows to arrive at the best estimate of the recoverable amount.

Impairment - guidelines applicable until 31 December 2017

The estimation of potential impairment charges was inherently uncertain and depended upon many factors in respect of credit risk, including impairment charges trends, portfolio grade profiles, economic climates, conditions in various industries to which Santander Bank Polska S.A. was exposed and other external factors such as legal and regulatory requirements. Impairment charges were posted for financial assets with indications of impairment if in the management's opinion the estimated recovery from the debtor, including value of the existing collateral, might be lower than the outstanding exposure. For all the impaired exposures, Santander Bank Polska S.A. calculated 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 required impairment charges to be posted was based on several independent review levels. Quality and impairment charges for financial asstes were independently monitored by head office personnel on a regular basis. A group-wide system for grading financial assets according to agreed credit criteria existed with an important objective being the timely identification of vulnerable financial assets so that remedial action could be taken at the earliest opportunity. The credit grading system played a key role in the calculation of impairment charges in Santander Bank Polska S.A. This was the starting point of a process that ended in an impairment charge being posted against the individual exposures that were at the risk of default.

The analysis of impairment was 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 (currently: Corporate and Investment 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.

Santander Bank Polska S.A. regularly reviewed the methodologies and assumptions underpinning estimation of cash flows and periods of time in which they occured; in particular Santander Bank Polska S.A. compared estimated and actual cash flows to arrive at the best estimate of the recoverable amount.

Santander Bank Polska S.A. does not identify low credit risk exposures under IFRS 9 standard rules, which allows to recognize 12-month expected loss even in cease of siginificant increase of credit risk since initial recognition.

Revenue from Contracts with Customers

IFRS 15 introduces the five-step revenue recognition model and its assumptions as well as the impact on revenue recognition method are described in part 2.8. " Accounting principles ".

The five-step revenue recognition model involves a subjective assessment and identification of:

- the timing of satisfaction of performance obligations
- transaction price, and
- amounts allocated to the performance obligation.

According to Santander Bank Polska S.A., the performance obligation is satisfied at a specific point in time for most of significant categories of revenues as there are indicators of the transfer of control, such as Santander Bank Polska S.A. present right to payment for the asset (if a customer is presently obliged to pay for an asset, it means that he has gained the ability to direct the use of and obtain substantially all of the remaining benefits from that asset). However, the identification of timing of performance obligation (whether satisfied at a point in time or over time) is not a crucial estimate, because contractual provisions provide for monthly settlement periods that ensure a correct recognition of revenues in proper reporting periods.

The transaction price usually refers to the consideration payable to a customer, due to the absence of:

- variable consideration,
- significant financing component in the contract,
- non-cash consideration.

As regards revenue from contracts with customers based on the success fee (i.e. contracts which do not guarantee the remuneration for Santander Bank Polska S.A. or provide for the minimum level of remuneration during the term of the contract until a certain condition is met, thus entitling Santander Bank Polska S.A. to receive significant remuneration to compensate for long-term efforts to perform the contract), then the variable consideration is the prevailing – if not the only one – component of the transaction price. However, variable consideration is usually subject to contractual limits (expressed as a percentage or a value threshold).

Promised assets usually are not distinct, therefore Santander Bank Polska S.A. combines these items with other promised goods or services until it identifies a bundle of goods or services that is distinct. Consequently, Santander Bank Polska S.A. accounts for all the goods or services promised in a contract as a single performance obligation, so that the allocation of transaction price to that performance obligation (which involves assessment of sale prices for promised goods or services and allocation of discounts and variable consideration to individual elements of the contract) is not of key importance.

As regards the different types of revenues governed by IFRS 15, Santander Bank Polska S.A. estimates provisions for refunds only in relation to income from insurance intermediation activities, which is substantiated by the nature of the income, respective contractual and legal clauses, constructive obligations and availability of historical information about refunds.

Refunds from insurance agreements are calculated by means of the vintage method whereby expected refunds are estimated on the basis of average cumulative amount of refunds obtained in the previous period.

The percentage share of refunds vs. the remuneration for Santander Bank Polska S.A. is calculated in monthly periods (determined by the effective date of the insurance agreement), indicating the month when the refund was made. The percentage share of refunds for a given month is the sum of refunds obtained in specific years of the insurance agreement (and considering the expected level of refunds).

Fair value of financial instruments, including instruments which do not meet the contractual cash flows test

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.

Santander Bank Polska S.A. has developed a methodology for measuring the fair value of credit exposures and debt instruments which, as a result of non-fulfilment of the contractual cash flows test, on 1.01.2018 have been reclassified from the group of assets measured at amortised cost to the group of assets measured at fair value through profit or loss.

In the case of the instruments with distinguishable on-balance sheet and off-balance sheet components, the extent of fair value measurement will depend on the nature of the underlying exposure, and:

- the on-balance sheet portion will be measured at fair value;
- the off-balance sheet portion will be measured at fair value only if at least one of the following conditions is met:
  - (a) condition 1: the exposure has been designated as measured at fair value (option) or
  - (b) condition 2: the exposure may be settled net in cash or through another instrument or
  - (c) condition 3: Santander Bank Polska S.A. sells the obligation immediately after its sanction or
  - (d) condition 4: the obligation was sanctioned below the market conditions.

Santander Bank Polska S.A. measures fair value with the use of valuation techniques appropriate in the circumstances and for which sufficient data are available, maximising the use of relevant observable inputs and minimising the use of unobservable inputs. Three widely used valuation techniques are:

- market approach – uses prices and other relevant information generated by market transactions involving identical or comparable (similar) assets, liabilities, or a group of assets and liabilities (e.g. a business unit)
- cost approach – reflects the amount that would be required currently to replace the service capacity of an asset
- income approach – converts future amounts (cash flows or income and expenses) to a single current (discounted) amount. When the income approach is used, the fair value measurement reflects the current market expectations as to the future amounts.

Santander Bank Polska S.A. uses the income approach for fair value measurement relating to financial instruments which do not meet contractual cash flows test.

The following arguments support the use of the income approach:

- no active market;
- the cost approach is not used in the case of financial assets (it usually applies to property, plant and equipment and property investments).

In the case of credit exposures and debt instruments, the present value method within income approach is typically used. In this method, the expected future cash flows are estimated and discounted using a relevant interest rate. In the case of the present value method, Santander Bank Polska S.A. uses the following elements in the valuation:

- expectations as to the future cash flows;
- expectations as to potential changes in cash flow amounts and timing (uncertainties are inherent in cash flow estimates);
- the time value of money, estimated using risk-free market rates;
- the price of uncertainty risk inherent in cash flows (risk premium) and

- other factors that market participants would take into account in the circumstances.

The present value measurement approach used by Santander Bank Polska S.A. is based on the following key assumptions:

- cash flows and discount rates reflect the assumptions that market participants would adopt in the measurement of an asset;
- cash flows and discount rates reflect only the factors allocated to the subject to measurement;
- discount rates reflect the assumptions which are in line with the cash flow assumptions;
- discount rates are consistent with the key economic factors relating to the currency in which the cash flows are denominated.

The fair value determination methodology developed by Santander Bank Polska S.A. provides for adaptation of the fair value measurement model to the characteristics of the financial asset subject to measurement. When determining the need for adaptation of the model to the features of the asset subject to measurement, Santander Bank Polska S.A. takes into account the following factors:

- approach to the measurement (individual/collective) given the characteristics of the instrument subject to measurement;
- whether the asset is impaired;
- whether a schedule of payments is available;
- whether the asset subject to measurement is still offered by Santander Bank Polska S.A. and whether the products recently provided to customers can be a reference group for that asset.

Other significant groups of financial instruments measured at fair value are all derivatives, financial assets held within a residual business model, debt investment financial assets held within a business model whose objective is achieved by both collecting contractual cash flows and selling financial assets, and equity investment financial assets. These financial instruments are either measured with reference to a quoted market price for that instrument or by using a respective measurement 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, Santander Bank Polska S.A. takes into account the need to identify additional adjustments to the fair value of the counterparty credit risk.

The fair value measurement models are reviewed periodically.

A summary of the carrying amounts and fair values of the individual groups of assets and liabilities is presented in Note 42.

Classification of leases

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

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

Operating lease

In the case of lease contracts made by Santander Bank Polska S.A. as the lessor, the leased assets are recognised in the statement of financial position because of the transfer of substantially all the risks and rewards of ownership to the lessee.

In the case of lease contracts made by Santander Bank Polska S.A. as the lessee, the leased assets are not recognised in the statement of financial position.

All operating lease payments are recognised as income or expense in the income statement on a straight-line basis over the lease term.

Finance lease

Santander Bank Polska S.A. as the lessor

In the case of leases under which substantially all the risks and rewards of ownership are transferred, assets subject to lease are derecognised from the statement of financial position. However, Santander Bank Polska S.A. presents a receivable at an amount equal to the present value of the minimum lease payments. Lease payments are divided between financial income and reduction of the receivable balance in a way enabling Santander Bank Polska S.A. to obtain a constant rate of return on the outstanding receivable.

Lease payments under contracts which do not meet the criteria of a finance lease are recognised as income in the income statement on a straight-line basis over the lease term.

Santander Bank Polska S.A. as the lessee

In the case of leases under which substantially all the risks and rewards of ownership are transferred to Santander Bank Polska S.A., assets subject to lease are recognised as fixed assets. Concurrently, liabilities are recognised at an amount equal to the present value of the minimum lease payments at inception of the lease. Lease payments are divided between lease expenses and reduction of the liability balance in a way enabling Santander Bank Polska S.A. to obtain a constant rate of return on the outstanding liability. Finance lease expenses are recognised directly in the income statement.

Fixed assets which are subject of finance lease contracts are amortised on the basis applicable to own fixed assets. However, if it is not certain whether ownership of the underlying asset is transferred, fixed assets used under finance lease contracts are amortised for the shorter of the following periods: expected useful life or lease term.

Lease payments under contracts which do not meet the criteria of a finance lease are recognised as expenses in the income statement on a straight-line basis over the lease term.

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.

Information about changes to the classification of leases and impact on the statement of financial position arising from the implementation of IFRS 16 Leases as of 1 January 2019 is presented in Section 2.2 “New standards and interpretations and changes to existing standards or interpretations which can be applicable to Santander Bank Polska S.A. and are not yet effective and were not previously introduced”.

Economic life of intangible and tangible fixed assets

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

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

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

Economic life of fixed assets is periodically reviewed by Santander Bank Polska S.A.

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 Santander Bank Polska S.A. assesses probability of the programme vesting which affects the programme value in the costs of the reporting period. Description of the share-based incentive scheme is contained in Note 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.

Changes in judgements and estimates

In 2018, the scope of data covered by estimates changed in comparison with Santander Bank Polska S.A. unconsolidated financial statements for 2017, due to:

- obligatory assessment of business model, introduced under IFRS 9 Financial Instruments (previously not required under IAS 39 Financial Instruments: Recognition and Measurement), and a change in approach to estimating losses on the credit exposures measured at amortised cost or at fair value through other comprehensive income and introduction of the mandatory rule that financial assets which do not meet the contractual cash flow test are measured at fair value through profit or loss, and
- disclosure of judgements (and changes in the judgements) made in applying this Standard that significantly affect the determination of the timing of satisfaction of performance obligations, the transaction price and the amounts allocated to performance obligations – this requirement having been introduced under IFRS 15 Revenue from Contracts with Customers.

2.7. Evaluations that may significantly affect the amounts recognized in the financial statement

When applying the accounting principles, the management of Santander Bank Polska S.A., in addition to assessments that require estimates, makes various subjective assessments that may significantly affect the amounts recognized in financial statements.

Assessment whether contractual cash flows are solely payments of principal and interest

The key issue for Santander Bank Polska S.A. business, is to assess whether the contractual terms related to financial assets component indicate the existence of certain cash flow dates, which are only the repayment of the nominal value and interest on the outstanding nominal value.

For the purposes of this assessment, 'principal' is defined as the fair value of the financial asset on initial recognition and 'interest' is defined as consideration for the time value of money, for the credit risk associated with the principal amount outstanding during a particular period of time and for other basic lending risks and costs (e.g. liquidity risk and administrative costs), as well as a profit margin.

In assessing whether the contractual cash flows are solely payments of principal and interest, Santander Bank Polska S.A. considers the contractual terms of the instrument. This includes assessing whether the financial assets contains a contractual term that could change the timing or amount of contractual cash flows such that it would not meet this condition. In making the assessment the Santander Bank Polska S.A. considers:

- contingent events that would change the amount and timing of cash flows,
- leverage features,
- prepayment and extension terms,
- terms that limit Santander Bank Polska S.A. claim to cash flows from specified assets (e.g. non-recourse asset arrangements)
- features that modify consideration for the time value of money.

A prepayment feature is consistent with the SPPI criterion if the prepayment amount substantially represents unpaid amounts of principal and interest on the principal amount outstanding, which may include reasonable compensation for early termination of the contract.

In addition, a prepayment feature is treated as consistent with this criterion if a financial asset is acquired or originated at a premium or discount to its contractual paramount, the prepayment amount substantially represents the contractual par amount plus accrued (but unpaid) contractual interest (which may also include reasonable compensation for early termination), and the fair value of the prepayment feature is insignificant on initial recognition.

In the process of applying Santander Bank Polska S.A. accounting policy management assessed whether financial assets, including loan agreements, whose interest rate construction contains a multiplier greater than 1, meet classification criteria allowing their valuation at Amortised cost, that is:

- business model and
- characteristics of contractual cash flows.

The most significant portfolio of financial assets, whose interest rate construction contained a multiplier greater than 1, includes credit cards granted until 01.08.2016, whose interest rate formula was based on 4x lombard rate and did not contain direct reference to the provisions of the Civil Code in the regard of interest cap.

This financial asset portfolio is maintained in a business model whose objective is to hold financial assets in order to collect contractual cash flows. Credit risk for these assets is the basic risk managed in portfolios, and historical analysis of frequency and volume of sales do not indicate significant sales of asset portfolios for reasons other than credit risk.

In addition, it was not found that:

- fair value was a key performance indicator (KPI) for assessing portfolio performance for internal reporting purposes,
- the assessment of the portfolio's results was based only on the fair value of assets in the analyzed portfolio,
- remuneration of portfolio managers was related to the fair value of assets in the analyzed portfolio.

Whereas contractual terms related to a financial asset indicate that there are specific cash flow terms that are not solely payments of principal and interest on the principal outstanding due to the existence of a financial leverage in the construction of interest rate. It increases the variability of the contractual cash flows with the result that they do not have the economic characteristics of interest. The credit card portfolio with the above characteristics has been reclassified from the portfolio measured at amortised cost to the portfolio measured at fair value through profit or loss.

Business Model Assessment

Business models at Santander Bank Polska S.A. are determined at a level that reflects how groups of financial assets are managed together to achieve a particular business objective. The business model does not depend on the intentions of the Santander Bank Polska S.A. management regarding a particular instrument, which is why the model is assessed at a higher level of aggregation.

The business model refers to how Santander Bank Polska S.A. manages its financial assets in order to generate cash flows. That is, the business model determines whether cash flows will result from:

- a contract (a business model whose objective is to hold assets in order to collect contractual cash flows)
- the sale of financial assets (other/residual business model) or
- from both of those sources (a business model whose objective is achieved by both collecting contractual cash flows and selling financial assets).

The assessment of a business model involves the analysis of qualitative and quantitative criteria (both presented in the section concerning classification of financial assets).

If Santander Bank Polska S.A. changes the business model for financial asset management, the entire portfolio of assets covered by that business model is reclassified on the level of a specific reporting segment, and the consequences arising from the change of the assessment category are recognised at a point of time in the profit and loss account or other comprehensive income.

Santander Bank Polska S.A. expects that such changes will take place rarely. They are determined by Santander Bank Polska S.A. senior management as a result of external or internal changes and must be significant to Santander Bank Polska S.A. operations and demonstrable to external parties.

2.8. Accounting policies

With the exception of the changes described in point 2.3, the Santander Bank Polska S.A. consistently applied the adopted accounting principles both for the reporting period for which the statement is prepared and for the comparative period.

Accounting principles applied by the Santander Bank Polska S.A. in relation to financial instruments, by December 31, 2017 they were described in point 2.9.

Foreign currency

Foreign currency transactions

The Polish zloty (PLN) is the functional currency of Santander Bank Polska S.A.

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 equity instruments of other entities measured at fair value through other comprehensive income, which are recognised in other comprehensive income.

Financial assets and liabilities

Recognition and derecognition

Initial recognition

Santander Bank Polska S.A. recognises a financial asset or a financial liability in its statement of financial position when, and only when, it becomes bound by contractual provisions of the instrument.

A regular way purchase or sale of financial assets is recognised and derecognised, as applicable, at the settlement date.

Derecognition of financial assets

Santander Bank Polska S.A. derecognises a financial asset when and only when, if:

- contractual rights to the cash flows from that financial asset have expired, or
- Santander Bank Polska S.A. transfers a financial asset, and such operation meets the derecognition criteria specified further in this policy.

Santander Bank Polska S.A. transfers a financial asset when and only when, if:

- Santander Bank Polska S.A. transfers contractual rights to the cash flows from that financial asset, or
- Santander Bank Polska S.A. retains contractual rights to receive the cash flows from that financial asset, but assumes a contractual obligation to pay the cash flows to one or more recipients in an arrangement that meets the conditions specified further in this policy.

When Santander Bank Polska S.A. retains the contractual rights to receive the cash flows of a financial asset (the 'original asset'), but assumes a contractual obligation to pay those cash flows to one or more entities (the 'eventual recipients'), then Santander Bank Polska S.A. treats the transaction as a transfer of a financial asset if, and only if, all of the following three conditions are met:

- Santander Bank Polska S.A. has no obligation to pay amounts to the eventual recipients unless it collects equivalent amounts from the original asset,
- Santander Bank Polska S.A. is prohibited by the terms of the transfer contract from selling or pledging the original asset other than as security to the eventual recipients for the obligation to pay them cash flows,
- Santander Bank Polska S.A. has an obligation to remit any cash flows it collects on behalf of the eventual recipients without material delay. In addition, Santander Bank Polska S.A. is not entitled to reinvest such cash flows, except for investments in cash or cash equivalents (as defined in IAS 7 Statement of Cash Flows) during the short settlement period from the collection date to the date of required remittance to the eventual recipients, and interest earned on such investments is passed to the eventual recipients.

When Santander Bank Polska S.A. transfers a financial asset, it shall evaluate the extent to which it retains the risks and rewards of ownership of the financial asset. In such a case:

- if Santander Bank Polska S.A. transfers substantially all of the risks and rewards of ownership, then it shall derecognise the financial asset and recognise separately as assets or liabilities any rights and obligations created or retained in the transfer;
- Santander Bank Polska S.A. transfers substantially all the risks and rewards of ownership, then it shall continue to recognise the financial asset;
- Santander Bank Polska S.A. neither transfers nor retains substantially all the risks and rewards of ownership, then it shall verify if it has retained control of the financial asset. In such a case:
    - (a) if Santander Bank Polska S.A. has not retained control, it shall derecognise the financial asset and recognise separately as assets or liabilities any rights and obligations created or retained in the transfer;
    - (b) if Santander Bank Polska S.A. has retained control, it shall continue to recognise the financial asset to the extent of its continuing involvement in the financial asset.

The transfer of risks and rewards is evaluated by comparing Santander Bank Polska S.A. exposure, before and after the transfer, with the variability in the amounts and timing of the net cash flows of the transferred asset. Santander Bank Polska S.A. has retained substantially all the risks and rewards of ownership of a financial asset if its exposure to the variability in the present value of the future net cash flows from the financial asset does not change significantly as a result of the transfer. Santander Bank Polska S.A. transfers substantially all the risks and rewards of ownership of a financial asset if its exposure to such variability is no longer significant in relation to the total variability in the present value of the future net cash flows associated with the financial asset.

Santander Bank Polska S.A. derecognises a part of financial asset (or a group of similar financial assets) when and only when, if the asset to be derecognised fulfills one of the three conditions:

- that part comprises only specifically identified cash flows on a financial asset (or a group of similar financial assets),
- that part comprises only a proportionate share of cash flows from that financial asset (or a group of similar financial assets),
- that part comprises only a fully proportionate (pro rata) share of specifically identified cash flows from a financial asset (or a group of similar financial assets).

In all other cases, Santander Bank Polska S.A. derecognises a part of financial asset (or a group of similar financial assets).

Derecognition of financial liabilities

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

An exchange between Santander Bank Polska S.A. and the lender of debt instruments with substantially different terms shall be accounted for as an extinguishment of the original financial liability and the recognition of a new financial liability. Similarly, a substantial modification of the terms of an existing financial liability or a part of it (whether or not attributable to the financial difficulty of the debtor) shall be accounted for as an extinguishment of the original financial liability and the recognition of a new financial liability.

The difference between the carrying amount of a financial liability (or part of a financial liability) extinguished or transferred to another party and the consideration paid, including any non-cash assets transferred or liabilities assumed, shall be recognised in profit or loss.

If Santander Bank Polska S.A. repurchases a part of a financial liability, Santander Bank Polska S.A. shall allocate the previous carrying amount of the financial liability between the part that continues to be recognised and the part that is derecognised based on the relative fair values of those parts on the date of the repurchase. The difference between:

- the carrying amount allocated to the part derecognised, and
- the consideration paid, including any non-cash assets transferred or liabilities assumed, for the part derecognised,

are recognised in profit or loss.

Classification of financial assets and financial liabilities

Classification of financial assets

Classification of financial assets which are not equity instruments

Unless Santander Bank Polska S.A. has made a prior decision to measure a financial asset at fair value through profit or loss, the Santander Bank Polska S.A. classifies financial asset that are not an equity instrument as subsequently measured at amortised cost or at fair value through other comprehensive income or fair value through profit or loss on the basis of both:

- the business model of Santander Bank Polska S.A. for managing the financial assets and
- the contractual cash flow characteristics of the financial asset.

A financial asset is measured at amortised cost if both of the following conditions are fulfilled:

- the financial asset is held in a business model whose purpose is to hold financial assets to collect contractual cash flows, and
- the contractual terms of a financial asset give rise on specified dates to cash flows that are solely payments of principal and interest on the principal amount outstanding.

A financial asset is measured at fair value through other comprehensive income if both of the following conditions are fulfilled:

- the financial asset is held in a business model whose objective is achieved by both collecting contractual cash flows and selling financial assets, and
- the contractual terms of a financial asset give rise on specified dates to cash flows that are solely payments of principal and interest on the principal amount outstanding.

If a financial asset is not measured at amortised cost or at fair value through other comprehensible income, it is measured at fair value through profit or loss.

Santander Bank Polska S.A. may, at initial recognition, irrevocably designate a financial asset as measured at fair value through profit or loss if doing so eliminates or significantly reduces a measurement or recognition inconsistency (sometimes referred to as an “accounting mismatch”) that would otherwise arise from measuring assets or liabilities or recognising the gains and losses on them on different bases.

Classification of financial assets which are equity instruments

The financial asset that is an equity instrument, the Santander Bank Polska S.A. measures at fair value through the profit or loss, unless Santander Bank Polska S.A. made an irrevocable election at initial recognition for particular investments in equity instruments to present subsequent changes in fair value in other comprehensive income.

Business models

Business models at Santander Bank Polska S.A. are determined at a level that reflects how groups of financial assets are managed together to achieve a particular business objective. The business model does not depend on the intentions of the Santander Bank Polska S.A. key management regarding a particular instrument.

The business model refers to how Santander Bank Polska S.A. manages its financial assets in order to generate cash flows. That is, the business model determines whether cash flows will result from:

- collecting contractual cash flows
- selling financial assets
- or both.

Consequently, the business model assessment is not performed on the basis of scenarios that Santander Bank Polska S.A. does not reasonably expect to occur, such as so-called “worst case” or “stress case” scenarios.

Santander Bank Polska S.A. determines the business model on the basis of the assessment of qualitative and quantitative criteria.

Qualitative criteria for the assessment of a business model

The business model for managing financial assets is a matter of fact and not merely an assertion. It is observable through the activities undertaken to achieve the objective of the business model. Santander Bank Polska S.A. uses judgement when it assesses its business model for managing financial assets and that assessment is not determined by a single factor or activity. Santander Bank Polska S.A. considers all relevant qualitative and quantitative criteria available at the date of business model assessment. Such relevant evidence includes the following issues:

- policies and business objectives applicable to a given portfolio and their effective delivery. In particular, the assessment covers the management strategy for generating income from contractual interest payments, maintaining a specific profile of portfolio interest rates, managing liquidity gap and generating cash flows from the sale of financial assets;

- method for assessing the profitability of the financial asset portfolio and its reporting and analysis by the key management personnel;

- risks which affect the profitability and effectiveness of a specific business model (and financial assets held within such a business model) as well as method for managing such risks;

- method for remunerating business managers as part of a specific business model, i.e. whether the remuneration payable to the key management personnel depends on changes in the fair value of financial assets or the value of contractual cash flows.

Quantitative criteria for the assessment of a business model

In addition to qualitative criteria, the business model should also be reviewed in terms of quantitative aspects, unless the initial analysis of qualitative criteria clearly implies a residual model managed on the fair-value basis.

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.

As part of the analysis of quantitative criteria, Santander Bank Polska S.A. reviews the frequency, values and the time of sale of financial assets in the previous periods, reasons for such sale and expectations as to the future sales activity.

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

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

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

Business model types

The analysis of qualitative and quantitative criteria makes it possible to identify three basic business models applied in the operations of Santander Bank Polska S.A.:

- the business model whose objective is to hold assets in order to collect contractual cash flows (hold to collect),
- the business model whose objective is achieved by both collecting contractual cash flows and selling financial assets (hold to collect and sell),
- the other/ residual business model (the business model whose objective is achieved by selling assets).

Presented below are characteristics of all business models, with an indication of the financial instruments assigned to each.

A business model whose objective is to hold assets in order to collect contractual cash flows

Financial assets that are held within a business model whose objective is to hold assets in order to collect contractual cash flows are managed to realise cash flows by collecting contractual payments over the life of the instrument. That is, Santander Bank Polska S.A. manages the assets held within the portfolio to collect those particular contractual cash flows (instead of managing the overall return on the portfolio by both holding and selling assets). In determining whether cash flows are going to be realised by collecting the financial assets' contractual cash flows, it is necessary to consider the frequency, value and timing of sales in prior periods, the reasons for those sales and expectations about future sales activity. However, sales in themselves do not determine the business model and therefore cannot be considered in isolation. Instead, information about past sales and expectations about future sales provide evidence related to how Santander Bank Polska S.A. stated objective for managing the financial assets is achieved and, specifically, how cash flows are realised. Santander Bank Polska S.A. each time considers information about past sales within the context of the reasons for those sales and the conditions that existed at that time as compared to current conditions. Although the objective of the business model may be to hold financial assets in order to collect contractual cash flows, Santander Bank Polska S.A. needs not hold all of those instruments until maturity. Thus, Santander Bank Polska S.A. business model can be to hold financial assets to collect contractual cash flows even when sales of financial assets occur or are expected to occur in the future.

A business model whose objective is to hold assets in order to collect contractual cash flows spans the entire spectrum of credit activity, including but not limited to mortgage and consumer loans, credit cards, loans granted and debt instruments (e.g. treasury bonds, corporate bonds), which are not held for liquidity management purposes. Financial assets on account of trading settlements are substantially also recognised under this model. Such assets are recognised in the books of Santander Bank Polska S.A. on the basis of an invoice issued payable within maximum 12 months.

A business model whose objective is achieved by both collecting contractual cash flows and selling financial assets

Santander Bank Polska S.A. may hold financial assets in a business model whose objective is achieved both by collecting contractual cash flows and by selling financial assets. In this type of business model, the key management personnel of Santander Bank Polska S.A. decided that both collecting contractual cash flows and selling financial assets are integral to achieving the business model's objective. There are various objectives that may be consistent with this type of business model. For example, the objective of the business model may be to manage everyday liquidity needs, to maintain a particular interest yield profile or to match the duration of the financial assets to the duration of the liabilities that those assets are funding. To achieve such an objective, Santander Bank Polska S.A. will both collect contractual cash flows and sell financial assets.

Compared to a business model whose objective is to hold financial assets to collect contractual cash flows, this business model will typically involve greater frequency and value of sales. This is because selling financial assets is integral to achieving the business model's objective instead of being only incidental to it. However, there is no specific frequency or sales value threshold that must be achieved in this business model as collecting contractual cash flows and selling financial assets are both integral to achieving the model's objective.

A business model whose objective is achieved by both collecting contractual cash flows and selling financial assets includes:

- financial assets acquired for the purpose of liquidity management, such as State Treasury bonds or NBP bond and
- loans and advances subject to underwriting, i.e. portion of credit exposures that are planned to be sold before maturity for reasons other than increase in credit risk

Other/ residual business model

Financial assets are measured at fair value through profit or loss if they are not held within a business model whose objective is to hold assets to collect contractual cash flows or within a business model whose objective is achieved by both collecting contractual cash flows and selling financial assets. A business model that results in measurement at fair value through profit or loss is one in which Santander Bank Polska S.A. manages the financial assets with the objective of realising cash flows through the sale of the assets. Santander Bank Polska S.A. makes decisions based on the assets' fair values and manages the assets to realise those fair values. In this case, Santander Bank Polska S.A. objective will typically result in active buying and selling. Even though Santander Bank Polska S.A. will collect contractual cash flows while it holds the financial assets, the objective of such a business model is not achieved by both collecting contractual cash flows and selling financial assets. This is because the collection of contractual cash flows is not integral to achieving the business model's objective; instead, it is incidental to it.

Another, residual, model is used for classifying assets held by Santander Bank Polska S.A. but not covered by the first or second category of the business model. They include assets from the "held for trading" category in the financial statements, such as listed equity instruments, commercial bonds acquired for trading purposes and derivatives (e.g. options, IRS, FRA, CIRS, FX Swap contracts) which are not embedded derivatives.

The business model whose objective is to hold assets in order to collect contractual cash flows is the most frequent business model in Santander Bank Polska S.A. except in the case of:

- debt instruments measured at fair value through other comprehensive income that are maintained in the ALM segment and credits and loans covered by underwriting process described above; those instruments are subject to the business model whose objective is achieved by both collecting contractual cash flows and selling financial assets,
- instruments held for trading, including bonds and derivative instruments which are not subject to hedge accounting; those instruments are covered by the other/ residual business model.

Changing the business model

Santander Bank Polska S.A. reclassifies all affected financial assets when, and only when, it changes its business model for managing financial assets. Such changes are expected to be very infrequent. They are determined by the senior management of Santander Bank Polska S.A. as a result of external or internal changes and must be significant to the Santander Bank S.A. Polska operations and demonstrable to external parties. Accordingly, a change in the business model of Santander Bank Polska S.A. will occur only when Santander Bank Polska S.A. either begins or ceases to perform an activity that is significant to its operations (for example, when a business line has been acquired, disposed of or terminated).

The objective of the business model of Santander Bank Polska S.A. is changed before the reclassification date.

The following are not changes in business model:

- a change in intention related to particular financial assets (even in circumstances of significant changes in market conditions),
- the temporary disappearance of a particular market for financial assets,
- a transfer of financial assets between parts of Santander Bank Polska S.A. with different business models.

If Santander Bank Polska S.A. reclassifies a financial asset, it applies the reclassification prospectively from the reclassification date.

If Santander Bank Polska S.A. reclassifies a financial asset out of the amortised cost measurement category and into the fair value through profit or loss measurement category, its fair value is established at the reclassification date. Any gain or loss arising from a difference between the previous amortised cost of the financial asset and fair value is recognised in profit or loss.

Characteristics of contractual cash flows

Santander Bank Polska S.A. classifies financial assets on the basis of the contractual cash flow characteristics of the financial asset if that asset is held within a business model:

- whose objective is to hold assets to collect contractual cash flows or
- whose objective is achieved by both collecting contractual cash flows and selling financial assets unless Santander Bank Polska S.A. has designated that financial asset to be measured at fair value through profit or loss.

For this purpose, Santander Bank Polska S.A. determines if the contractual cash flows generated by the asset in question are solely payments of principal and interest on the principal amount outstanding.

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).

Interest should include the consideration for:

- the time value of money,
- credit risk,
- other basic lending risks and costs,
- and a profit margin.

The time value of money is the element of interest that provides consideration for only the passage of time. That is, the time value of money element does not provide consideration for other risks or costs associated with holding the financial asset. In order to assess whether the element provides consideration for only the passage of time, Santander Bank Polska S.A. applies judgement and considers relevant factors such as the currency in which the financial asset is denominated and the period for which the interest rate is set.

Credit risk is defined as the risk that one party to a financial instrument will cause a financial loss for Santander Bank Polska S.A. by failing to discharge an obligation. In other words, credit risk refers to the possibility of the Customer's failure to repay the principal and interest due within the contractual deadline.

Other basic lending risks and costs include for example administration costs related to the analysis of the credit application, assessment of the customer's repayment capacity, monitoring of the customer's economic and financial standing, etc.

Financial instruments which do not meet the requirements of contractual cash flow characteristics include:

- credit card portfolios whose interest rates are set on the basis of principles applicable in Santander Bank Polska S.A. since 1 August 2016;

- instruments providing for participation of Santander Bank Polska S.A. in the customer's profit or loss; and

- other instruments whose contractual cash flows do not meet the definition of interest due to the lack of an economic relationship between the amount of interest accrued and the amount of interest payable to Santander Bank Polska S.A.

Classification of financial liabilities

Santander Bank Polska S.A. classifies all financial liabilities as subsequently measured at amortised cost, except for:

- financial liabilities measured at fair value through profit or loss. Such liabilities, including derivatives that are liabilities, shall be subsequently measured at fair value.
- financial liabilities that arise when a transfer of a financial asset does not qualify for derecognition or when the continuing involvement approach applies;
- financial guarantee contracts. After initial recognition at fair value, the issuer shall measure contract at the higher of:
    (1) amount of the expected credit loss allowance,
    (2) initial recognised amount, less respective cumulated income recognised as per IFRS 15;
- commitments to provide a loan at a below-market interest rate. If the liability is not measured at fair value through profit or loss, the issuer shall measure it at the higher of:
    (1) amount of the expected credit loss allowance,
    (2) Initial recognised amount, less respective cumulated income recognised as per IFRS 15;
- contingent consideration recognised by the acquire under the business combination arrangement governed by IFRS 3. Such contingent consideration shall subsequently be measured at fair value with changes recognised in profit or loss.

Upon initial recognition of the liability, Santander Bank Polska S.A. may irrevocably classify such item as the one measured at fair value through profit or loss if such an accounting method provides a better view of the accounts, because:

- it eliminates or largely prevents the accounting mismatch that would arise if assets or liabilities or related profit or loss were recognised under different accounting methods, or
- a group of financial assets or liabilities is managed and measured at fair value as per the documented strategy for risk management and investments, and information about these items are provided to key executives within the Santander Bank Polska S.A. (as per the definition specified in IAS 24 Related Party Disclosures).

Embedded derivatives

An embedded derivative is a component of a hybrid contract that also includes a non-derivative host—with the effect that some of the cash flows of the combined instrument vary in a way similar to a stand-alone derivative. An embedded derivative causes some or all of the cash flows that otherwise would be required by the contract to be modified according to a specified interest rate, financial instrument price, commodity price, foreign exchange rate, index of prices or rates, credit rating or credit index, or other variable, provided in the case of a non-financial variable that the variable is not specific to a party to the contract. A derivative that is attached to a financial instrument but is contractually transferable independently of that instrument, or has a different counterparty, is not an embedded derivative, but a separate financial instrument.

For financial assets that meet the definition of embedded derivatives, a derivative which is a component of a hybrid contract is not separated from the host contract which is not a derivative.

Measurement of financial assets and financial liabilities

Initial measurement

At initial recognition, Santander Bank Polska S.A. measures a financial asset or financial liability at its fair value plus or minus, in the case of a financial asset or financial liability not 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.

However, if the fair value of the financial asset or financial liability at initial recognition differs from the transaction price, Santander Bank Polska S.A. recognises this instrument on that date as follows:

- when the fair value is evidenced by a quoted price in an active market for an identical asset or liability (i.e. a Level 1 input) or based on a valuation technique that uses only data from observable markets, then Santander Bank Polska S.A. recognises the difference between the transaction price and the fair value at initial recognition as a gain or loss.
- in all other cases, at the measurement adjusted to defer the difference between the fair value at initial recognition and the transaction price. After initial recognition, Santander Bank Polska S.A. recognises that deferred difference as a gain or loss only to the extent that it arises from a change in a factor (including time) that market participants would take into account when pricing the asset or liability.

At initial recognition, Santander Bank Polska S.A. shall measure trade receivables that do not have a significant financing component (determined in accordance with IFRS 15) at their transaction price (as defined in IFRS 15).

Subsequent measurement of financial assets

After initial recognition, Santander Bank Polska S.A. recognises a financial asset:

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

Impairment charges are not calculated for financial assets measured at fair value through profit or loss.

Subsequent measurement of financial liabilities

After initial recognition, Santander Bank Polska S.A. recognises a financial liability:

- at amortised cost, or
- at fair value through profit or loss.

“Other financial liabilities” cover items other than financial liabilities measured at fair value through profit or loss. These are liabilities measured at amortised costs, and they include: deposits from banks, deposits from customers, liabilities due to repo transactions, loans and advances obtained, issued debt instruments and subordinated liabilities.

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

Amortised cost measurement

Financial assets

Effective interest method

Interest revenue is calculated by applying the effective interest rate to the gross carrying amount of financial assets, except for credit-impaired financial assets. At the time a financial asset or a group of similar financial assets is reclassified to stage 3, interest revenue is calculated on the basis of a net value of a financial asset and presented at the interest rate used for the purpose of discounting the future cash flows for the purpose of measurement of impairment.

This does not apply to POCI assets, in the case of which the interest revenue is calculated on the basis of the gross carrying amount, applying the effective interest rate adjusted for credit risk over the lifetime of the asset. The credit-adjusted effective interest rate is calculated by taking into account the future cash flows adjusted for the effect of credit risk over the lifetime of the asset.

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, Santander Bank Polska S.A. shall estimate cash flows considering all contractual terms of the financial instrument (for example, prepayment, call and similar options) but does not consider future credit losses.

The calculation includes 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.

Credit-adjusted effective interest rate is the rate that exactly discounts the estimated future cash payments or receipts through the expected life of the financial asset to the amortised cost of a financial asset that is a purchased or originated credit-impaired financial asset. When calculating the credit-adjusted effective interest rate, Santander Bank Polska S.A. estimates the expected cash flows by considering all contractual terms of the financial asset (for example, prepayment, extension, call and similar options) and expected credit losses. The calculation includes all fees and points paid or received between parties to the contract that are an integral part of the effective interest rate, transaction costs, and all other premiums or discounts. There is a presumption that the cash flows and the expected life of a group of similar financial instruments can be estimated reliably. However, in those rare cases when it is not possible to reliably estimate the cash flows or the remaining life of a financial instrument (or group of financial instruments), Santander Bank Polska S.A. uses the contractual cash flows over the full contractual term of the financial instrument (or group of financial instruments).

Gross carrying amount of a financial asset is the amortised cost of a financial asset, before adjusting for any loss allowance and without taking into account the value of penalty interest calculated on the overdue principal.

Modification of contractual cash flows

The concept of modification

Changes to the contractual cash flows in respect of the financial asset are regarded by Santander Bank Polska S.A. as modification if made in the form of an annex. Changes to the contractual cash flows arising from performance of the contractual obligations are not considered to be a modification.

If the terms of the financial asset agreement change, the Santander Bank Polska S.A. assesses whether the cash flows generated by the modified asset differ significantly from cash flows generated by financial asset before modification of the terms of the asset agreement. The result on modification is the difference between present value of the modified cash flows discounted using the old effective interest rate and instrument's gross balance sheet value before modification.

Modification criteria

When assessing whether a modification is substantial or minor, Santander Bank Polska S.A. takes into account both quantitative and qualitative criteria. Both criteria groups are each time analyzed together.

Quantitative criteria

To determine the significance of the impact of modifications, the so-called "10% test" is carried out which is based on a comparison of discounted cash flows of the modified financial instrument (using the original effective interest rate) with discounted (also with the original effective interest rate) cash flows of the financial instrument before modification, whose value should correspond to the value of non-available capital, increased by the value of unsecured interest and adjusted for the amount of unsettled commission.

Qualitative criteria

During the qualitative analysis, Santander Bank Polska S.A. takes into account the following aspects:

- adding / removing a feature that violates the contractual cash flow test result,
- currency conversion - except for currency conversions resulting from the transfer of the contract for collection,
- change of the main debtor - change of the contractor results in a significant modification of contractual terms and
- consolidation of several exposures into one under an annex.

Substantial modification

A substantial modification resulting in the exclusion of a financial instrument from the statement of financial position occurs when:

- cash flows of the modified financial instrument are "materially different" from the original financial instrument, i.e. when the difference between discounted cash flows of the modified financial instrument (using the original effective interest rate) and the discounted (also with the original effective interest rate), cash flows of the financial instrument before the modification, is higher than 10%,
- at least one of the quality criteria described above has been breached.

If the modification of a financial asset results in derecognition of the existing financial asset and recognition of the modified financial asset, the modified asset is considered as a "new" financial asset. The new asset is recognized at fair value and the new effective interest rate applied to the new asset is calculated.

Minor modification

If the difference between the value of the future cash flows arising from the changed financial asset discounted at the original effective interest rate and the value of the future cash flows arising from the original asset discounted at the same interest rate does not exceed 10% and the qualitative criteria are not met, the modification is regarded by Santander Bank Polska S.A. as insignificant.

The qualitative criterion does not apply to loans subject to restructuring (i.e. insignificant modification is always recognised in relation to assets in restructuring).

When the contractual cash flows of a financial asset are renegotiated or otherwise modified and the renegotiation or modification does not result in the derecognition of that financial asset in accordance with this policy, Santander Bank Polska S.A. recalculates the gross carrying amount of the financial asset and shall recognise a modification gain or loss in profit or loss. The gross carrying amount of the financial asset shall be recalculated as the present value of the renegotiated or modified contractual cash flows that are discounted at the financial asset's original effective interest rate (or credit-adjusted effective interest rate for purchased or originated credit-impaired financial assets) or, when applicable, the revised effective interest rate. Any costs or fees incurred adjust the carrying amount of the modified financial asset and are amortised over the remaining term of the modified financial asset.

Write-off

Santander Bank Polska S.A. directly reduces the gross carrying amount of a financial asset when the entity has no reasonable expectations of recovering a financial asset in its entirety or a portion thereof. A write-off constitutes a derecognition event.

Write-off may relate to a financial asset in its entirety or to a part of it.

Santander Bank Polska S.A. writes off financial assets if at least one of the following conditions apply:

- The irrecoverability of the debt has been documented;
- there are no reasonable expectations of recovering the financial asset in full or in part;
- the debt is due and payable in its entirety and the value of the credit loss allowance corresponds to the gross value of the exposure, while the expected debt recovery proceeds are nil;
- the asset originated as a result of a crime and the perpetrators have not been identified or
- Santander Bank Polska S.A. has received:
  - a decision on discontinuation of debt enforcement proceedings due to irrecoverability of the debt (in relation to all obligors), issued by a relevant enforcement authority pursuant to Article 824 § 1 (3) of the Polish Code of Civil Procedure, which is recognised by the creditor (Santander Bank Polska S.A.) as corresponding to the facts; or
  - a court decision:
    - dismissing a bankruptcy petition, if the insolvent debtor's assets are insufficient to cover the cost of the proceedings or suffice to cover this cost only; or
    - discontinuing the bankruptcy proceedings or
    - closing the bankruptcy proceedings.

Financial assets written off are them recorded off balance sheet.

Impairment

General approach

Santander Bank Polska S.A. recognises allowances for expected credit losses on a financial asset in respect of:

- financial assets measured at amortised cost or at fair value through other comprehensive income;
- lease receivables;
- contract assets, i.e. the consideration to which Santander Bank Polska S.A. is entitled in exchange for the goods or services transferred to the customer in accordance with IFRS 15 Revenue from Contracts with Customers;
- loan commitments and
- off-balance sheet credit liabilities and financial guarantees.

Santander Bank Polska S.A. applies the impairment requirements for the recognition and measurement of a loss allowance for financial assets that are measured at fair value through other comprehensive income. However, the loss allowance is recognised in other comprehensive income and does not reduce the carrying amount of the financial asset in the statement of financial position.

At each reporting date, Santander Bank Polska S.A. measures the loss allowance for a financial instrument at an amount equal to the lifetime expected credit losses if the credit risk on that financial instrument has increased significantly since initial recognition.

The objective of the impairment requirements is to recognise lifetime expected credit losses for all financial instruments for which there have been significant increases in credit risk since initial recognition — whether assessed on an individual or collective basis — considering all reasonable and supportable information, including that which is forward-looking.

If, at the reporting date, the credit risk on a financial instrument has not increased significantly since initial recognition, Santander Bank Polska S.A. measures the loss allowance for that financial instrument at an amount equal to 12-month expected credit losses.

For loan commitments and financial guarantee contracts, the date that Santander Bank Polska S.A. becomes a party to the irrevocable commitment shall be considered to be the date of initial recognition for the purposes of applying the impairment requirements.

If Santander Bank Polska S.A. has measured the loss allowance for a financial instrument at an amount equal to lifetime expected credit losses in the previous reporting period, but determined at the current reporting date that the credit risk for that financial instrument has declined, Santander Bank Polska S.A. measures the loss allowance at an amount equal to 12-month expected credit losses at the current reporting date.

Santander Bank Polska S.A. recognises in profit or loss, as an impairment gain or loss, the amount of expected credit losses that is required to adjust the loss allowance at the reporting date to the amount that is required to be recognised.

Pursuant to the guidelines contained in the ITG document of 11 December 2015 (IFRS Transition Resource for Impairment of Financial Instruments: "Measurement of the loss allowance for credit-impaired financial assets"), Santander Bank Polska S.A. presents the interest income adjustment (i) in the statement of financial position: a reduction of the interest income for exposures classified to stage 3 to the level of recoverable interest as an element of an allowance for expected credit losses; (ii) in the income statement: in the net interest income.

Simplified approach for trade receivables and contract assets

In the case of trade receivables and contract assets, Santander Bank Polska S.A. always measures the loss allowance at an amount equal to lifetime expected credit losses for trade receivables or contract assets that result from transactions that are within the scope of IFRS 15, and that do not contain a significant financing component (or when Santander Bank Polska S.A. applies the practical expedient for contracts that are one year or less) in accordance with IFRS 15.

Purchased or originated credit-impaired financial assets

At the reporting date, Santander Bank Polska S.A. recognises only the changes in lifetime expected credit losses as a loss allowance for purchased or originated credit-impaired financial assets.

Interest revenue on POCI assets is calculated on the basis of the net carrying amount, applying the effective interest rate adjusted for credit risk over the lifetime of the asset. The credit-adjusted effective interest rate is calculated by taking into account the future cash flows adjusted for the effect of credit risk over the lifetime of the asset.

At each reporting date, Santander Bank Polska S.A. recognises in profit or loss the amount of the change in lifetime expected credit losses as an impairment gain or loss. Santander Bank Polska S.A. recognises favourable changes in lifetime expected credit losses as an impairment gain, even if the lifetime expected credit losses are less than the amount of expected credit losses that were included in the estimated cash flows on initial recognition.

Contingent liabilities

Santander Bank Polska S.A. creates provisions for impairment risk-bearing irrevocable contingent 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 contingent exposure set using the Credit Conversion Factor (CCF) and the current value of expected future cash flows under this exposure.

Santander Bank Polska S.A. raises provisions for off-balance sheet liabilities subject to credit risk, broken down into 3 stages.

Approach to the estimation of risk parameters used to calculate expected losses

For the purpose of estimating allowances for expected losses, Santander Bank Polska S.A. continues using own estimates of risk parameters that are based on internal models, however with the necessary modifications in the context of IFRS 9 requirements (such as estimating the parameters over the lifetime of the exposure or taking into account future macroeconomic conditions). Santander Bank Polska S.A. has developed a methodology for models' parameters and built models compliant with IFRS 9. Expected credit losses are equal to the estimated PD parameter multiplied by the estimated LGD and EAD parameters. The final value of expected credit losses is the sum of expected losses from all periods (depending on the stage, either in 12 months or in the entire lifetime) discounted using the effective interest rate. The estimated parameters are adjusted for macroeconomic scenarios in accordance with the assumptions of IFRS 9. The scenarios used by Santander Bank Polska S.A. are developed internally.

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

Gains and losses

A gain or loss on a financial asset or liability measured at fair value is recognised in profit or loss unless the asset or liability is:

- a part of a hedging relationship,
- an investment into an equity instrument and Santander Bank Polska S.A. has decided to present gains and losses on that investment in other comprehensive income,
- a financial liability designated as measured at fair value through profit or loss and Santander Bank Polska S.A. is required to present the effects of changes in the liability's credit risk in other comprehensive income; or
- is a financial asset measured at fair value through other comprehensive income and Santander Bank Polska S.A. is required to recognise some changes in fair value in other comprehensive income.

Dividends are recognised in profit or loss only if:

- the right of Santander Bank Polska S.A. to receive payment of the dividend is established,
- it is probable that the economic benefits associated with the dividend will flow to Santander Bank Polska S.A., and
- the amount of the dividend can be measured reliably.

A gain or loss on a financial asset that is measured at amortised cost and is not part of a hedging relationship is recognised in profit or loss through the amortisation process or in order to recognise impairment gains or losses. A gain or loss on a financial liability that is measured at amortised cost and is not part of a hedging relationship is recognised in profit or loss when the financial liability is derecognised and through the amortisation process.

With regard to the financial assets recognised by Santander Bank Polska S.A. at the settlement date, any change in the fair value of the asset to be received during the period between the trade date and the settlement date is not recognised for assets measured at amortised cost. For assets measured at fair value, however, the change in fair value is recognised in profit or loss or in other comprehensive income, as appropriate. The trade date means the date of initial recognition for the purposes of applying the impairment requirements.

Investments in equity instruments

Investments in equity instruments are measured at fair value through profit or loss unless at their initial recognition Santander Bank Polska S.A. makes an irrevocable election to present in other comprehensive income subsequent changes in the fair value of an investment in an equity instrument within the scope of this policy that is neither held for trading nor contingent consideration recognised by an acquirer in a business combination to which IFRS 3 applies.

If Santander Bank Polska S.A. has elected to measure equity instruments at fair value through profit or loss, dividends from that investment are recognised in profit or loss.

As at the reporting date, Santander Bank Polska S.A. elected to measure all equity instruments other than shares in subsidiaries, associates and joint ventures at fair value through other comprehensive income.

Liabilities designated as measured at fair value through profit or loss

Santander Bank Polska S.A. presents a gain or loss on a financial liability that is designated as measured at fair value through profit or loss as follows:

a) the amount of change in the fair value of the financial liability that is attributable to changes in the credit risk of that liability is presented in other comprehensive income, and

b) the remaining amount of change in the fair value of the liability is presented in profit or loss unless the treatment of the effects of changes in the liability's credit risk described in (a) would create or enlarge an accounting mismatch in the profit or loss of Santander Bank Polska S.A.

If the requirements specified above would create or enlarge an accounting mismatch in the profit or loss of Santander Bank Polska S.A., Santander Bank Polska S.A. presents all gains or losses on that liability (including the effects of changes in the credit risk of that liability) in profit or loss.

Santander Bank Polska S.A. presents in profit or loss all gains and losses on loan commitments and financial guarantee contracts that are designated as measured at fair value through profit or loss.

Assets measured at fair value through other comprehensive income

A gain or loss on a financial asset measured at fair value through other comprehensive income is recognised in other comprehensive income, except for impairment gains or losses and foreign exchange gains and losses, until the financial asset is derecognised or reclassified. If the financial asset is derecognised or reclassified out of the fair value through other comprehensive income measurement category, Santander Bank Polska S.A. accounts for the cumulative gain or loss that was previously recognised in other comprehensive income in profit or loss. Interest calculated using the effective interest method is recognised in profit or loss.

If a financial asset is measured at fair value through other comprehensive income, the amounts that are recognised in profit or loss are the same as the amounts that would have been recognised in profit or loss if the financial asset had been measured at amortised cost.

Financial instruments held for trading

A financial asset or financial liability is classified by Santander Bank Polska S.A. as held for trading if:

- it has been acquired or incurred principally for the purpose of selling or repurchasing in the near term,
- on initial recognition it is a 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; or
- it is a derivative (except for a derivative that is a financial guarantee contract or a designated and effective hedging instrument).

Derivative financial instruments are recognised at fair value without any deduction for transactions costs to be incurred on sale. 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).

If a hybrid contract contains a host contract that is not an asset within the scope of this IFRS 9, Santander Bank Polska S.A. separates the embedded derivative from the host contract and accounts for it as other derivatives 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 in the profit and loss account.

Santander Bank Polska S.A. uses derivative financial instruments to hedge its exposure to FX risk and interest rate risk arising from Santander Bank Polska S.A. operations. The derivatives that do not qualify for hedge accounting are accounted for as instruments held for trading and recognised at fair value.

Hedge accounting

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

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

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

Santander Bank Polska S.A. discontinues hedge accounting when:

(a) it is determined that a derivative is not, or has ceased to be, highly effective as a hedge;

(b) the derivative expires, or is sold, terminated, or exercised;

(c) the hedged item matures or is sold, or repaid,

(d) the hedging relationship ceases.

Fair value hedge

This is a hedge of the exposure to changes in fair value of a recognised asset or liability or an unrecognised firm commitment, or an identified portion of such an asset, liability or firm commitment, that is attributable to a particular risk and could affect the 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 rule applies if the hedged item is otherwise measured at amortised cost or is a financial asset measured at fair value through other comprehensive income.

Cash flow hedge

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

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

(b) could affect profit and losses.

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

Interest income and expenses 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, Santander Bank Polska S.A. discontinues hedge accounting. All profits or losses on the hedging instrument pertaining to the effective hedge recognised in other comprehensive income remains an element of equity until the forecast transaction occurs, when it is recognised in 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.

Repurchase and reverse repurchase transactions

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

Securities sold subject to repurchase agreements ("repo and sell-buy-back 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.

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 Santander Bank Polska S.A. 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

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

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.

Intangible assets

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 Santander Bank Polska S.A., and that will probably generate economic benefits exceeding expenditures beyond one year, are recognised as intangible assets.

Development costs

Santander Bank Polska S.A. capitalises direct costs and a justified part of indirect costs related to the design, construction and testing of a chosen alternative for new or improved processes, systems or services.

Santander Bank Polska S.A. recognises the development costs as intangible assets based on the future economic benefits and fulfilment of conditions specified in IAS 38, i.e.: Santander Bank Polska S.A.:

- has the ability and intention to complete and use the asset that is being generated,
- has the adequate technical and financial measures to complete the works and use the asset that is being generated and
- can reliably measure the amount of expenditure incurred during the development works that can be allocated to the generated intangible asset.

The economic life of development costs is definite. The amortisation rates are adjusted to the length of the economic life. Santander Bank Polska S.A. indicates separately the costs from internal development and the costs acquired through business combinations.

Development expenditure comprises all expenditure that is directly attributable to development activities.

Other intangible assets

Other intangible assets that are acquired by Santander Bank Polska S.A. 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

Fixed assets held for sale

On initial date of classification of non-current assets as assets held-for-sale, Santander Bank Polska S.A. measures them at the lower of carrying amount and fair value less cost to sell.
Any initial or subsequent write-down of assets held-for-sale to fair value less cost to sell is recognised in the income statement.

Other trade and other receivables

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

Other liabilities

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

Equity

Equity comprises capital and funds created in accordance with applicable law, acts and the Articless 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 financial assets measured at fair value through other comprehensive income and adjustments relating to the valuation of effective cash flow hedges taking into account deferred tax and actuarial gains from estimating provision for retirement. The revaluation reserve is not distributable.

On derecognition of all or part of financial assets measured at fair value through other comprehensive income the total effects of periodical change in the fair value reflected in the revaluation reserve are reversed. The value of a given financial asset measured at fair value through other comprehensive income is increased or decreased by the whole amount or an adequate portion of the impairment allowance made previously. 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 Santander Bank Polska S.A. 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 at the end of the reporting period are recognised as dividend liabilities in "other liabilities" item.

Provisions

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

Income statement

Net interest income

Santander Bank Polska S.A. presents the interest income recognised at the effective interest rate and credit-adjusted effective interest rate in separate lines of the income statement: "Interest income from financial assets measured at amortised cost" and "Interest income from assets measured at fair value through other comprehensive income".

In turn, the interest income from financial assets which do not meet the contractual cash flows test is presented in line "Income similar to interest - financial assets measured at fair value through profit or loss".

Net fee and commission income

The commission income consists mainly of revenues recognized in accordance with the 5-element revenue recognition model resulting from IFRS 15 "Revenues from contracts with customers", whose elements are described below, as well as commission income recognized in accordance with other standards (IAS 17 Leases and IFRS 9 Financial instruments.

Step 1: Identifying 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. Santander Bank Polska S.A. recognises a contract with a customer within the scope of IFRS 15 if all the following conditions are met:

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

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

In the process of identifying a contract with the customer, Santander Bank Polska S.A. takes into account both combination and modification of contracts as this may affect the method of recognising revenue from contracts with customers.

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

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

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, Santander Bank Polska S.A. continues to apply IFRS 15 to the existing contract until the contract modification is approved.

A contract modification may exist even though the parties to the contract have a dispute about the scope or price (or both) of the modification or the parties have approved a change in the scope of the contract but have not yet determined the corresponding change in price. In determining whether the rights and obligations that are created or changed by a modification are enforceable,

Santander Bank Polska S.A. considers all relevant facts and circumstances including the terms of the contract and other evidence. If the parties to a contract have approved a change in the scope of the contract but have not yet determined the corresponding change in price, Santander Bank Polska S.A. estimates the change to the transaction price arising from the modification in relation to the estimation of variable consideration and constraining estimates of variable consideration.

Step 2: Identifying 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 the asset is separately identifiable from other assets in the contract. In such a case, Santander Bank Polska S.A. is dealing with separate performance obligations.

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

- Santander Bank Polska S.A. does not provide a significant service of integrating the asset with other assets promised in the contract into a bundle of assets that represent the combined output for which the customer has contracted.
- The asset does not significantly modify or customise another asset 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, Santander Bank Polska S.A. combines that asset with other promised assets until it identifies a bundle of assets that is distinct. In some cases, that would result in Santander Bank Polska S.A. accounting for all the assets promised in a contract as a single performance obligation.

Step 3: Determining the transaction price. In accordance with IFRS 15, the transaction price is the amount of consideration that Santander Bank Polska S.A. expects to be entitled to in exchange for assets promised. It represents the amount of the revenue that will be recognised as a result of performance of the contract. In addition to the amount of consideration, the transaction price should also reflect any highly probable 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, Santander Bank Polska S.A. reviews it as at each balance sheet date.

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

Step 4: Allocating 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 unit selling prices.

Step 5: Recognising revenue at the moment of satisfying each performance obligation. 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 been transferred 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 Santander Bank Polska S.A., the indicators of the transfer of control include the following:

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

If any of the above criteria is satisfied, income is recognised over time. In other cases, income is recognised at a point in time when control is transferred.

Below is the description of key assumptions made in respect of recognition of selected fee and commission income.
Fee and commission income from loans includes fees charged by Santander Bank Polska Group in respect of reminders, certificates, guarantees, debt collection activities as well as commitment fees. Due to its nature, the majority of such income is taken to profit or loss on a one-off basis, i.e. when a specific operation is performed for a customer. Other income, such as a guarantee fee, is settled over time during the term of an agreement with a customer.
Fee and commission income from credit cards includes fees in respect of card issuance, ATM withdrawals, issuance of a new card, generation of a credit card statement or activation of optional credit card-related services. The vast majority of income is recognised at a specific point in time, i.e. when a specific operation is performed for a customer. Fees in respect of additional services related to credit cards are recognised over time.

Net income on bancassurance

For the selected loan products, where linkage to the insurance product has been identified, the Santander Bank Polska S.A. splits realised income into a portion recognised as interest income according to effective interest rate method and a portion recognised as fee income. The Santander Bank Polska S.A. 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 Santander Bank Polska S.A. separates the fair value of the financial instrument offered and the fair value of the intermediation service of insurance product sold together with such instrument. The portion that represents an element of the amortised cost of the financial instrument and the portion that represents remuneration for the agency services are split in proportion to the fair value of the financial instrument and the fair value of the agency service cost, respectively, relative to the sum of the two values.
The portion of income that is considered an agency fee for sales of an insurance product linked to a loan agreement is recognised by the Santander Bank Polska S.A. as fee income when the fee is charged for sales of an insurance product.
The Santander Bank Polska S.A. verifies the accuracy of the assumed allocation of different types of income at least annually.

Employee benefits

Short-term employee benefits

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

Long-term employee benefits

The Santander Bank Polska S.A. 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 Santander Bank Polska S.A. cannot estimate reliable the fair value of the goods or services received, the Santander Bank Polska S.A. measures their value, and the corresponding increase in equity, indirectly, by reference to the fair value of the equity instruments granted.
Vesting conditions included in the terms of the grant are not taken into account in estimating fair value except where those terms are dependent on market conditions. Non-market vesting conditions are taken into account by adjusting the number of awards included in the measurement of the cost of employee services so that ultimately, the amount recognised in the income statement reflects the number of vested awards.
The expense related to share based payments is credited to shareholder's equity. Where the share based payment arrangements give rise to the issue of new shares, the proceeds of issue of the shares are credited to share capital (nominal amount) and share premium (if any) when awards are exercised.

Cash-settled share-based payment transactions

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

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 Santander Bank Polska S.A. 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 classified to the portfolio of financial assets measured at fair value through other comprehensive income; and

- changes in the fair value of hedged and hedging instruments, including ineffective portion of cash flow hedges.
Santander Bank Polska S.A. 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 Santander Bank Polska S.A. These are primarily revenues and costs from the sale and liquidation of fixed assets, income from sale of other services, paid and received damages, penalties and fines.

Impairment losses on loans and advances

The line item "Net impairment losses on loans and advances" presents impairment losses on balance sheet and off-balance sheet exposures and the gains/losses on the sale of credit receivables.
The result on loan receivables' sale is computed at the assets' derecognition date in the difference between balance sheet amount and remuneration received.

Staff and general and administrative expenses

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

Corporate income tax

Corporate income tax comprises current and deferred tax. Income tax is recognised in income statement except to the extent that it relates to items recognised in other comprehensive income.
Current tax is the tax payable on the taxable income for the year using tax rates enacted or substantively enacted at the end of the reporting period and any adjustment to tax payable in respect of previous years.
Deferred tax assets and liabilities are provided, using the balance sheet method, on temporary differences between the tax bases of assets and liabilities and their values arising from the statement of financial position. Deferred income tax is determined using tax rates based on legislation enacted or substantively enacted at the end of the reporting period and expected to apply when the deferred tax asset is realised or the deferred tax liability is settled. Deferred tax assets are recognised at realizable amount – it is to the extent that is probable that the Santander Bank Polska S.A. generates taxable profit allowing partial or wholly realisation of deferred tax assets. The carrying value of deferred tax assets is verified at the end of each reporting period. The Santander Bank Polska S.A. reduces the carrying amount of the deferred tax asset to the realizable value - that is, to the extent that it is probable that taxable income will be sufficient to partially or fully realize the deferred tax asset.
Deferred and current tax assets and liabilities are only offset when they arise in the same tax reporting group and where there is both the legal right and the intention to settle on a net basis or to realise the asset and settle the liability simultaneously.

2.9. Accounting principles applicable until 31 December 2017

This section presents the accounting principles applied by Santander Bank Polska S.A. to comparative data related to financial instruments and revenues which are not accounted for using an effective interest method. These principles were applicable until 31 December 2017.

The accounting principles other than those mentioned below have not changed.

Financial assets and financial liabilities – classification and measurement

Classification

The Santander Bank Polska S.A. classified 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 was a financial asset or liability that met either of the following conditions:

- Classified as held for trading.
- A financial asset or financial liability was classified as held for trading if:
  - it was acquired or incurred principally for the purpose of selling or repurchasing in the near term;
  - it was part of a portfolio of identified financial instruments that were managed together and for which there was evidence of a recent actual pattern of short-term profit taking;
  - derivatives were held for trading unless the derivative was a designated and effective hedging instrument.
- Upon initial recognition it was designated by the Santander Bank Polska S.A. at fair value through profit and loss.

  In 2017, Santander Bank Polska S.A. did not have a category of financial instruments with elected measurement at fair value through profit or loss at initial recognition.

Loans and receivables

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

- those that Santander Bank Polska S.A. intended to sell immediately or in the near term, which should be classified as held for trading, and those that Santander Bank Polska S.A. upon initial recognition designated as at fair value through profit or loss;
- those that Santander Bank Polska S.A. upon initial recognition designated as available for sale;
- those for which the holder may not recover substantially all of its initial investment, other than because of credit deterioration, which should be classified as available for sale.

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

Available-for-sale financial assets

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

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

The accounting policy of Santander Bank Polska S.A. regarding:

- initial recognition of financial assets and liabilities;

- recognition of gains and losses arising from measurement at each subsequent balance sheet date;
- principles and criteria for derecognition of financial assets and liabilities from the statement of financial position;
- hedge accounting;
- measurement of financial liabilities;

has not changed as a result of implementation of IFRS 9 Financial Instruments.

Impairment of financial assets

Assets carried at amortised cost - loans and receivables

The Santander Bank Polska S.A. assessed at the end of each reporting period whether there was 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 were incurred if, and only if, there was 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) had an impact on the estimated future cash flows of the financial asset or group of financial assets that could 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, were not recognised. Objective evidence that a financial asset or group of assets was 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 Santander Bank Polska S.A., for economic or legal reasons relating to the debtor's financial difficulty, granting to the debtor a concession that the Santander Bank Polska S.A. 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 was 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 could not yet be identified with the individual financial assets, including:
 (i) adverse changes in the payment status of debtors in the Santander Bank Polska S.A., or
 (ii) national or local economic conditions that correlated with defaults on the assets in the Santander Bank Polska S.A.

If there was 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 had a variable interest rate, the discount rate for measuring any impairment loss was the current effective interest rate determined under the contract. If a floating rate financial asset or floating rate financial liability was recognised initially at an amount equal to the principal receivable or payable on maturity, re-estimating the future interest payments normally had no significant effect on the carrying amount of the asset or liability. The carrying amount of the asset should be reduced through establishing an impairment charge. The amount of the impairment charge should be recognised in profit or loss.

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

The Santander Bank Polska S.A. periodically reviewed its loan portfolio to check whether there was any objective evidence that a financial asset or group of financial assets were impaired.

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

Impairment of individual loan exposures was 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 selected the strategy that reflected the current recovery method. Within each strategy, consideration was given to other possible scenarios. The selected strategy affected the limitations of other parameters' value that could be used in the model. In the individual approach, the impairment charge was 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 were 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 were 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 Santander Bank Polska S.A. determined that no objective evidence of impairment existed for an individually assessed financial asset, whether significant or not, it included the asset in a group of financial assets with similar credit risk characteristics and collectively assessed them for impairment. Assets that were individually assessed for impairment and for which an impairment loss was or continued to be recognised by the Santander Bank Polska S.A. were not included in a collective assessment of impairment.

For the purpose of the collective evaluation of impairment, financial assets were grouped on the basis of similar credit risk characteristics that were indicative of the debtors' ability to pay all amounts due according to the contractual terms (for example, on the basis of the Santander Bank Polska S.A. credit risk evaluation or the Santander Bank Polska S.A. grading process that considered asset type, industry, geographical location, collateral type, past-due status and other relevant factors). The characteristics chosen were 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 were 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 were collectively evaluated for impairment were 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 was 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 was based and to remove the effects of conditions in the historical period that did not exist currently.

Estimates of changes in future cash flows reflected and were 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 were indicative of impairment charges in the group and their magnitude). The Santander Bank Polska S.A. reviews regularly the methodology and assumptions used for estimating future cash flows in order to reduce any differences between estimates and actual impairment charge experience.

IBNR (Incurred But Not Reported) impairment charges were also maintained to cover loans, which were 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 were maintained at levels that were 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) took into account the following key factors:

- EP - Emergence Period i.e. time between the occurrence of event of default and its identification by Santander Bank Polska S.A.;
- PD - Probability of Default, based on historical observations together with EP was considered to be best indicator of incurred but not reported losses;

- LGD - Loss Given Default i.e. the fraction of the exposure amount that would 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 were 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 was related objectively to an event occurring after the impairment was recognised, the previously recognised impairment charge was reversed either directly or by adjusting the impairment charge. The reversal should not result in a carrying amount of the financial asset that exceeded what the amortised cost would have been had the impairment not been recognised at the date the impairment was reversed.
The amount of the reversal was recognised in income statement.
When a loan has been subject to a specific provision and the prospects of recovery did not improve, eventually it may be concluded that there was no real prospect of recovery. When this point was reached, the amount of the loan which was considered to be non-recoverable was written off against the related impairment charge for loan. Subsequent recoveries of amounts previously written off decreased the amount of the charge for loan impairment in the income statement.

Available-for-sale financial assets

For financial assets classified as available-for-sale for which there was objective evidence that the asset was impaired, the cumulative impairment charge that had been recognised directly in other comprehensive income should be removed and recognised in income statement. The amount of the cumulative impairment charge that was removed from other comprehensive income and recognised in income statement should 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 increased and the increase could be objectively related to an event occurring after the impairment loss was recognised, the impairment loss should be reversed, with the amount of the reversal recognised in income statement.
If there was objective evidence that an impairment loss has been incurred on an unquoted equity instrument that was not carried at fair value because its fair value could not be reliably measured, the amount of the impairment loss was 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 were not reversed through income statement.

Contingent liabilities

Santander Bank Polska S.A. created 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.

Net interest income

Interest income from a financial asset was recognised when it is probable that the economic benefits will flow to the Santander Bank Polska S.A. and the amount of income could be measured reliably.
Interest income and expenses for all financial instruments was recognised in the income statement at amortised cost using the effective interest rate method.
In case impairment was recognised for a financial asset, interest income was 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 on overdrafts, revolving loans, credit cards and off balance sheet liabilities were recognised on a straight-line basis in the income statement.

Other fees and charges, which are not settled according to the effective interest rate, were included in income statement in accordance with accrual method.

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

3. Risk management

Santander Bank Polska SA is exposed to a variety of risks in its ordinary business activities. The objective of risk management is to ensure that the Bank takes risk in a responsible and controlled manner when maximising the value for shareholders. Risk is a possibility of materialisation of events impacting the achievement of the Bank's strategic goals.

Risk management policies are designed to identify and measure risk, define the most profitable return within the accepted risk level (risk-reward), and to continually set appropriate risk mitigation limits. Santander Bank Polska SA modifies and develops risk management methods on an ongoing basis, taking into consideration changes in the Bank's risk profile, economic environment, regulatory requirements and best market practice.

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

The **Supervisory Board** continuously oversees the risk management system. The Supervisory Board approves the strategy, key risk management policies and risk appetite, and monitors the use of 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 remedial actions. The Supervisory Board assesses if the control activities performed by the Management Board are effective and aligned with the Supervisory Board's policy. The assessment also includes the risk management system.

The **Audit and Compliance Committee** supports the Supervisory Board in fulfilment of its oversight obligations. The Committee performs annual reviews of the Bank's financial controls, and receives reports from the independent audit function and the compliance function. The Committee also receives quarterly reports on the degree of implementation of post-audit recommendations, and on that basis evaluates the quality of the actions taken. The Committee assesses the effectiveness of internal control system and risk management system. Moreover, the Committee monitors financial audits, in particular inspections carried out by the audit company, controls, monitors and assesses independence of the chartered auditor and audit company, and reports the outcomes of inspections to the Supervisory Board. In addition, the Committee develops the policy and procedure for selecting the audit company and presents to the Supervisory Board the recommendations on election, re-election and recalling of External Auditor and on the External Auditor's fee.

The **Risk Committee** supports the Supervisory Board in assessing the effectiveness of the internal control and risk management systems and measures adopted and planned to ensure an effective management of material risks.

Moreover, the Supervisory Board is also supported by the **Remuneration Committee** and the **Nominations Committee**, however outside the risk management area.

The **Management Board** is responsible for the effectiveness of risk management. In particular, it 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, implements and updates the written risk management strategies, and ensures transparency of the activities. The Management Board reviews the financial results of the Bank. It established a number of committees which are 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, where the Management Board members are supported by key risk management officers.

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

The **Risk Control Committee** monitors the risk level across different areas of the bank's operations and supervises the activities of lower-level risk management committees set up by the Management Board. These committees, acting within the respective remits defined by the Management Board, are directly responsible for developing risk management methods and monitoring risk levels in specific areas.

The Risk Control Committee supervises the activities of the below-listed committees operating in the risk management field:

The **Risk Management Forum**, which approves and supervises risk management policy and risk measurement methodology as well as monitors credit risk, market risk on the banking book, market risk on the trading book, structural risk for the balance sheet and liquidity risk. The Forum operates through four panels:

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

The **Credit Committee** takes credit decisions within the assigned lending discretions.

The **Provisions Committee** takes decisions on impairment charges in an individual and collective approach, for credit exposures, as well as other financial instruments and assets and on legal risk provisions. Moreover, the Committee formulates the methodology, reviews the adequacy of parameters applied when setting the impairment in an individual and collective approach for Santander Bank Polska SA, excluding Santander Consumer Bank S.A.

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

The **Cyber Risk Committee** 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.

The **Operational Risk Management Committee (ORMCo)** sets the direction for strategic operational risk actions in Santander Bank Polska SA in the area of business continuity, information security and fraud prevention.

The **Assets and Liabilities Management Committee** supervises the activity on the bank's and the Group's banking book, manages liquidity and interest rate risk in the banking book and is responsible for the funding and balance sheet management, including for the pricing policy and the currency structure.

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

The **Disclosure Committee** verifies if the financial information published by Santander Bank Polska SA meets the legal and regulatory requirements.

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

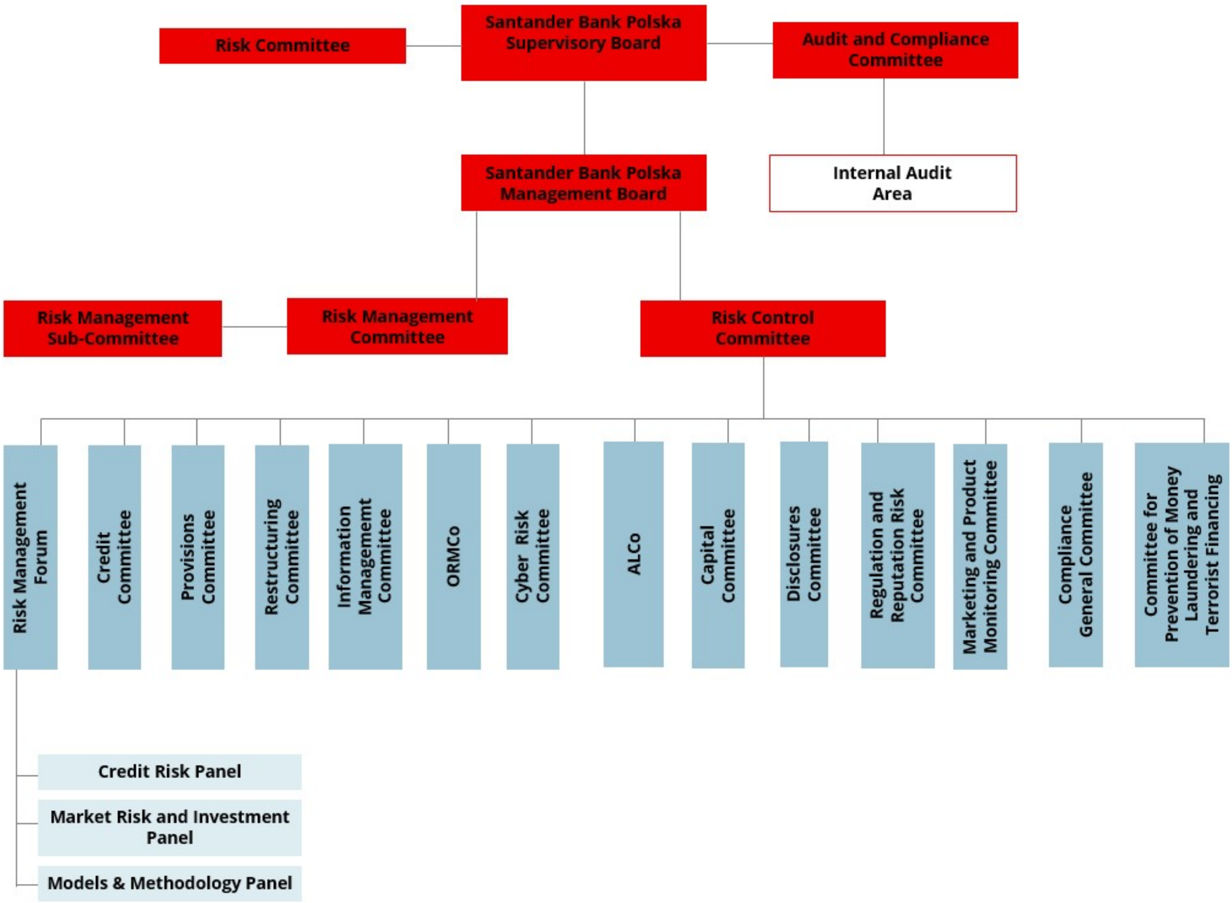
The **General Compliance Committee** is responsible for setting standards with respect to the management of compliance risk and the codes of conduct adopted by the Bank.

The **Regulatory and Reputational Risk Committee** is responsible for monitoring and taking decisions on cases relating to the Bank's compliance with law, regulatory guidelines and market/ industry standards relating to the Bank's operations.

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

The **Recovery Committee** takes decisions as to the dealing with borrowers in distress, including with respect to the relationship management strategy, approval of the causes of loss analysis and monitoring of the portfolio and effectiveness of recovery processes.

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



Risk management is in line with the “Risk Management Strategy” adopted by the bank’s Management Board and approved by the Supervisory Board. An important part of strategic risk management is defining the bank’s risk appetite. At Santander Bank Polska SA, risk appetite is expressed as quantitative limits and captured in the “Risk Appetite Statement” adopted by the Management Board and approved by the Supervisory Board. Global limits are used to set watch limits and shape risk management policies.

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

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

The key rules, roles and responsibilities of the Bank companies are set out in relevant internal policies relating to the management of individual risk types.

Santander Bank Polska SA pays special attention to the consistency of risk management processes across the Bank, which ensures adequate control of the risk exposure. The subsidiaries implement risk management policies and procedures reflecting the principles adopted by Santander Bank Polska SA.

Acting under the applicable law, the bank exercises oversight of risk management in Santander Consumer Bank S.A. in line with the same oversight rules as applied to other Santander Bank Polska SA companies. Th bank's representatives on the Supervisory Board of Santander Consumer Bank S.A. are: the Management Board member in charge of the Risk Management Division and the Management Board member in charge of the Retail Banking Division. Pursuant to the "Santander Bank Polska S.A. strategy of investments in capital market instruments", they are responsible for supervision over Santander Consumer Bank S.A. and they ensure, together with the company's Supervisory Board, that the company operates in line with adopted plans and operational security procedures. The bank monitors the profile and level of Santander Consumer Bank S.A. risk via risk management committees of Santander Bank Polska S.A.

Credit risk

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

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

The Bank 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 Bank is closely looking at the macroeconomic environment and analysing its credit exposure to particular customer segments and economic sectors to respond with an adequate and prompt action and adjust its credit policy parameters accordingly.

The year 2018 was quite stable in this respect, and the introduced changes modified the policy only moderately, mainly optimising and harmonising the existing elements of the credit process as well as reflecting changes arising from new regulations. The key regulation affecting the measurement of credit risk was the entry into force of IFRS 9 as of 1 January 2018. In 2017, the Bank completed a number of key adaptation initiatives concerning the process of classification and measurement of financial instruments. The output of these initiatives was implemented early in 2018. During 2018, no significant changes were made in these processes, other than those connected with ongoing monitoring and calibration of parameters for the purpose of measurement of financial instruments.

In the context of the credit policy, the main challenge was to adapt it to the acquired portfolio of Deutsche Bank Polska S.A. To achieve the strategic objectives related to this transaction, the Bank modified its credit policy primarily with regard to the segments of affluent customers and freelancers to reflect the profile of the customers from the portfolio acquired from Deutsche Bank Polska S.A. The Bank will continue this work also in 2019. In 2018, the Bank improved its credit exposure monitoring tools to ensure faster identification of potential threats both at the portfolio level and at the level of individual exposures. At the same time, the Bank modified its monitoring strategies, focusing on early measures designed to limit the effects of potential risk materialisation.

One of the Bank's priorities in 2018 was close monitoring of foreign currency housing loan portfolio. In response to the numerous legislative proposals the Bank conducted multivariate analyzes and actively participated in the consultation processes. The Bank pays particular attention to credit risk on these portfolios.

Risk Management Forum

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

Risk Management Division

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

Credit Policies

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

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

Credit Decision Making Process

The credit decision-making process as a part of the risk management policy is based upon Individual Credit Discretions vested in credit officers, commensurate with their knowledge and experience within the business segments. Credit exposures in excess of PLN 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 Santander Bank Polska SA 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.

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

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

Credit Reviews

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

Collateral

In the Bank's security model, the Collateral and Credit Agreements Department is the central unit responsible for creation and maintenance of 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/ receivable	Type of collateral
Cash loan	bills, guarantees, credit insurance
Credit on liquid assets	guaranty deposit, amounts frozen on account, investment funds
Student loan	sureties
Housing loan	mortgage, credit insurance, transfer of claim
Leasing	bills, guarantees, transfer of rights to bank's account; court registered pledge on movables; transfer of ownership, open mortgage, obligation of the leased asset supplier to buy the asset back (buy-back guarantee)

Business customers

Type of loan/ receivable	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, Santander Bank Polska SA 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 Bank aims at voluntary proceedings in the course of collateral execution. When there is no evidence of cooperation with a collateral provider, the Bank'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 Santander Bank Polska as at 31.12.2018:

In thousands of PLN

Financial effect of collateral		Gross Amount	Financial effect of collateral
Loans and advances to customers			
	housing loans	45 927 616	(230 296)
	business	58 823 206	(936 791)
Total balance sheet		**104 750 822**	**(1 167 087)**
Total off-balance sheet		**22 866 807**	**(15 090)**

The table below present financial effect of collateral of Santander Bank Polska as at 31.12.2017:

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

Credit risk stress testing

Stress testing is 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 Santander Bank Polska SA 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.

Impairment calculation

Santander Bank Polska SA posts impairment allowances in accordance with International Financial Reporting Standard 9 (IFRS 9), as it replaced International Accounting Standard 39 (IAS 39), which ceased to apply at the end of 2017. IFRS 9 introduced a new approach to the estimation of allowances for credit losses. The approach is based on estimation of the expected credit loss (ECL), in contrast to the previous IAS 39 model, which was based on the concept of incurred loss. ECL allowances reflect an unbiased and probability-weighted amount that is determined by evaluating a range of possible outcomes, the time value of money; and reasonable and supportable information that is available without undue cost or effort at the reporting date about past events, current conditions and forecasts of future economic conditions. ECL allowances are measured at an amount equal to a 12-month ECL or the lifetime ECL, when it is deemed there has been a significant increase in credit risk since initial recognition. Accordingly, the ECL model gives rise to measurement uncertainty, especially in relation to:

- measurement of a 12-month ECL or the lifetime ECL;
- determination of when a significant increase in credit risk occurred;
- determination of any forward-looking events reflected in ECL estimation, and their likelihood.

In accordance with IFRS 9, the recognition of expected credit losses will depend on changes in risk after recognition of the exposure. The standard introduces 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 will be 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 will be recognised.
- Stage 3: exposures for which the risk of default has materialised (indications of impairment have been identified). For such exposures, lifetime expected credit losses will be recognised.

Lifetime expected losses are recognised also for the exposures classified as POCI (purchased or originated credit-impaired).

In the case of classification into stage 3, the Bank applies objective indications of impairment, as defined in accordance with the Basel Committee's recommendations and Recommendation R. The Bank did not introduce any material changes in this respect.

In thousands of PLN

The Bank estimates ECL using using both an individual approach (for individually significant exposures with objectively evidenced impairment [stage 3]) and collective approach (individually insignificant exposures with objectively evidenced impairment, and incurred but not reported losses).

Twice a year, the Bank recalibrates its models and updates the forward-looking information used for estimating ECL, taking into account the impact of changes in economic conditions, modifications of the Bank's credit policies and recovery strategies, which is designed to ensure appropriate level of impairment allowances.

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

Loans and advances to customers measured at amortised cost

31.12.2018	Provision cover	individuals	housing loans	business	Total
impaired portfolio					
Exposures classified to Stage 3- Individually assesed					
	up to 50%	-	-	1 124 640	
	50% - 70%	-	-	318 502	
	70% - 85%	-	-	76 541	
	over 85%	-	-	428 188	
Gross amount		-	-	**1 947 871**	**1 947 871**
Impairment					(716 772)
Net amount					**1 231 099**
Exposures classified to Stage 3-Collectivelly assesed					
	up to 50%	108 533	142 484	167 323	
	50% - 70%	97 698	106 473	69 037	
	70% - 85%	4 503	27 290	71 348	
	over 85%	429 341	187 763	793 102	
Gross amount		**640 075**	**464 010**	**1 100 810**	**2 204 895**
Impairment					(1 346 730)
Net amount					**858 165**
Exposures classified to Stage 2					
	up to 0.10%	868	1 798	237 424	
	0.10%-0.30%	3 923	12 377	141 419	
	0.30%-0.65%	10 468	49 363	161 706	
	over 0.65%	468 048	782 242	1 560 497	
Gross amount		**483 308**	**845 780**	**2 101 045**	**3 430 133**
Impairment					(264 130)
Net amount					**3 166 003**
Exposures classified to Stage 1					
	up to 0.10%	1 275 875	40 729 643	29 516 472	
	0.10%-0.30%	3 471 309	1 131 936	10 867 316	
	0.30%-0.65%	3 757 587	1 774 797	5 700 870	
	over 0.65%	3 953 532	770 042	7 518 903	
Gross amount		**12 458 303**	**44 406 418**	**53 603 561**	**110 468 282**
Impairment					(362 453)
Net amount					**110 105 829**
Exposures classified as purchased or created items of financial assets that are impaired at the time of origination due to credit risk (POCI)					
Gross amount		**107 831**	**215 384**	**405 205**	**728 420**
Impairment					(32 917)
Net amount					**695 503**
					-
Loans and advances to customers measured at amortised cost					**116 056 599**

In thousands of PLN

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

Credit quality step *	Loans and advances to banks	Loans and advances to customers - Debt securities measured at amortised cost	Loans and advances to customers - Debt securities measured at fair value through profit or loss	Debt securities measured at fair value through other comprehensive income	Debt securities measured at fair value through profit or loss	Financial assets held for trading - debt securities
1 (AAA to AA-)	528 888	-	-	235 685	-	-
2 (A+ to A-)	1 873 359	-	-	35 176 881	131 005	8 667 540
3 (BBB+ to BBB-)	335 608	923 855	-	-	-	3 232
4 (BB+ to BB-)	1 582	-	-	-	-	-
5 (B+ to B-)	1 406	-	-	-	-	-
6 (<B-)	-	-	-	-	-	-
none	118 636	324 895	106 374	27 270	-	951
Total	**2 859 479**	**1 248 750**	**106 374**	**35 439 836**	**131 005**	**8 671 723**

* according to Fitch

Loans and advances to banks are assessed using ratings. The assessment method was set out in the Bank's internal regulations. Each institutional client (exposure) is assigned a rating by one of the reputable rating agencies (Fitch, 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.

Financial instruments from the investment securities measured at fair value 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] debt instruments 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-.

For all instruments presented above (including also loans and advances to customers measured at fair value through other comprehensive income), there is no overdue or impairment, therefore they are classified to Stage 1.

The significant majority of 'other assets' items are non-past due and unimpaired.

Credit risk concentration

Santander Bank Polska SA 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 31.12.2018, pursuant to art. 71 of the Banking Law Act, the maximum limits for the Bank amounted to:

- PLN 5,188,801 k (25% of Bank's own funds).

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

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

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

The analysis of the Bank's exposures in terms of sector concentrations, proved that the Bank does not have any exposures in excess of the limits imposed by the regulator in 2018.

In thousands of PLN

A list of the 20 largest borrowers (or capital-related group of borrowers) of Santander Bank Polska SA (performing loans) as at 31.12.2018.

Industry code (PKD)	Industry description	Total credit exposure	Balance sheet exposure	Committed credit lines, guarantees, treasury limits and capital investments
64	OTHER FINANCIAL SERVICES	7 219 681	5 138 988	2 080 693
64	OTHER FINANCIAL SERVICES	6 823 000	3 982 897	2 840 103
64	OTHER FINANCIAL SERVICES	3 930 626	316 557	3 614 069
61	TELECOMMUNICATION	1 716 665	1 553 263	163 402
35	POWER INDUSTRY	1 490 000	106 364	1 383 636
68	REAL ESTATE SERVICES	1 088 532	986 831	101 701
46	WHOLESALE	984 490	760 018	224 472
06	MINING	960 461	186 108	774 353
06	MINING	828 520	253 495	575 025
35	POWER INDUSTRY	810 000	210 500	599 500
61	TELECOMMUNICATION	683 281	551 281	132 000
19	RAFINERY	671 031	150 500	520 531
35	POWER INDUSTRY	619 795	581 781	38 014
41	CONSTRUCTION	602 003	531 698	70 305
41	CONSTRUCTION	539 000	-	539 000
35	POWER INDUSTRY	529 371	458 971	70 400
19	RAFINERY	397 095	397 095	-
64	OTHER FINANCIAL SERVICES	369 972	299 972	70 000
68	REAL ESTATE SERVICES	367 194	354 509	12 685
68	REAL ESTATE SERVICES	360 005	343 733	16 272
Total gross exposure		**30 990 722**	**17 164 561**	**13 826 161**

In thousands of PLN

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

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

Industry concentration

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

As at 31.12.2018, the highest concentration level was recorded in the “distribution” sector (11% of the Santander Bank Polska SA exposure), “manufacturing” (10%) and “property” (9%).

In thousands of PLN

Groups of PKD by industries:

	Industry	Gross exposure 31.12.2018	Gross exposure 31.12.2017
	Distribution	13 253 443	11 206 089
	Manufacturing	11 655 525	8 282 887
	Financial sector	10 484 251	9 979 473
	Property	9 659 412	7 832 541
	Energy	2 179 265	2 510 916
	Transportation	1 788 775	1 373 327
	Agriculture	1 317 813	1 218 554
	Construction	1 258 559	1 040 444
	Other industries	6 997 236	5 421 923
A	**Total Business Loans**	**58 594 279**	**48 866 154**
B	**Retail (including mortgage loans)**	**60 173 805**	**44 695 670**
A+B	**Santander Bank Polska SA portfolio**	**118 768 084**	**93 561 824**
C	**Other receivables (commercial bonds)**	**11 517**	**7 304**
A+B+C	**Total Santander Bank Polska SA**	**118 779 601**	**93 569 128**

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 Santander Bank Polska SA 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 nonperforming assets in the Bank, that is loans and receivables are measured at amortised cost using the effective interest method. If the terms of a loan, receivable or held-to-maturity investment are renegotiated or otherwise modified because of financial difficulties of the borrower or issuer, the exposure is measured using the original effective interest rate before the modification of terms (in accordance with IAS 39 AG 84).

In thousands of PLN

		Book value	
		31.12.2018	31.12.2017
Loans and advances to customers- gross amount			
under forebearance measure:		**2 936 302**	**3 081 530**
	corporate exposures	2 004 097	1 959 502
	mortgage exposures	584 155	946 212
	individuals exposures	348 050	175 816
Allowance for impairment - forbearance clients		**(857 596)**	**(651 099)**
of which:	individually impaired	(412 796)	(413 055)
Loans and advances to forebearance clients- net amount		**2 078 706**	**2 430 431**

Analysis of credit quality of financial assets subject to forbearance:

Loans and advances to customers under forebearance	Gross exposure		Collateral value		Allowance for impairment	
	31.12.2018	31.12.2017	31.12.2018	31.12.2017	31.12.2018	31.12.2017
Loans and advances -impaired	**1 981 742**	**1 568 024**	**9 364 984**	**9 064 413**	**(743 709)**	**(612 227)**
Loans and advances -unimpaired	**954 560**	**1 513 506**	**3 411 569**	**2 789 490**	**(113 887)**	**(38 872)**
non-overdue	756 817	1 196 468	3 129 973	2 281 523	(97 980)	(25 663)
from 1 to 30 days overdue	115 223	227 848	149 043	381 650	(6 873)	(10 685)
from 31 to 60 days overdue	57 507	61 403	100 349	89 545	(5 304)	(1 619)
from 61 to 90 days overdue	25 013	27 787	32 204	36 772	(3 730)	(905)
Total gross amount	**2 936 302**	**3 081 530**	**12 776 553**	**11 853 903**	**(857 596)**	**(651 099)**

Interest income on assets subject to forbearance was PLN 65,512 k as at 31 December 2018 and PLN 69,601 k as at 31 December 2017.

Loans and advances to customers under forbearance by geographical region	31.12.2018	31.12.2017
Dolnośląskie	344 853	317 404
Kujawsko-Pomorskie	142 021	43 223
Lubelskie	32 834	30 685
Lubuskie	41 392	40 316
Mazowieckie	975 437	1 317 268
Małopolskie	125 909	195 950
Opolskie	31 198	23 716
Podkarpackie	38 044	21 918
Podlaskie	41 386	34 566
Pomorskie	175 465	155 802
Warmińsko-Mazurskie	33 560	28 335
Wielkopolskie	202 677	155 554
Zachodniopomorskie	80 605	58 649
Śląskie	592 051	529 202
Świętokrzyskie	22 913	70 008
Łódzkie	55 957	58 934
Total	**2 936 302**	**3 081 530**

In thousands of PLN

Loans and advances to customers under forbearance by industry (gross amount)	31.12.2018	31.12.2017
Construction	318 947	224 891
Distribution	184 092	82 793
Energy	475 310	398 913
Financial sector	2 300	557
Other industries	180 197	179 333
Property	541 962	799 621
Manufacturing	232 664	169 215
Agriculture	26 344	69 065
Transportation	42 281	35 114
Individuals	932 205	1 122 028
Total	**2 936 302**	**3 081 530**

	31.12.2018	31.12.2017
Net carrying amount as at beginning of the period	**2 430 431**	**2 887 385**
Allowance for impairment	(206 497)	82 296
Loans and advances derecognised during the period	(1 170 904)	(144 515)
Loans and advances recognised during the period	1 147 687	1 135 017
Other changes/repayments	(122 011)	(1 529 752)
Net carrying amount as at the end of the period	**2 078 706**	**2 430 431**

Market risk

Introduction

Market risk is defined as an adverse earnings impact of changes in interest rates, FX rates, share quotations, stock exchange indices, etc. It arises both in trading and banking activity (FX products, interest rate products, equity linked trackers).

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

The activity and strategies on market risk management are directly supervised by the Risk Management Forum and are pursued in accordance with the framework set out in the Market Risk Policy and the Structural Risk Policy approved by the Management Board and the Supervisory Board.

Risk management structure and organisation

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

The market risk policies of Santander Bank Polska SA establish a number of risk measurement and mitigation parameters in the form of limits and metrics. Risk limits are periodically reviewed to align them with the Bank's strategy.

Interest rate and FX risks linked to the banking business are 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 by the Risk Management Forum, the bank's Management Board and the Supervisory Board.

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

The market risk on the trading portfolio is managed by the Corporate and Investment Banking Department, which is also responsible for the activities of Santander Brokerage Poland. The Bank's trading activity is subject to a system of measures and limits, including Value at Risk, stop loss, position limits and sensitivity limits. 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 risk measurement, implementation of control procedures and risk monitoring and reporting. The Department is also responsible for shaping the market risk policy, proposing risk measurement methodologies and ensuring consistency of the risk management process across the Bank. Owing to the fact that the Department is a part of the Risk Management Division, the risk measurement and monitoring processes are separate from the risk-taking units.

The market risk of equity instruments held by Santander Brokerage Poland (shares, index-linked securities) is managed by Santander Brokerage Poland itself and supervised by the Risk Management Forum of Santander Bank Polska S.A.

The bank's Risk Management Forum, chaired by the Management Board member in charge of the Risk Management Division, is responsible for independent control and monitoring of market risk in the banking and trading books.

Risk identification and measurement

The trading book of Santander Bank Polska SA contains securities and derivatives held by the Corporate and Investment 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. Market risk in the trading book includes interest rate risk, currency risk and repricing risk.

The interest rate risk in the Bank's banking book is the risk of adverse impact of interest rate changes on the Bank's income and the value of its assets and liabilities. Interest rate risk arises primarily on transactions entered in the bank's branches and in the business and corporate centres, as well as the transactions made in the wholesale 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 other sources than the interbank market.

Santander Bank Polska SA uses several methods to measure its market risk exposure. The methods employed for the banking portfolio are the MVE and NII sensitivity measures, stress tests and Value at Risk (VaR), while the methods used for the trading portfolio include: VaR, stop loss, sensitivity measures (PV01) and stress tests. The risk measurement 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).

At Santander Bank Polska SA, the VaR in the trading portfolio is determined using a historical method 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 two risks at the same time. VaR is also calculated for the repricing risk of the equity instruments portfolio of Santander Brokerage Poland.

Due to the limitations of the VaR methodology, the Bank additionally performs sensitivity measurement (showing how position values change in reaction to price/profitability movements), Stressed VaR measurement and stress tests.

Risk reporting

The responsibility for reporting market risk rests with the Risk Management Division, specifically the Financial Risk Department.

Each day, the Financial Risk Department controls the market risk exposure of the trading book in accordance with the methodology laid down in the Market Risk Policy. It verifies the use of risk limits and reports risk levels to units responsible for risk management in the trading book, to Santander Group and to the Risk Management Forum.

Once a month, the Financial Risk Department provides information about the risk exposure of the trading book and selected measures to the Risk Management Forum and prepares the Risk Dashboard (in cooperation with other units of the Risk Management Division), which is presented to the Risk Management Committee.

The results of market risk measurement with regard to the banking book are reported by the Financial Risk Department to persons responsible for operational management of the bank's balance sheet structure and to persons in charge of structural risk management on a daily basis (information about the ALCO portfolio) or on a monthly basis (interest rate gap, NII and MVE sensitivity measures, stress test results, VaR). This information is also reported each month to the bank's senior executives (Risk Management Forum, ALCO). The selected key interest rate risk measures, including risk appetite measures defined for the Group's banking book, are reported to the bank's Management Board and Supervisory Board.

Risk prevention and mitigation

The bank has adopted a conservative approach to risk-taking both in terms of the size of exposures and the types of products. A large portion of the Financial Market Area activity revolves around mitigating the risk related to customer transactions at the retail and corporate level. In addition, flows from customer transactions are generally for non-market amounts and tenors and thus risk capacity is required to manage these mismatches with wholesale transactions.

In thousands of PLN

From the bank's perspective, the market risk limits are small and are in place to allow sufficient capacity and time to neutralise interest rate and foreign exchange risks, while at the same time allowing the Financial Market Area to hold some of portfolio positions opened to add value to the organisation.

There is a greater emphasis placed on market making over pure mark to market trading and this is reflected in both limit utilisation and budgetary targets.

The combination of transactions made by the Financial Market Area and positions transferred from the bank arising from customers' FX and derivative activity create the overall interest rate and currency risk profiles, which are managed under the policy and operational limits in place. The Financial Market Area subsequently decides either to close these positions or keep them open in line with market view and approved limits. The return earned is a mix of flow management and market making. However, there is no intention to keep aggressive trading positions.

The interest rate and currency risk of the Financial Market Area is managed via the trading book in accordance with the Market Risk Policy approved by the Management Board. Accounting and risk systems help to ensure allocation of each position into appropriate books. The relevant desks are responsible for suitable risk activity (interest rate or currency risk).

To ensure that the trading book positions are marketable, the bank controls the gross value of the positions (separately long and short positions) versus the entire market. This is to check if it is technically possible to close an open position one way, without taking into account other closings. The control is performed by the Financial Risk Department separately for currency positions and interest rate positions. The control results are reported to the first line of defence.

As regards market risk in the banking book, all positions that generate repricing risk are transferred for management to the Financial Management Division, responsible for shaping the bank's balance sheet structure, including by entering into transactions in the interbank market so as to manage the 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 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 Santander Bank Polska SA.

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

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

The sensitivity measures for 2018 and 2017 are shown 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.

	NII Sensitivity		MVE Sensitivity	
1 day holding period	**31.12.2018**	**31.12.2017**	**31.12.2018**	**31.12.2017**
Maximum	273	238	375	377
Average	224	211	316	267
as at the end of the period	273	238	298	347
Limit	**300**	**310**	**400**	**380**

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).

The key methods of measurement of the interest rate risk in the trading book include the VaR methodology, stop loss, PV01 sensitivity measurement and stress tests.

The VaR is set for open positions of the Corporate and Investment Banking Division using the historical simulations method. Under this method the bank estimates the portfolio value of 520 scenarios generated on the basis of historically observable changes in market parameters. VaR is then estimated as the difference between the current valuation and the valuation of the 99th percentile of the lowest valuations.

The stop-loss mechanism is used to manage the risk of loss on positions subject to fair value measurement through profit or loss.

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

In thousands of PLN

The table below shows risk measures at the end of 2018 and 2017 for 1-day position holding period:

Interest rate risk	VAR	
1 day holding period	**31.12.2018**	**31.12.2017**
Average	1 702	1 559
Maximum	5 966	4 777
Minimum	523	373
as at the end of the period	1 508	839
Limit	**6 767**	**6 266**

In 2018, the VaR limit for interest rate risk was not exceeded.

FX risk is the risk that adverse movements in foreign exchange rates will have an impact on performance (and result in losses). This risk is managed on the basis of the VaR limit for the open currency positions in the Bank's trading portfolio and the portfolio of Santander Brokerage Poland which manages 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 trading positions.

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

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

The table below illustrates the risk measures at the end of December 2018 and 2017.

FX risk	VAR	
1 day holding period	**31.12.2018**	**31.12.2017**
Average	473	414
Maximum	1 939	1 725
Minimum	53	50
as at the end of the period	150	175
Limit	**2 820**	**2 611**

In 2018, the VaR limit for currency risk was not exceeded.

As regards the structural exposure to currency risk in the Bank's balance sheet, in 2018 the share of foreign currency assets in the bank's balance sheet continued to decrease. This was affected by the substantial increase in PLN loans and advances to customers, including as a result of acquisition of a demerged part of Deutsche Bank Polska S.A. and the gradual decrease in the balance of CHF loans as a result of the continuing amortisation of the CHF mortgage portfolio.

The resulting funding gap relating to individual currencies was closed by entering into swap transactions in the FX market.

The tables below present the Bank's key FX positions as at 31 December 2018 and in the comparable period.

31.12.2018	PLN	EUR	CHF	USD	Other	Total
ASSETS						
Cash and balances with central banl	8 291 811	356 753	25 593	77 185	90 560	8 841 902
Loans and advances to banks	396 844	1 514 213	6 225	686 402	255 795	2 859 479
Loans and advances to customers	91 546 461	16 482 852	8 233 865	1 211 893	17 419	117 492 490
Investment securities	34 147 558	1 468 753	-	755 802	-	36 372 113
Selected assets	**134 382 674**	**19 822 571**	**8 265 683**	**2 731 282**	**363 774**	**165 565 984**
LIABILITIES						
Deposits from banks	787 130	217 536	13 677	17 491	4 145	1 039 979
Deposits from customers	117 447 983	15 543 186	402 317	4 617 741	1 458 549	139 469 776
Subordinated liabilities	1 008 173	1 535 767	-	-	-	2 543 940
Selected liabilities	**119 243 286**	**17 296 489**	**415 994**	**4 635 232**	**1 462 694**	**143 053 695**

In thousands of PLN

31.12.2017	PLN	EUR	CHF	USD	Other	Total
ASSETS						
Cash and balances with central banl	3 646 691	316 341	16 408	74 683	60 678	4 114 801
Loans and advances to banks	244 786	1 293 502	2 738	315 221	155 871	2 012 118
Loans and advances to customers	67 445 351	13 898 367	8 414 097	643 975	135 213	90 537 003
Investment securities	24 534 492	803 778	-	445 759	-	25 784 029
Selected assets	**95 871 320**	**16 311 988**	**8 433 243**	**1 479 638**	**351 762**	**122 447 951**
LIABILITIES						
Deposits from banks	301 469	1 061 276	5 103	37 292	9 308	1 414 448
Deposits from customers	82 989 622	13 629 198	342 796	4 101 665	1 092 242	102 155 523
Subordinated liabilities	-	1 488 602	-	-	-	1 488 602
Selected liabilities	**83 291 091**	**16 179 076**	**347 899**	**4 138 957**	**1 101 550**	**105 058 573**

The risk attached to the prices of equity instruments listed in active markets is managed by Santander Brokerage Poland, which operates within the Corporate and Investment Banking Division. This risk is generated by own trades of Santander Brokerage Poland concluded in regulated markets (spot market instruments and futures).

It is measured using a Value at Risk model based on the historical analysis method.

The market risk management in Santander Brokerage Poland is supervised by the Risk Management Forum of Santander Bank Polska S.A. The Forum sets the VaR limit for Santander Brokerage Poland, approves changes in the risk measurement methodology and oversees the risk management process.

The table below presents the risk measures in 2018 and 2017.

Equity risk	VAR	
1 day holding period	**31.12.2018**	**31.12.2017**
Average	208	304
Maximum	584	694
Minimum	5	46
as at end of the period	106	90
Limit	**3 760**	**3 621**

In 2018, the VaR limit for equity risk was not exceeded.

Liquidity risk

Introduction

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.

The activity and strategies on liquidity risk management are directly supervised by the Risk Management Forum and are pursued in accordance with the framework set out in the Liquidity Risk Policy approved by the Management Board and the Supervisory Board.

Risk management structure and organisation

The objective of the Liquidity Risk Policy of Santander Bank Polska SA is 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, including the intraday mismatch of cash flows;
- set a scale of the liquidity risk in the form of various internal limits;
- ensure proper organisation of the liquidity management process within the whole Santander Bank Polska SA;
- prepare the organisation for emergence of adverse factors, either external or internal;
- ensure compliance with regulatory requirements, both qualitative and quantitative.

The general principle adopted by Santander Bank Polska SA in its liquidity management process is that all expected outflows occurring within one month in respect of deposits, current account balances, 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 HQLA category substantially includes: cash on hand, funds held in the nostro account with the NBP (National Bank of Poland) in excess of the minimum reserve requirement and securities which may be sold or pledged under repo transactions or NBP lombard loans. As at 31 December 2018, the value of the HQLA buffer was PLN 37.75 bn.

The purpose of this policy is also to ensure an adequate structure of funding in relation to the growing scale of the Bank's business by maintaining structural liquidity ratios at pre-defined levels.

The Bank uses a suite of additional watch limits and thresholds 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;
- M3 and M4 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;
- the HQLA buffer;
- the buffer of assets which might be liquidated over an intraday horizon.

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.

At least once a year, Santander Bank Polska SA carries out the Internal Liquidity Adequacy Assessment Process (ILAAP), which is designed to ensure that the Bank can effectively control and manage liquidity risk. In particular, the ILAAP ensures that the Bank:

- maintains sufficient capacity to meet its obligations as they fall due;
- reviews the key liquidity risk drivers and ensures that stress testing reflects these drivers and that they are appropriately controlled;
- provides a record of both the liquidity risk management and governance processes;
- carries out assessment of counterbalancing capacity.

The ILAAP results are subject to approval by the Management Board and the Supervisory Board to confirm adequacy of the liquidity level of Santander Bank Polska SA in terms of liquid assets, prudent funding profile and the Bank's liquidity risk management and control mechanisms.

Risk identification and measurement

The responsibility for identification and measurement of liquidity risk rests with the Risk Management Division, specifically the Financial Risk Department.

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

Liquidity is measured by means of the modified liquidity gap, which is designed separately for the PLN and currency positions. The reported future contractual cash flows are subject to modifications based on: statistical analyses of the deposit and credit base behaviour and assessment of product/ market liquidity – in the context of evaluation of the possibility to liquidate Treasury securities by selling or pledging them in repo transactions or using liquidity support instruments with NBP, as well as the possibility 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 derivative transactions and collateral needs related to secured financing transactions resulting from the downgrade of the bank's credit rating, among other things.

Concurrently, liquidity is measured in accordance with KNF Resolution no. 386/2008 on setting liquidity standards for banks (in force as at 31 December 2018), and with the requirements laid down in the CRD IV/ CRR package and in their implementing provisions.

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

- baseline scenario, which assumes non-renewability of wholesale funding;
- idiosyncratic liquidity crisis scenarios (specific to the bank);
- local systemic liquidity crisis scenario;

In thousands of PLN

- global systemic liquidity crisis scenario;
- combined liquidity crisis scenario (idiosyncratic crisis and local systemic crisis);
- deposit outflows in a one-month horizon.

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

In addition, the bank performs stress tests for intraday liquidity as well as reverse stress tests.

Risk reporting

The responsibility for reporting liquidity risk rests with the Risk Management Division, specifically the Financial Risk Department.

The results of liquidity risk measurement are reported by the Financial Risk Department 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).

Risk prevention and mitigation

The responsibility for supervision over the liquidity risk management process rests with 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 funding the bank's activity. Day-to-day management of liquidity is delegated to the Financial Management Division. The Assets and Liabilities Management Department, which is a part of the Division, is responsible for developing and updating the relevant liquidity management strategies.

The bank has a liquidity contingency plan approved by the Management Board and Supervisory Board to cater for unexpected liquidity problems, whether caused by external or internal factors. The plan, accompanied by stress tests, includes different types of scenarios and enables the bank to take adequate and effective actions in response to unexpected external or internal liquidity pressure through:

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

In 2018, Santander Bank Polska SA focused on keeping its loan-to-deposit ratio at a comfortable level (92% as at 31 December 2018) and controlling key short and long-term liquidity measures. As at 31 December 2018, the consolidated Liquidity Coverage Ratio was 190%, and 169% as at 31 December 2017. In 2018 and in the comparable period, all key regulatory ratios applicable to the Bank were maintained at the required levels.

The tables below show the cumulated liquidity gap on an unconsolidated level (for Santander Bank Polska S.A.) as at 31 December 2018 and in the comparable period (by nominal value).

31.12.2018	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	22 200 320	15 328 453	4 222 219	9 431 435	9 315 557	14 916 635	36 773 241	76 206 830
Liabilities and equity	85 429 245	25 082 447	15 064 408	13 222 262	7 189 917	1 803 168	4 203 844	32 265 440
including:								
- Sell-buy-back transactions	-	8 234 700	-	-	-	-	-	-
- Deposits from banks	150 124	163 643	103 273	277 167	132 025	45 173	61 223	57 678
- Deposits from customers	85 279 121	16 680 560	14 917 966	11 274 837	6 170 320	966 886	203 186	3 731
- Debt securities in issue	-	-	-	661 633	527 375	16 181	2 166 069	-
- Subordinated liabilities	-	-	(343)	8 267	-	-	-	2 535 530
Contractual liquidity mismatch/ gap	(63 228 926)	(9 753 994)	(10 842 188)	(3 790 827)	2 125 640	13 113 466	32 569 396	43 941 389
Cumulative liquidity gap	(63 228 926)	(72 982 920)	(83 825 108)	(87 615 935)	(85 490 295)	(72 376 829)	(39 807 433)	4 133 957
Net derivatives	-	40 305	(25 109)	(11 332)	(2 739)	(59 305)	(450 675)	(308 246)

In thousands of PLN

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

Liquidity Coverage Ratio

Table 1 contains the values and components of the liquidity coverage ratio in accordance with the template that is a part of the EBA/GL/2017/01 guidelines on LCR disclosure.

In thousands of PLN

Table 1:

Scope of consolidation (solo) Currency and units (PLN million)		Total unweighted value (average)				Total weighted value (average)			
Quarter ending		31.12.2018	30.09.2018	30.06.2018	31.03.2018	31.12.2018	30.09.2018	30.06.2018	31.03.2018
Number of data points used in the calculation of averages		12	12	12	12	12	12	12	12
	HIGH-QUALITY LIQUID ASSETS								
1	TOTAL HIGH-QUALITY LIQUID ASSETS (HQLA)					30 591	27 685	26 462	24 733
	CASH-OUTFLOWS								
2	Retail deposits and deposits from small business customers, of which:	63 347	59 550	58 772	57 570	4 886	4 438	4 364	4 244
3	*Stable deposits*	*43 839*	*43 066*	*42 619*	*42 151*	*2 192*	*2 153*	*2 131*	*2 108*
4	*Less stable deposits*	*19 508*	*16 484*	*16 153*	*15 419*	*2 694*	*2 285*	*2 233*	*2 136*
5	Unsecured wholesale funding	27 404	23 887	22 385	21 390	12 526	11 031	10 465	10 047
6	*Operational deposits (all counterparties) and deposits in networks of cooperative banks*	*5 646*	*5 379*	*5 341*	*5 223*	*1 409*	*1 343*	*1 333*	*1 304*
7	*Non-operational deposits (all counterparties)*	*21 655*	*18 384*	*16 877*	*15 958*	*11 014*	*9 564*	*8 965*	*8 534*
8	*Unsecured debt*	*103*	*124*	*167*	*209*	*103*	*124*	*167*	*209*
9	Secured wholesale funding					0	0	0	0
10	Additional requirements	20 588	20 761	21 525	22 459	3 967	3 988	4 086	4 229
11	*Outflows related to derivative exposures and other collateral requirements*	*1 209*	*1 366*	*1 398*	*1 462*	*1 209*	*1 365*	*1 398*	*1 463*
12	*Outflows related to loss of funding on debt products*	*0*	*0*	*0*	*0*	*0*	*0*	*0*	*0*
13	*Credit and liquidity facilities*	*19 379*	*19 395*	*20 127*	*20 997*	*2 758*	*2 623*	*2 688*	*2 766*
14	Other contractual funding obligations	2 016	1 751	1 857	1 834	1 799	1 540	1 666	1 652
15	Other contingent funding obligations	7 260	6 157	5 234	3 906	360	304	246	162
16	TOTAL CASH OUTFLOWS					23 538	21 301	20 827	20 334
	CASH-INFLOWS								
17	Secured lending (eg reverse repos)	152	83	24	78	0	0	0	0
18	Inflows from fully performing exposures	2 502	2 221	2 093	2 007	1 918	1 675	1 543	1 458
19	Other cash inflows	552	534	520	557	553	534	520	557
EU-19a	(Difference between total weighted inflows and total weighted outflows arising from transactions in third countries where there are transfer restrictions or which are denominated in non-convertible currencies)					-	0	0	0
EU-19b	(Excess inflows from a related specialised credit institution)					-	0	0	0
20	TOTAL CASH INFLOWS	3 206	2 838	2 637	2 642	2 471	2 209	2 063	2 015
EU-20a	***Fully exempt inflows***	*0*	*0*	*0*	*0*	*0*	*0*	*0*	*0*
EU-20b	***Inflows Subject to 90% Cap***	*0*	*0*	*0*	*0*	*0*	*0*	*0*	*0*
EU-20c	***Inflows Subject to 75% Cap***	*3 206*	*2 838*	*2 637*	*2 642*	*2 471*	*2 209*	*2 063*	*2 015*
	TOTAL ADJUSTED VALUE								
21	LIQUIDITY BUFFER					30 591	27 685	26 462	24 733
22	TOTAL NET CASH OUTFLOWS					21 067	19 092	18 764	18 318
23	LIQUIDITY COVERAGE RATIO (%)					145%	145%	141%	136%

The Bank uses secured instruments to fund its activity to a limited degree only. However, in accordance with the existing contractual provisions, if the Bank's rating is reduced by one notch (to BBB), the maximum potential additional security on account of those instruments would be PLN 556 m. At the same time, it should be noted that this potential obligation is not unconditional and its final value would depend on negotiations between the bank and its counterparty concerning the transactions.

Operational Risk

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

Santander Bank Polska SA 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 Santander Bank Polska SA. 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.

Santander Bank Polska SA uses the following tools:

- Identification and assessment of operational risk

Primary tool for identification and assessment of operational risk is self-assessment. In the self-assessment process, Santander Bank Polska SA 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 Bank runs a database of operational incidents identified across Santander Bank Polska SA. The data are used to analyse the root cause and consequences of the incidents, capture lessons learned and take preventive and corrective measures.

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

- Analysis of risk indicators

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

- Defining actions lowering the risk

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

- Business continuity management (BCM)

Each 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 Santander Bank Polska SA that critical business processes may be restored at the required service level and within the agreed timeframe. Santander Bank Polska SA 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 Santander Bank Polska, 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 Santander Bank Polska SA business environment and assessment of specific information security and information systems requirements.

- Insurance

For the purpose of operational risk mitigation, Santander Bank Polska SA 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.

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, Santander Bank Polska is exposed to the compliance risk mainly in the following areas:

- domestic an international regulations concerning the type of offered products and service delivery methods applied by the Bank and the Santander Bank Polska Group (in particular: the legislation on consumer and competition protection, capital markets, financial markets etc.);
- good practice codes and other regulations implemented by the Bank, including in connection with membership in domestic or international trade associations ;
- 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.

As part of Compliance Policy implementation, employees of the Compliance Unit have the appriopiste scope of authority, as units supporting management in effective compliance risk management and reporting all issues related to ensuring compliance to the Bank's Management Board , the Risk Management Committee and the Compliance Committee of the Supervisory Board.

These bodies 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 Bank's Management Board and the Supervisory Board – in particular through the Audit and Compliance Committee regularly reviews key compliance issues identified by the Compliance Area as well as Anti-Money Laundering Department mainly through:

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

The Compliance Unit's tasks are delivered through:

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

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 image perceived by the Bank's customers, shareholders and communities arising from materialisation of other risks, including individual types of compliance risk.

Santander Bank Polska SA 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 coordinates the following committees:

- General Compliance Committee;
- Regulatory and Reputational Risk Committee;
- Local Marketing and Monitoring Committee;
- Anti-Money Laundering and Counter-Terrorism Financing Committee.

4. Capital management

Introduction

It is the policy of Santander Bank Polska SA to maintain a 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 the bank and Santander Bank Polska Group and capital requirements estimated for unexpected losses is determined in accordance with:

- The so-called CRD IV / CRR package, which 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 include the recommendations of the KNF regarding the use of national options and higher risk weight for exposures secured by real estate mortgages, including: residential real estate, for which the amount of principal or interest installment depends on changes in exchange rates or currencies other than the currencies of revenue achieved by the debtor, where a risk weight of 150% is assigned, and office premises or other commercial real estate located in the Republic of Poland, where a risk weight of 100% is assigned.

- The Act of 5 August 2015 on macroprudential supervision over the financial system and crisis management in the financial system ("Macroprudential Supervision Act"), implementing CRD IV into the Polish law with regard to, among other things, additional capital buffers to be maintained by banks.

- Recommendations of the KNF regarding an additional capital requirement relating to the portfolio of FX mortgage loans for households.

The Management Board is accountable for capital management, calculation and maintenance processes, including the assessment of capital adequacy in different economic conditions and the evaluation of stress test results and their impact on internal and regulatory capital and capital ratios. Responsibility for the general oversight of internal capital estimation rests with the Supervisory Board.

The Management Board has delegated ongoing capital management to the Capital Committee which conducts a regular assessment of the capital adequacy of the bank and Santander Bank Polska Group, including in extreme conditions, the monitoring of the actual and required capital levels and the initiation of transactions affecting these levels (e.g. by recommending the value of dividends to be paid). The Capital Committee is the first body that defines the capital policy, principles of capital management and principles of capital adequacy assessment. However, ultimate decisions regarding any increase or decrease in capital are taken by relevant authorities within the bank in accordance with the applicable law and the bank's Statutes.

Pursuant to the bank's information strategy, details about the level of own funds and capital requirements are presented in the separate report entitled "Information on capital adequacy of Santander Bank Polska Group as at 31 December 2018".

In 2018, the Bank and Santander Bank Polska Group met all regulatory requirements regarding capital management.

Capital Policy

As at 31 December 2018, the minimum capital ratios satisfying the provisions of the CRR and the Macroprudential Supervision Act as well as regulatory recommendations regarding additional own funds requirements under Pillar 2 at the level of Santander Bank Polska SA were as follows:

- Tier 1 capital ratio of 11.76%;
- total capital ratio of 13.89%;

The above capital ratios take into account:

- The minimum capital ratios as required by the CRR: Common Equity Tier 1 ratio at 4.5%, Tier 1 capital ratio at 6.0% and total capital ratio at 8.0%.
- Recommendation of the KNF regarding an additional capital requirement relating to the portfolio of FX mortgage loans for households.

  Pursuant to the KNF's decisions of 15 October 2018 and 28 November 2018, Santander Bank Polska SA maintains own funds to cover an additional capital requirement for risk attached to foreign currency home mortgages for households. As at 31 December 2018, the buffer for Santander Bank Polska SA was set at 0.51 p.p. above the total capital ratio for Santander Bank Polska SA The buffer includes at least 75% of Tier 1 capital (which corresponds to the capital requirement of 0.38 p.p. above Tier 1 capital ratio for Santander Bank Polska SA) and at least 56% of the Common Equity Tier 1 capital (which corresponds to the capital requirement of 0.29 p.p. above the Common Equity Tier 1 capital for Santander Bank Polska SA).
- The capital buffer for Santander Bank Polska SA as other systemically important institution.

  On 4 October 2017, the KNF identified Santander Bank Polska SA as other systemically important institution and imposed on it an additional capital buffer of 0.5 p.p.
- The capital conservation buffer maintained in accordance with the Macroprudential Supervision Act.

  On 1 January 2018, the minimum capital ratios for the banking sector in Poland were increased by the capital conservation buffer of 1.875 p.p. Following adaptation to the CRR requirements, the buffer will be 2.5 p.p. in 2019.
- The systemic risk buffer introduced by Regulation of the Minister of Economic Development and Finance of 1 September 2017, which applies to all the exposures in Poland.

  Since 1 January 2018, the systemic risk buffer has been 300 p.p.

From 1 January 2019, the capital conservation buffer will be 2.5 p.p., which will affect the minimum ratios for the bank, i.e.:

- Tier 1 capital ratio of 12.38%;
- total capital ratio of 14.51%.

Regulatory Capital

The capital requirement for Santander Bank Polska SA is determined in accordance with Part 3 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), which formed a legal basis as at the reporting date, i.e. 31 December 2017.

Santander Bank Polska SA 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 carrying amount, 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.

In thousands of PLN

The table below presents the calculation of the capital ratio for the bank as at 31 December 2018 and in the comparative period.

		31.12.2018	31.12.2017
I	**Total Capital requirement (Ia+Ib+Ic+Id)**, of which:	**9 206 462**	**7 542 253**
Ia	- due to credit risk & counterparty credit risk	8 223 999	6 606 686
Ib	- due to market risk	87 984	120 618
Ic	- due to credit valuation ajdustment risk	22 632	38 337
Id	- due to operational risk	871 847	776 612
II	Total own funds*	23 778 731	20 930 984
III	Reductions	3 023 528	3 067 603
IV	**Own funds after reductions (II-III)**	**20 755 203**	**17 863 381**
V	**CAD [IV/(I*12.5)]**	**18,04%**	**18,95%**
VI	**Tier I ratio**	**15,85%**	**17,37%**

*On 31 October 2018, a part of the bank's profit (PLN 581,844,321) for the period between 1 January 2018 and 30 June 2018 was allocated to own funds, in accordance with the KNF's consent of 28 September 2018.

Internal Capital

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

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

In the ICAAP the bank uses assessment models based on the statistical loss estimation for measurable risks, such as credit risk, market risk and operational risk, plus 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 (PD) by Santander Bank Polska SA customers and the loss given default (LGD).

The bank 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 business of Santander Bank Polska SA and to take account of any new risks and the management's judgement.

The review and assessment is the responsibility of the bank's risk management committees, including: the 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. Under the new issue conditions, the maturity of the bonds has been extended to 5 August 2025. Pursuant to the KNF's decision of 18 May 2017, the bank was authorised to allocate EUR 100m of the new issue to Tier 2 capital.

As part of the strategy to increase the Tier 2 capital, on 2 December 2016 Santander Bank Polska issued own bonds of EUR 120m, allocating them to Tier 2 in accordance with the KNF's decision of 24 February 2017.

On 22 May 2017, the bank issued additional subordinated bonds with a nominal value of EUR 137.1m and by the KNF's decision of 19 October 2017 was authorised to allocate them to the Tier 2 capital.

On 12 June 2018, Santander Bank Polska SA obtained the KNF's approval for allocating series F subordinated bonds with a total nominal value of PLN 1bn, issued on 5 April 2018, to Tier 2 capital instruments.

For more information on subordinated liabilities, see Note 32.

In thousands of PLN

5. Net interest income

Interest income and similar to interest	Interest income on financial assets measured at amortised cost	Interest income on financial assets measured at fair value through other comprehensive income	Income similar to interest - financial assets measured at fair value through profit or loss	Total
	01.01.2018-31.12.2018			
Loans and advances to enterprises	1 779 301	4 179	2 037	1 785 517
Loans and advances to individuals, of which:	2 325 892	-	72 583	2 398 475
Home mortgage loans	1 161 901	-	-	1 161 901
Debt securities incl.:	-	679 807	13 694	693 501
Investment securities	-	679 807	-	679 807
Trading portfolio	-	-	13 694	13 694
Loans and advances to banks	36 156	-	-	36 156
Loans and advances to public sector	9 730	-	-	9 730
Reverse repo transactions	72 952	-	-	72 952
Interest recorded on hedging IRS	177 878	-	-	177 878
Total	4 401 909	683 986	88 314	5 174 209

Interest expenses	Interest expenses on financial liabilities measured at amortised cost	Interest expenses on financial liabilities measured at fair value trought other comprehensive income	Expenses similar to interest - financial liabilities measured at fair value trought profit or loss	Total
	01.01.2018-31.12.2018			
Deposits from individuals	(503 018)	-	-	(503 018)
Deposits from enterprises	(358 765)	-	-	(358 765)
Repo transactions	(81 036)	-	-	(81 036)
Deposits from public sector	(52 324)	-	-	(52 324)
Deposits from banks	(15 795)	-	-	(15 795)
Subordinated liabilities and issue of securities	(100 215)	-	-	(100 215)
Total	(1 111 153)	-	-	(1 111 153)
Net interest income	**3 290 756**	**683 986**	**88 314**	**4 063 056**

As at 31.12.2018 interest income on financial assets measured at amortised cost includes interest on impaired loans of PLN 165,654 k (as at 31.12.2017- PLN 167,387 k).

In thousands of PLN

Interest income	01.01.2017-31.12.2017
Loans and advances to enterprises	1 654 877
Loans and advances to individuals, of which:	2 140 362
Home mortgage loans	986 586
Debt securities incl.:	609 508
Investment portfolio available for sale	575 907
Trading portfolio	33 601
Loans and advances to banks	60 405
Loans and advances to public sector	6 289
Reverse repo transactions	27 342
Interest recorded on hedging IRS	204 404
Total	4 703 187

Interest expenses	01.01.2017-31.12.2017
Deposits from individuals	(433 880)
Deposits from enterprises	(294 514)
Repo transactions	(48 361)
Deposits from public sector	(51 277)
Deposits from banks	(16 486)
Subordinated liabilities and issue of securities	(73 120)
Total	(917 638)
Net interest income	**3 785 549**

In thousands of PLN

6. Net fee and commission income

Fee and commission income	01.01.2018-31.12.2018	01.01.2017-31.12.2017
eBusiness & payments	575 791	577 356
Current accounts and money transfer	315 053	329 905
Asset management fees	-	3 637
Foreign exchange commissions	396 008	346 056
Credit commissions	298 167	247 099
Insurance commissions	56 289	69 397
Brokerage activities	66 947	88 166
Credit cards	84 646	88 275
Off-balance sheet guarantee commissions	74 032	62 396
Issue arrangement fees	9 374	14 865
Distribution fees	18 179	163 891
Other commissions	5 759	6 838
Total	**1 900 245**	**1 997 881**
Fee and commission expenses	**01.01.2018-31.12.2018**	**01.01.2017-31.12.2017**
eBusiness & payments	(188 045)	(204 087)
Brokerage activities	(9 593)	(11 175)
Credit cards	(15 312)	(15 469)
Credit commissions paid	(30 006)	(8 647)
Insurance commissions	(6 554)	(5 172)
Finance lease commissions	(185)	(135)
Other	(33 647)	(26 548)
Total	**(283 342)**	**(271 233)**
Net fee and commission income	**1 616 903**	**1 726 648**

Included above is fee and commission income on credits, credit cards and off-balance sheet guarantee commissions of PLN 428,488 k (2017: PLN 397,770 k) and fee and commission expenses on credits cards and paid to credit agents of PLN (45,318) k (2017: PLN (24,116) k) (other than fees included in determining the effective interest rate), relating to financial assets and liabilities not carried at fair value through profit or loss.

Details information on changes in comparability is presented in note 2.4.

7. Dividend income

Dividend income	01.01.2018-31.12.2018	01.01.2017-31.12.2017
Dividends from subsidiaries and associates	392 573	222 791
Dividends from equity financial assets available for sale	-	76 181
Dividends income from equity investment security	98 907	-
Dividends income from equity financial assets at fair value through profit or loss	1 127	546
Total	**492 607**	**299 518**

In thousands of PLN

8. Net trading income and revaluation

Net trading income and revaluation	01.01.2018-31.12.2018	01.01.2017-31.12.2017
Derivative instruments and interbank fx transactions	142 692	184 968
Profit on equity instruments	-	4 265
Profit on debt instruments	-	(6 004)
Profit on equity securities measured at fair value through profit or loss	(3 674)	-
Profit on debt securities measured at fair value through profit or loss	22 431	-
Change in fair value of loans and advances mandatorily measured at fair value through profit or loss	(7 885)	-
Total	**153 564**	**183 229**

Net trading income and revaluation includes the change of the value of derivative instruments in the amount of PLN (1,629) k for 2018 and PLN (10,354) k for 2017.

The amounts included CVA and DVA adjustments which in 2018 and 2017 totaled PLN (742) k and PLN (11,572) k respectively.

9. Gains (losses) from other financial securities

Gains (losses) from other financial securities	01.01.2018-31.12.2018	01.01.2017-31.12.2017
Profit on sale of equity securities available for sale	-	26 420
Profit on sale of debt securities available for sale	-	20 549
Profit on sale of debt securities measured at fair value through other comprehensive income	28 327	-
Change in fair value of debt securities mandatorily measured at fair value through profit or loss	12 120	-
Total profit (losses) on financial instruments	**40 447**	**46 969**
Change in fair value of hedging instruments	(16 561)	23 760
Change in fair value of underlying hedged positions	16 636	(26 115)
Total profit (losses) on hedging and hedged instruments	**75**	**(2 355)**
Total	**40 522**	**44 614**

10. Other operating income

Other operating income	01.01.2018-31.12.2018	01.01.2017-31.12.2017
Income on sale of services	31 467	20 612
Reimbursements of BGF charges	-	433
Release of provision for legal cases and other assets	51 364	5 430
Settlements of leasing agreements	592	944
Recovery of other receivables (expired, canceled and uncollectable)	6 280	5 598
Profit on sales or liquidation of fixed assets, intangible assets and assets for disposal	50 611	12 314
Received compensations, penalties and fines	2 274	821
Other income from legal cases	-	24 238
Other	11 747	13 373
Total	**154 335**	**83 763**

In thousands of PLN

11. Impairment losses on loans and advances

Impairment losses on loans and advances measured at amortised cost for reporting period: 01.01.2018-31.12.2018	Stage 1	Stage 2	Stage 3	POCI	Total
Charge for loans and advances to banks	(66)	-	-	-	(66)
Charge for loans and advances to customers	(111 640)	35 760	(745 091)	51 267	(769 704)
Recoveries of loans previously written off	-	-	(7 717)	-	(7 717)
Off-balance sheet credit related facilities	(1 348)	5 556	(4 232)	-	(24)
Total	**(113 054)**	**41 316**	**(757 040)**	**51 267**	**(777 511)**

Impairment losses on loans and advances	01.01.2017-31.12.2017
Collective and individual impairment charge	(512 966)
Incurred but not reported losses charge	(28 111)
Recoveries of loans previously written off	(2 103)
Off-balance sheet credit related facilities	2 805
Total	**(540 375)**

12.Employee costs

Employee costs	01.01.2018-31.12.2018	01.01.2017-31.12.2017
Salaries and bonuses	(1 133 392)	(1 042 255)
Salary related costs	(187 098)	(174 422)
Staff benefits costs	(29 827)	(30 252)
Professional trainings	(15 083)	(14 170)
Retirement fund, holiday provisions and other employee costs	29 267	6 095
Total	**(1 336 133)**	**(1 255 004)**

13. General and administrative expenses

General and administrative expenses	01.01.2018-31.12.2018	01.01.2017-31.12.2017
Maintenance and rentals of premises	(289 483)	(289 413)
Marketing and representation	(122 172)	(69 549)
IT systems costs	(175 455)	(141 664)
Cost of BFG, KNF and KDPW	(196 554)	(195 838)
Postal and telecommunication costs	(45 714)	(36 725)
Consulting fees	(71 542)	(55 354)
Cars, transport expenses, carriage of cash	(62 753)	(58 546)
Other external services	(128 517)	(82 207)
Stationery, cards, cheques etc.	(21 819)	(17 705)
Sundry taxes and charges	(31 483)	(28 025)
Data transmission	(7 334)	(9 327)
KIR, SWIFT settlements	(27 518)	(25 986)
Security costs	(26 072)	(23 976)
Costs of repairs	(22 961)	(13 210)
Other	(24 765)	(20 668)
Total	**(1 254 142)**	**(1 068 193)**

In thousands of PLN

14. Other operating expenses

Other operating expenses	01.01.2018-31.12.2018	01.01.2017-31.12.2017
Charge of provisions for legal cases and other assets	(106 098)	(42 144)
Impairment loss on property, plant, equipment and intangible assets	(13 054)	(8 342)
Costs of purchased services	(14 797)	(8 177)
Other memebership fees	(797)	(783)
Paid compensations, penalties and fines	(2 106)	(2 883)
Donations paid	(4 594)	(4 670)
Other	(10 972)	(14 191)
Total	**(152 418)**	**(81 190)**

15. Corporate income tax

Corporate income tax	01.01.2018-31.12.2018	01.01.2017-31.12.2017
Current tax charge in the income statement	(668 355)	(459 896)
Deffered tax	175 169	(139 447)
Adjustments from previous years	2 283	169
Total tax on gross profit	**(490 903)**	**(599 174)**

Corporate total tax charge information	01.01.2018-31.12.2018	01.01.2017-31.12.2017
Profit before tax	2 658 064	2 515 330
Tax rate	19%	19%
Tax calculated at the tax rate	(505 032)	(477 913)
Non-tax-deductible expenses	(10 856)	(8 403)
The fee to the Bank Guarantee Fund	(34 510)	(34 971)
Tax on financial institutions	(81 143)	(73 717)
The gain on aquisition of organised part of enterprise	69 305	-
Sale of receivables	(6 109)	(52 237)
Non-taxable income (dividends)	93 440	56 753
Non-tax deductible bad debt provisions	(17 847)	(10 970)
Adjustment of prior year tax	2 283	169
Other	(434)	2 115
Total tax on gross profit	**(490 903)**	**(599 174)**

Deferred tax recognised in other comprehensive income	31.12.2018	31.12.2017
Relating to equity securities available-for-sale	-	(132 797)
Relating to debt securities available-for-sale	-	(55 657)
Relating to valuation of debt investments measured at fair value through other comprehensive income	(127 697)	-
Relating to valuation of equity investments measured at fair value through other comprehensive income	(127 204)	-
Relating to cash flow hedging activity	15 694	21 446
Relating to valuation of defined benefit plans	(2 553)	(75)
Total	**(241 760)**	**(167 083)**

In thousands of PLN

16. Earnings per share

Earnings per share	01.01.2018-31.12.2018	01.01.2017-31.12.2017
Profit for the period attributable to ordinary shares	2 167 161	1 916 156
Weighted average number of ordinary shares	99 725 949	99 275 197
Earnings per share (PLN)	**21,73**	**19,30**
Profit for the period attributable to ordinary shares	2 167 161	1 916 156
Weighted average number of ordinary shares	99 725 949	99 275 197
Weighted average number of potential ordinary shares	171 095	187 456
Diluted earnings per share (PLN)	**21,69**	**19,27**

The weighted average number of ordinary shares contains dilutive instruments in the form of share capital presented in note 37 and the share based incentive scheme included in note 51.

17.Cash and balances with central banks

Cash and balances with central banks	31.12.2018	31.12.2017
Cash	2 431 098	2 249 508
Current accounts in central banks	6 410 804	1 857 293
Term deposits	-	8 000
Total	**8 841 902**	**4 114 801**

Santander Bank Polska SA holds an obligatory reserve on a current account in the National Bank of Poland. The figure is calculated at a fixed percentage of the monthly average balance of the customers' deposits, which was 3.5% as at 31.12.2018 and 31.12.2017.

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

18. Loans and advances to banks

Loans and advances to banks	31.12.2018	31.12.2017
Loans and advances	1 255 204	851 061
Current accounts	1 604 341	1 161 057
Gross receivables	**2 859 545**	**2 012 118**
Allowance for impairment	(66)	-
Total	**2 859 479**	**2 012 118**

Fair value of loans and advances to banks is presented in Note 42.

In thousands of PLN

Loans and advances to banks

Gross carrying amount	Stage 1	Stage 2	Stage 3	POCI	Total
Balance at the beginning of the period	**2 012 118**	**-**	**-**	**-**	**2 012 118**
Transfers					-
Transfer to Stage 1	-	-	-	-	-
Transfer to Stage 2	-	-	-	-	-
Transfer to Stage 3	-	-	-	-	-
New financial assets registered	1 701 482	-	-	-	1 701 482
Changes in existing financial assets	-	-	-	-	-
Financial assets derecognised that are not write-offs	(842 342)	-	-	-	(842 342)
Write-offs	-	-	-	-	-
FX and others movements	(11 713)	-	-	-	(11 713)
Balance at the end of the period	**2 859 545**	**-**	**-**	**-**	**2 859 545**

19. Financial assets and liabilities held for trading

Financial assets and liabilities held for trading	31.12.2018 Assets	31.12.2018 Liabilities	31.12.2017 Assets	31.12.2017 Liabilities
Trading derivatives	**1 088 081**	**1 062 313**	**1 231 990**	**1 263 859**
Interest rate operations	**560 854**	**545 539**	**312 783**	**276 635**
Forward	65	6 640	-	68
Options	13 898	13 911	13 211	13 226
IRS	543 493	523 788	297 054	261 776
FRA	3 398	1 200	2 518	1 565
Transactions on equity instruments	**3 279**	**3 279**	**6 053**	**6 053**
Options	3 279	3 279	6 053	6 053
FX operations	**523 948**	**513 495**	**913 154**	**981 171**
CIRS	192 483	206 346	282 186	275 786
Forward	40 065	61 233	41 175	160 814
FX Swap	192 760	147 492	493 265	447 589
Spot	585	376	1 360	1 832
Options	98 055	98 048	95 168	95 150
Debt and equity securities	**8 688 624**	**-**	**2 189 557**	**-**
Debt securities	**8 671 723**	**-**	**2 174 096**	**-**
Government securities:	8 667 540	-	2 170 048	-
- bonds	8 667 540	-	2 170 048	-
Commercial securities:	4 183	-	4 048	-
- bonds	4 183	-	4 048	-
Equity securities:	**16 901**	**-**	**15 461**	**-**
- listed	16 901	-	15 461	-
Short sale	**-**	**175 689**	**-**	**-**
Total financial assets/liabilities	**9 776 705**	**1 238 002**	**3 421 547**	**1 263 859**

Financial assets and liabilities held for trading - trading derivatives include the change in the value of counterparty risk in the amount of PLN (1 017) k as at 31.12.2018 and PLN (28) k as at 31.12.2017.

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

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

In thousands of PLN

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 31.12.2018 and in comparable period there were no cases of instruments designated to financial assets measured at fair value through profit and loss at initial recognition.

Offsetting financial assets and financial liabilities

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

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

	31.12.2018		31.12.2017	
Offsetting financial assets and financial liabilities	**Financial assets**	**Financial liabilities**	**Financial assets**	**Financial liabilities**
Fair value measurements of derivative instruments	1 140 635	1 965 483	1 378 714	1 842 657
Value of collateral accepted/provided	(146 882)	(1 291 885)	(347 951)	(751 068)
Maximum amount of potential set-off	(316 971)	(316 971)	(388 627)	(388 627)
Assets and liabilities not subject to set-offs	**676 782**	**356 627**	**642 136**	**702 962**

In thousands of PLN

The table below presents derivatives' nominal values.

	Derivatives' nominal values	31.12.2018	31.12.2017
1.	**Term derivatives (hedging)**	**21 807 562**	**23 570 504**
a)	Single-currency interest rate swap (IRS)	2 131 000	2 404 709
b)	Macro cash flow hedge -purchased (IRS)	1 575 000	1 575 000
c)	Macro cash flow hedge -purchased (CIRS)	8 746 338	9 707 988
d)	Macro cash flow hedge -sold (CIRS)	9 355 224	9 882 807
2.	**Term derivatives (trading)**	**408 209 745**	**285 338 721**
a)	Interest rate operations	261 807 412	170 594 604
	Single-currency interest rate swap (IRS)	230 258 701	158 895 602
	FRA - purchased amounts	21 444 400	3 260 000
	Options	7 097 193	8 370 402
	Forward- purchased amounts	84 100	-
	Forward- sold amounts	2 923 018	68 600
b)	FX operations	146 402 333	114 744 117
	FX swap – purchased amounts	37 836 903	29 904 524
	FX swap – sold amounts	37 779 343	29 837 481
	Forward- purchased amounts	10 183 310	8 226 882
	Forward- sold amounts	10 233 343	8 393 420
	Cross-currency interest rate swap (CIRS) – purchased amounts	13 749 426	10 992 948
	Cross-currency interest rate swap (CIRS) – sold amounts	13 768 772	10 991 112
	FX options -purchased CALL	5 622 329	4 036 440
	FX options -purchased PUT	5 803 289	4 162 435
	FX options -sold CALL	5 622 329	4 036 440
	FX options -sold PUT	5 803 289	4 162 435
3.	**Currency transactions- spot**	**1 598 307**	**2 893 238**
	Spot-purchased	799 268	1 446 436
	Spot-sold	799 039	1 446 802
4.	**Transactions on equity financial instruments**	**555 792**	**817 734**
	Derivatives contract - purchased	270 165	401 987
	Derivatives contract - sold	285 627	415 747
	Total	**432 171 406**	**312 620 197**

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

20. Hedging derivatives

	31.12.2018		31.12.2017	
Hedging derivatives	**Assets**	**Liabilities**	**Assets**	**Liabilities**
Derivatives hedging fair value	312	129 205	2 283	115 496
Derivatives hedging cash flow	52 242	773 965	144 441	463 302
Total hedging derivatives	**52 554**	**903 170**	**146 724**	**578 798**

Hedging derivatives – derivatives hedging cash flow include value adjustments day first profit or loss for start forward CIRS transactions in the amount of PLN (8,562) k as at 31.12.2018 and (9,613) k as at 31.12.2017.

In thousands of PLN

21. Loans and advances to customers

Loans and advances to customers	31.12.2018 Measured at amortised cost	31.12.2018 Measured at fair value through other comprehensive income	31.12.2018 Measured at fair value through profit or loss	31.12.2017
Loans and advances to enterprises	58 823 206	366 751	106 374	49 011 673
Loans and advances to individuals, of which:	59 619 111	-	962 766	44 322 763
Home mortgage loans	*45 927 616*	-	-	*33 723 865*
Loans and advances to public sector	325 767	-	-	227 389
Other	11 517	-	-	7 303
Gross receivables	**118 779 601**	**366 751**	**1 069 140**	**93 569 128**
Allowance for impairment *	(2 723 002)	-	-	(3 032 125)
Total**	**116 056 599**	**366 751**	**1 069 140**	**90 537 003**

*The impairment allowance for loans and advances to customers measured at fair value through other comprehensive income is included in the 'Revaluation reserve' item and does not reduce the carrying amount of the loan.

** As at 31.12.2018 debt securities carried at loans and advances to customers was PLN 1 248 750 k, as at 31.12.2017 – PLN 1 279 563 k.

As at 31.12.2018 the fair value adjustment due to hedged risk on individual loans was PLN (1,336) k.

The gross carrying amount of a financial asset is the amortised cost of the asset before adjustment by any allowances for expected credit losses, excluding calculated penalty interest on overdue principal. Recognition of a full value of the calculated penalty interest on overdue principal would result in an increase in the gross carrying amount of loans and advances to customers, while causing the value of allowances for expected credit losses to increase by PLN 851,362 k.

Detailed currency analysis of mortgage loans is presented in the consolidated financial statements of Santander Bank Polska S.A. for 2018 released on 22.02.2019.

Fair value of "Loans and advances to customers" is disclosed in Note 42.

Loans and advances to customers

Gross carrying amount	Stage 1	Stage 2	Stage 3	POCI	Total
Balance at the beginning of the period	**84 789 664**	**4 173 833**	**4 302 736**	**302 895**	**93 569 128**
Transfers					
Transfer to Stage 1	1 577 739	(1 528 156)	(49 583)	-	-
Transfer to Stage 2	(2 138 524)	2 202 692	(64 168)	-	-
Transfer to Stage 3	(842 545)	(541 595)	1 384 140	-	-
New financial assets registered	39 496 799	-	-	421 518	39 918 317
Changes in existing financial assets	(2 622 498)	(373 972)	(48 286)	(21 710)	(3 066 466)
Financial assets derecognised that are not write-offs	(9 194 927)	(457 472)	(511 107)	(218 638)	(10 382 144)
Write-offs	-	-	(745 478)	-	(745 478)
FX and others movements	(597 425)	(45 198)	(115 488)	244 355	(513 756)
Balance at the end of the period	**110 468 283**	**3 430 132**	**4 152 766**	**728 420**	**118 779 601**

In thousands of PLN

Movements on impairment losses on loans and advances to customers measured at amortised cost for reporting period 01.01.2018 - 31.12.2018	Stage 1	Stage 2	Stage 3	Total
Balance at the beginning of the period	**(257 277)**	**(298 654)**	**(2 112 224)**	**(2 668 155)**
Transfers				
Transfer to Stage 1	(12 186)	79 121	15 383	82 318
Transfer to Stage 2	72 339	(153 117)	37 149	(43 629)
Transfer to Stage 3	67 319	69 427	(588 739)	(451 993)
New financial assets registered	(489 543)	-	-	(489 543)
Changes in credit risk of existing financial assets	34 392	33 536	(300 050)	(232 122)
Changes in models and risk parameters	22 760	6 497	11 891	41 148
Financial assets derecognised that are not write-offs	41 426	26 958	328 440	396 824
Write-offs	-	-	745 478	745 478
FX and others movements	158 318	(27 899)	(200 830)	(70 411)
Balance at the end of the period	**(362 452)**	**(264 131)**	**(2 063 502)**	**(2 690 085)**

Movements on impairment losses on purchased or originated credit-impaired loans (POCI)	01.01.2018-31.12.2018
Balance at the beginning of the period	**-**
Charge/write back of current period	(32 603)
Write off/Sale of receivables	-
Transfer	-
F/X differences	(314)
Balance at the end of the period	**(32 917)**

Loans and advances to enterprises

Gross carrying amount	Stage 1	Stage 2	Stage 3	POCI	Total
Balance at the beginning of the period	**43 083 032**	**2 766 850**	**3 060 869**	**100 922**	**49 011 673**
Transfers					
Transfer to Stage 1	1 046 793	(1 036 580)	(10 213)	-	-
Transfer to Stage 2	(1 362 063)	1 377 507	(15 444)	-	-
Transfer to Stage 3	(488 109)	(317 414)	805 523	-	-
New financial assets registered	17 462 140	-	-	327 904	17 790 044
Changes in existing financial assets	(192 385)	(297 582)	(32 987)	(10 113)	(533 067)
Financial assets derecognised that are not write-offs	(6 690 070)	(381 160)	(46 524)	(148 502)	(7 266 256)
Write-offs	-	-	(358 142)	-	(358 142)
FX and others movements	406 164	(154 876)	(209 415)	137 081	178 954
Balance at the end of the period	**53 265 502**	**1 956 745**	**3 193 667**	**407 292**	**58 823 206**

In thousands of PLN

Movements on impairment losses on loans and advances to enterprises measured at amortised cost for reporting period 01.01.2018 - 31.12.2018	Stage 1	Stage 2	Stage 3	Total
Balance at the beginning of the period	**(139 164)**	**(195 808)**	**(1 459 297)**	**(1 794 269)**
Transfers				
Transfer to Stage 1	(7 454)	45 022	3 254	40 822
Transfer to Stage 2	44 795	(86 346)	10 874	(30 677)
Transfer to Stage 3	40 276	37 164	(314 285)	(236 845)
New financial assets registered	(186 161)	-	-	(186 161)
Changes in credit risk of existing financial assets	15 492	23 456	(55 147)	(16 199)
Changes in models and risk parameters	20 328	(3 001)	(2 936)	14 391
Financial assets derecognised that are not write-offs	23 259	20 027	15 015	58 301
Write-offs	-	-	358 142	358 142
FX and others movements	(16 534)	(3 953)	(56 486)	(76 973)
Balance at the end of the period	**(205 163)**	**(163 439)**	**(1 500 866)**	**(1 869 468)**

Loans and advances to individuals

Gross carrying amount	Stage 1	Stage 2	Stage 3	POCI	Total
Balance at the beginning of the period	**41 471 940**	**1 406 983**	**1 241 867**	**201 973**	**44 322 763**
Transfers					
Transfer to Stage 1	530 946	(491 576)	(39 370)	-	-
Transfer to Stage 2	(776 461)	825 185	(48 724)	-	-
Transfer to Stage 3	(354 437)	(224 180)	578 617	-	-
New financial assets registered	21 932 067	-	-	93 613	22 025 680
Changes in existing financial assets	(2 430 113)	(76 389)	(15 299)	(11 597)	(2 533 398)
Financial assets derecognised that are not write-offs	(2 504 856)	(76 313)	(464 583)	(70 136)	(3 115 888)
Write-offs	-	-	(387 336)	-	(387 336)
FX and others movements	(1 003 588)	109 678	93 926	107 274	(692 710)
Balance at the end of the period	**56 865 498**	**1 473 388**	**959 098**	**321 127**	**59 619 111**

Movements on impairment losses on loans and advances to individuals measured at amortised cost for reporting period 01.01.2018 - 31.12.2018	Stage 1	Stage 2	Stage 3	Total
Balance at the beginning of the period	**(118 113)**	**(102 846)**	**(652 927)**	**(873 886)**
Transfers				
Transfer to Stage 1	(4 732)	34 099	12 129	41 496
Transfer to Stage 2	27 544	(66 771)	26 275	(12 952)
Transfer to Stage 3	27 043	32 263	(274 454)	(215 148)
New financial assets registered	(303 383)	-	-	(303 383)
Changes in credit risk of existing financial assets	18 900	10 080	(244 902)	(215 922)
Changes in models and risk parameters	2 432	9 499	14 827	26 758
Financial assets derecognised that are not write-offs	18 166	6 931	313 425	338 522
Write-offs	-	-	387 336	387 336
FX and others movements	174 851	(23 946)	(144 344)	6 561
Balance at the end of the period	**(157 292)**	**(100 691)**	**(562 635)**	**(820 618)**

In thousands of PLN

Movements on impairment losses on loans and advances to customers	31.12.2017
Individual and collective impairment	
As at the beginning of the period	**(2 740 861)**
Charge/write back of current period	(512 966)
Write off/Sale of receivables	570 092
Transfer	(16 684)
F/X differences	25 657
Balance at the end of the period	**(2 674 762)**
IBNR	
As at the beginning of the period	**(341 566)**
Charge/write back of current period	(28 111)
Sale of receivables	3 429
Transfer	1 204
F/X differences	7 681
Balance at the end of the period	**(357 363)**
Allowance for impairment	**(3 032 125)**

Santander Bank Polska may write-off financial assets that are still subject to enforcement activity. The outstanding contractual amount of such assets written off during the year ended 31 December 2018 was PLN 170 560k.

22.Investment securities

Investment securities	31.12.2018
Debt securities measured at fair value through other comprehensive income	**35 439 836**
Government securities:	27 621 915
- bonds	27 621 915
Central Bank securities:	5 999 249
- bills	5 999 249
Other securities:	1 818 672
-bonds	1 818 672
Debt securities measured at fair value through profit and loss	**131 005**
Equity securities measured at fair value through other comprehensive income	**801 272**
- listed	-
- unlisted	801 272
Total	**36 372 113**

Financial assets available for sale	31.12.2017
Debt securities	**24 889 479**
Government securities:	21 419 899
- bonds	21 419 899
Central Bank securities:	1 379 839
- bills	1 379 839
Other securities:	2 089 741
-bonds	2 089 741
Equity securities	**894 550**
- listed	-
- unlisted	894 550
Total	**25 784 029**

As at 31.12.2018 fixed interest rate debt securities measured at fair value through other comprehensive income amount to PLN 25,191,336 k, variable interest rate securities amount to PLN 10,248,500 k.

In thousands of PLN

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

As at 31.12.2018 fair value adjustment resulting from fair value hedge on debt securities subject to hedging totaled PLN 118,750 k (as at 31.12.2017 PLN 107,005 k).

Fair value of „Investment securities" is presented in Note 42.

Movements on investment securities	Debt securities measured at fair value through other comprehensive income	Debt securities measured at fair value through profit and loss	Equity securities measured at fair value through other comprehensive income	Total
As at 31.12.2017	**24 889 479**	**-**	**894 550**	**25 784 029**
Impact of the implementation of IFRS 9	-	90 175	(105 893)	(15 718)
As at 1.01.2018 (restated)	**24 889 479**	**90 175**	**788 657**	**25 768 311**
Increases due to acquisition of demerged part of Deutsche Bank Polska SA	63 077	20 013	-	83 090
Additions	162 092 587	-	2 519	162 095 106
Disposals (sale and maturity)	(152 102 943)	-	(316)	(152 103 259)
Fair value adjustment	390 904	12 120	10 412	413 436
Movements on interest accrued	25 431	-	-	25 431
FX differences	81 301	8 697	-	89 998
As at 31.12.2018	**35 439 836**	**131 005**	**801 272**	**36 372 113**

Movements on financial assets available for sale	Debt securities	Financial instruments representing equity rights	Total
As at 1.01.2017	**25 467 070**	**855 291**	**26 322 361**
Additions	60 456 329	2 036	60 458 365
Disposals (sale and maturity)	(61 393 423)	(8 691)	(61 402 114)
Fair value adjustment	444 504	45 914	490 418
Movements on interest accrued	30 469	-	30 469
FX differences	(115 470)	-	(115 470)
As at 31.12.2017	**24 889 479**	**894 550**	**25 784 029**

23. Investments in subsidiaries and associates

Investments in subsidiaries and associates	31.12.2018	31.12.2017
Subsidiaries	2 360 331	2 340 431
Associates	36 606	36 606
Total	**2 396 937**	**2 377 037**

In thousands of PLN

Investments in subsidiaries and associates as at 31.12.2018 *

Name of entity	Santander Inwestycje Sp. z o.o.	Santander Finanse Sp. z o.o.	Santander Towarzystwo Funduszy Inwestycyjnych S.A.	Santander Securities S.A.	Santander Consumer Bank S.A.	Total
Registered office	Warszawa	Poznań	Poznań	Warszawa	Wrocław	
Type of connection	Subsidiary	Subsidiary	Subsidiary	Subsidiary	Subsidiary	
% of holding	100,00	100,00	50,00	100,00	60,00	
Balance sheet value	46 600	130 562	6 755	20 000	2 156 414	**2 360 331**
Total assets	39 944	251 704	260 918	177 011	18 691 765	**19 421 342**
Own funds of entity, of which:	39 875	245 701	208 433	42 891	3 297 131	**3 834 031**
Share capital	100	1 630	13 500	15 000	520 000	550 230
Other own funds, of which:	39 775	244 071	194 933	27 891	2 777 131	3 283 801
from previous years	4 881	-	-	1 506	466 785	473 172
net profit (loss)	176	35 859	189 921	(66)	559 042	784 932
Liabilities of entity	69	6 003	52 485	134 120	15 394 634	**15 587 311**
Revenue	335	51 993	314 123	1 740	2 047 370	**2 415 561**

* unaudited data

Name of entity	
Santander Inwestycje Sp. z o.o.	trading in shares of commercial companies as well as other securities; seeking investors for companies
Santander Finanse Sp. z o.o.	centralised managemet of the bank's subsidiaries: Santander Leasing S.A., Santander Faktor Sp. z o.o. and Santander F24 S.A.
Santander Towarzystwo Funduszy Inwestycyjnych S.A.	brokerage activities: managing customer's share portfolios (listed and not listed)
Santander Securities S.A.	accepting and forwarding orders to buy and sell financial instruments, and executing them on behalf and for the account of the principal, maintaining securities accounts and the cash accounts associated with them, offering financial instruments
Santander Consumer Bank S.A.	accepting savings and term deposits, granting and taking out loans and advances

Name of associate	Country of incorporation and place of business	The Bank's share in capital / voting power		Valuation method	Scope of business
		2018	2017		
Santander Aviva Towarzystwo Ubezpieczeń na Życie S.A.	Poland	49,00	49,00	Equity method	life insurance
Santander - Aviva Towarzystwo Ubezpieczeń S.A.	Poland	49,00	49,00	Equity method	property and personal insurance

	Santander - Aviva Towarzystwo Ubezpieczeń na Życie S.A.		Santander - Aviva Towarzystwo Ubezpieczeń S.A.	
	2018 *	2017	2018 *	2017
Loans and advances to banks	31 138	50 832	9 045	4 353
Financial assets held for trading	80 496	11 697	1 219	1 262
Investment securities	395 694	340 823	417 615	447 621
Deferred tax assets	761	67	-	-
Net life insurance assets where the deposit (investment) risk is incurred by the insuring party	257 117	383 694	-	-
Other settlements	34 090	18 021	32 052	29 561
Prepayments	229 415	162 202	148 807	199 364
Other items	675	818	554	859
Total assets	**1 029 386**	**968 154**	**609 292**	**683 020**
Technical insurance provisions	716 553	727 811	277 170	362 294
Reinsurers' share in provisions	(6 148)	(6 423)	(111 397)	(141 601)
Estimated recourses and recoveries (negative value)	-	-	(1 103)	(1 103)
Other liabilities	204 820	137 052	149 049	144 439
Prepayments and accruals	2 624	2 945	69 106	86 757
Special funds	50	34	40	32
Total liabilities	**917 899**	**861 419**	**382 865**	**450 818**
Income	236 531	180 571	145 825	156 972
Profit (loss) for the period	57 891	45 011	67 690	73 173
Dividends paid to Santander Bank Polska SA	25 035	19 142	35 660	25 719

* data are based on estimates of companies

In thousands of PLN

Investments in subsidiaries and associates as at 31.12.2017 *

Name of entity	Santander Inwestycje Sp. z o.o.	Santander Finanse Sp. z o.o.	Giełdokracja Sp. z o.o. in liquidation	Santander Towarzystwo Funduszy Inwestycyjnych S.A.	Santander Consumer Bank S.A.	Total
Registered office	Warszawa	Poznań	Poznań	Poznań	Wrocław	
Type of connection	Subsidiary	Subsidiary	Subsidiary	Subsidiary	Subsidiary	
% of holding	100,00	100,00	100,00	50,00	60,00	
Balance sheet value	46 600	130 562	100	6 755	2 156 414	**2 340 431**
Total assets	42 432	255 407	-	117 631	17 647 014	**18 062 484**
Own funds of entity, of which:	42 398	248 127	-	85 014	3 190 067	**3 565 606**
Share capital	100	1 165	-	13 500	520 000	534 765
Other own funds, of which:	42 298	246 962	-	71 514	2 670 067	3 030 841
from previous years	(6 232)	29 445	117	-	270 845	294 175
net profit (loss)	(384)	42 326	(117)	66 503	649 136	757 464
Liabilities of entity	34	7 280	-	32 617	14 456 947	**14 496 878**
Revenue	(364)	57 051	-	314 031	1 944 552	**2 315 270**

* unaudited data

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

In thousands of PLN

24. Intangible assets

Intangible assets Year 2018	Licences, patents etc.	Other	Expenditure on intangible assets	Total
Gross value - beginning of the period	**1 431 561**	**233 428**	**189 668**	**1 854 657**
Intangible assets recognised on acquisition of a demerged part of Deutsche Bank Polska S.A.	**2 441**	**192 628**	**908**	**195 977**
Additions from:				
- purchases	-	-	278 903	**278 903**
- intangible assets taken for use	205 823	-	-	**205 823**
- transfers	-	-	-	**-**
Disposals from:	**-**	**-**	**-**	**-**
- liquidation	(8 585)	-	(81)	**(8 666)**
- intangible assets taken for use	-	-	(205 823)	**(205 823)**
- transfers	-	-	-	**-**
Gross value - end of the period	**1 631 240**	**426 056**	**263 575**	**2 320 871**
Accumulated depreciation - beginning of the period	**(1 216 476)**	**(178 205)**	**-**	**(1 394 681)**
Additions/disposals from:				
- current year amortization	(138 504)	(20 330)	-	**(158 834)**
- liquidation, sale	8 552	-	-	**8 552**
- transfers				
Write down/Reversal of impairment write down				
Accumulated depreciation- end of the period	**(1 346 428)**	**(198 535)**	**-**	**(1 544 963)**
Balance sheet value				
Purchase value	1 631 240	426 056	263 575	**2 320 871**
Accumulated depreciation	(1 346 428)	(198 535)	-	**(1 544 963)**
As at 31 December 2018	**284 812**	**227 521**	**263 575**	**775 908**

Santander

In thousands of PLN

Intangible assets Year 2017	Licences, patents etc.	Other	Expenditure on intangible assets	Total
Gross value - beginning of the period	**1 334 854**	**233 428**	**176 183**	**1 744 465**
Additions from:				
- purchases	-	-	157 194	**157 194**
- intangible assets taken for use	140 791	-	-	**140 791**
- transfers	-	-	-	**-**
Disposals from:				
- liquidation	(44 084)	-	(670)	**(44 754)**
- intangible assets taken for use	-	-	(140 791)	**(140 791)**
- transfers	-	-	(2 248)	**(2 248)**
Gross value - end of the period	**1 431 561**	**233 428**	**189 668**	**1 854 657**
Accumulated depreciation - beginning of the period	**(1 127 440)**	**(152 717)**	**-**	**(1 280 157)**
Additions/disposals from:				
- current year amortization	(133 120)	(25 488)	-	**(158 608)**
- liquidation, sale	44 084	-	-	**44 084**
- transfers	-	-	-	**-**
Write down/Reversal of impairment write down	-	-	-	**-**
Accumulated depreciation- end of the period	**(1 216 476)**	**(178 205)**	**-**	**(1 394 681)**
Balance sheet value				
Purchase value	1 431 561	233 428	189 668	**1 854 657**
Accumulated depreciation	(1 216 476)	(178 205)	-	**(1 394 681)**
As at 31 December 2017	**215 085**	**55 223**	**189 668**	**459 976**

In thousands of PLN

25. Goodwill

As at 31.12.2018 and in the corresponding period, the goodwill covered the following item:

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

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

Test for impairment of goodwill arising from the merger between Santander Bank Polska and Kredyt Bank

In 2018 and in the corresponding period, the Bank conducted tests for impairment of goodwill arising from the merger with Kredyt Bank on 4 January 2013. The carrying amount as at 31 December 2018 was PLN 1,688,516 k (the same as at 31 December 2017).

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 Santander Bank Polska are in line with the 3-year financial projections of the Bank's management for 2019-2021.

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

Key assumptions for measuring value in use

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

31.12.2018	Segment Retail Banking	Segment Business and Corporate Banking	Segment Corporate & Investment Banking	Segment ALM and Centre	Total
Goodwill	764 135	578 808	222 621	122 952	**1 688 516**

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

Financial projection

The financial projection for 2019-2021 was prepared taking into account strategic and operational plans for 2019-2021 and available macroeconomic and market forecasts. According to the macroeconomic forecasts for 2019-2021 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 2019 and grow slightly 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 9.16% – 9.70%.

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 Santander Bank Polska published on the Bloomberg site and market risk premium. The risk-free rate for the next three years ranges from 3.44% to 3.98% 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 3.98%. As at the end of 2018, 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.

Under Polish law, the value of dividends payable by commercial banks in respect of their prior year profits depends on fulfilment of the minimum criteria laid down in the KNF's dividend policy. As recommended by the KNF, the banks which simultaneously meet the required total capital ratio (TCR), Tier 1 capital ratio and Common Equity Tier 1 (CET 1) ratio, should be able to pay in dividends up to 75% of their profit.

In addition, in the case of banks which have exposures on account of foreign currency loans to households, the dividend payout ratio should be adjusted depending on the share of:

- currency mortgage loans for households in the entire portfolio of receivables from the non-financial sector; and
- currency mortgage loans dating from 2007 and 2008 vs. all currency mortgage loans to households.

All the above factors have a negative impact on the capital available for distribution and, consequently, on the results of the goodwill impairment test.

The minimum solvency ratio imposed by the KNF for Santander Bank Polska S.A. relating to the payment of up to 75% profit distribution, taking into account the additional capital buffer to hedge against the risk connected with the portfolio of currency mortgage loans to households, the buffer for other systemically important institution (OSII) and conservation buffer, was 16.04%.

While the increased capital requirements ensure stability and security for Santander Bank Polska S.A. as they strengthen its capital base, they cause a corresponding reduction in dividends payable to shareholders, which in turn affect the cash-generating unit's value in use.

As at 31 December 2018, no goodwill impairment was identified.

In thousands of PLN

26.Property, plant and equipment

Property, plant & equipment Year 2018	Land and buildings	Financial leasing - land and buildings	Equipment	Transportation means	Other fixed assets	Financial leasing - other fixed assets	Financial leasing - expenditure	Capital expenditures	Total
Gross value - beginning of the period	**826 376**	**38 976**	**716 101**	**88 845**	**226 496**	**-**	**77 989**	**87 506**	**2 062 289**
Property, plant & equipment recognised on	**14 101**	**-**	**3 771**	**-**	**1 171**	**-**	**-**	**-**	**19 043**
Additions from:									
- purchases	-	-	-	-	-	-	31 961	165 484	**197 445**
- leasing	-	-	-	10 279	-	-	-	-	**10 279**
- fixed assets taken for use	12 397	105 157	84 812	-	11 070	3 266	-	-	**216 702**
- transfers	-	-	44	-	-	-	-	-	**44**
Disposals from:									
- sale, liquidation, donation	(100 701)	-	(20 443)	-	(37 678)	-	-	(3)	**(158 825)**
- fixed assets taken for use	-	-	-	-	-	-	(108 423)	(108 280)	**(216 703)**
- transfers	(35 803)	-	-	(9 952)	(139)	-	-	(358)	**(46 252)**
Gross value - end of the period	**716 370**	**144 133**	**784 285**	**89 172**	**200 920**	**3 266**	**1 527**	**144 349**	**2 084 022**
Accumulated depreciation - beginning of the	**(566 774)**	**(2 589)**	**(453 447)**	**(26 722)**	**(191 226)**	**-**	**-**	**-**	**(1 240 758)**
									-
Additions/disposals from:									**-**
- current year amortisation	(24 663)	(2 531)	(72 822)	(10 060)	(11 263)	(177)	-	-	**(121 516)**
- sale, liquidation, donation	79 670	-	20 354	-	36 715	-	-	-	**136 739**
- transfers	20 645	-	(43)	4 532	119	-	-	-	**25 253**
Write down/Reversal of impairment write down	(13 054)	-	-	-	-	-	-	-	**(13 054)**
Accumulated depreciation- end of the period	**(504 176)**	**(5 120)**	**(505 958)**	**(32 250)**	**(165 655)**	**(177)**	**-**	**-**	**(1 213 336)**
Balance sheet value									
Purchase value	716 370	144 133	784 285	89 172	200 920	3 266	1 527	144 349	**2 084 022**
Accumulated depreciation	(504 176)	(5 120)	(505 958)	(32 250)	(165 655)	(177)	-	-	**(1 213 336)**
As at 31 December 2018	**212 194**	**139 013**	**278 327**	**56 922**	**35 265**	**3 089**	**1 527**	**144 349**	**870 686**

In thousands of PLN

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

In thousands of PLN

27.Net deferred tax assets

Deferred tax assets	31.12.2018	Changes to equity*	Changes to financial result	Changes in temporary differences	31.12.2017
Allowance for expected credit losses	645 573	-	196 074	196 074	449 499
Valuation of derivative financial instruments	390 827	-	26 394	26 394	364 433
Valuation of cash flow hedges instruments	15 694	(5 752)	-	(5 752)	21 446
Other provisions	138 734	-	11 019	11 019	127 715
Deferred income	299 897	-	31 647	31 647	268 250
Unrealised interest expenses on loans, deposits and securities	131 558	-	84 781	84 781	46 777
Other negative temporary differences	7 927	-	(12 770)	(12 770)	20 697
Including impact of the implementation of IFRS 9	**45 867**				
Total assets of deferred tax	**1 630 210**	**(5 752)**	**337 145**	**331 393**	**1 298 817**
Deferred tax liabilities	**31.12.2018**	**Changes to equity***	**Changes to financial result**	**Changes in temporary differences**	**31.12.2017**
Valuation of investment securities	(259 109)	(74 018)	3 363	(70 655)	(188 454)
Provisions for retirement allowances	(2 553)	(2 477)	-	(2 477)	(76)
Valuation of derivative financial instruments	(216 336)	-	45 163	45 163	(261 499)
Unrealised interest income on loans, securities and interbank deposits	(161 378)	-	(21 935)	(21 935)	(139 443)
Prepayments regarding amortization of applied investment relief	(1 597)	-	154	154	(1 751)
Difference between balance sheet and taxable value of non-financial assets	(28 330)	-	(36 955)	(36 955)	8 625
Other positive temporary differences	(10 021)	-	(3 669)	(3 669)	(6 352)
Including impact of the implementation of IFRS 9	**8 742**				
Total liabilities deferred tax	**(679 324)**	**(76 495)**	**(13 879)**	**(90 374)**	**(588 950)**
Net deferred tax assets	**950 886**	**(82 247)**	**323 266**	**241 019**	**709 867**

*The changes carried in equity do not reflect the deferred tax effect in relation to the item recognised in non-controlling interests.

As at 31.12.2018 the assets in the calculation of deferred tax assets do not include purchased receivables in the amount of gross PLN 64,831 k and provisions for loans that do not become tax expense in the amount of gross PLN 89,020 k.

In thousands of PLN

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

Deferred tax liabilities	31.12.2017	Changes to equity*	Changes to financial result	Changes in temporary differences	31.12.2016
Revaluation of financial instruments available for sale	(188 454)	(98 026)	-	(98 026)	(90 428)
Provisions for retirement allowances	(76)	1 760	-	1 760	(1 836)
Valuation of derivative financial instruments	(261 499)	-	105 928	105 928	(367 427)
Unrealised interest income on loans, securities and interbank deposits	(139 443)	-	34 049	34 049	(173 492)
Prepayments regarding amortization of applied investment relief	(1 751)	-	125	125	(1 876)
Difference between balance sheet and taxable value of non-financial assets	8 625	-	3 365	3 365	5 260
Other positive temporary differences	(6 352)	-	(4 379)	(4 379)	(1 973)
Total liabilities deferred tax	**(588 950)**	**(96 266)**	**139 088**	**42 822**	**(631 772)**
Net deferred tax assets	**709 867**	**(100 993)**	**(139 447)**	**(240 440)**	**950 307**

*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.

In thousands of PLN

Movements on net deferred tax	31.12.2018	31.12.2017
As at the beginning of the period	709 867	950 307
Impact of the implementation of IFRS 9	54 609	-
Changes recognised in income statement	175 169	(139 447)
Changes recognised in other comprehensive income	(82 247)	(100 993)
Changes on deferred tax as a results of a business combination	93 488	-
Balance at the end of the period	**950 886**	**709 867**

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 2.3.

28. Assets classified as held for sale

Assets classified as held for sale	31.12.2018	31.12.2017
Land and buildings	11 123	8
Total	**11 123**	**8**

29. Other assets

Other assets	31.12.2018	31.12.2017
Interbank and interbranch settlements	59 395	142 701
Sundry debtors	616 481	560 421
Prepayments	63 828	55 225
Repossessed assets	6 849	-
Settlements of stock exchange transactions	25 179	31 711
Other	51	52
Total	**771 783**	**790 110**
of which financial assets*	701 055	734 833

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

30. Deposits from banks

Deposits from banks	31.12.2018	31.12.2017
Term deposits	144 907	64 023
Loans received from banks	-	628 107
Current accounts	895 072	722 318
Total	**1 039 979**	**1 414 448**

Fair value of “Deposits from banks” is presented in Note 42.

In thousands of PLN

Movements in loans received from banks	31.12.2018	31.12.2017
As at the beginning of the period	**628 107**	**664 188**
Increase (due to:)	**15 436**	**4 644**
- loans received	-	-
- interest on loans received	3 774	4 644
- FX differences and other changes	11 662	-
Decrease (due to):	**(643 543)**	**(40 725)**
- repayment of loans	(637 540)	-
- interest repayment	(6 003)	(4 785)
- FX differences and other changes	-	(35 940)
As at the end of the period	**-**	**628 107**

31. Deposits from customers

Deposits from customers	31.12.2018	31.12.2017
Deposits from individuals	**81 591 647**	**59 310 847**
Term deposits	26 315 057	16 321 736
Current accounts	55 180 825	42 948 226
Other	95 765	40 886
Deposits from enterprises	**54 101 104**	**38 702 801**
Term deposits	22 847 784	15 321 645
Current accounts	27 359 966	20 533 707
Loans	3 141 372	2 237 211
Other	751 982	610 238
Deposits from public sector	**3 777 025**	**4 141 874**
Term deposits	1 155 361	1 904 467
Current accounts	2 617 635	2 233 410
Other	4 029	3 997
Total	**139 469 776**	**102 155 522**

As at 31.12.2018 deposits held as collateral totalled PLN 413,246 k (as at 31.12.2017 - PLN 233,625 k).

Fair value of “Deposits from customers” is presented in Note 42.

Movements in loans received from other financial institutions	31.12.2018	31.12.2017
As at the beginning of the period	**2 237 211**	**3 020 931**
Increase (due to:)	**1 449 380**	**47 910**
- loans received	1 368 465	42 200
- interest on loans received	14 581	5 710
- FX differences and other changes	66 334	-
Decrease (due to):	**(545 219)**	**(831 630)**
- repayment of loans	(535 561)	(630 728)
- interest repayment	(9 658)	(5 922)
- FX differences and other changes	-	(194 980)
As at the end of the period	**3 141 372**	**2 237 211**

In thousands of PLN

32. Subordinated liabilities

Subordinated liabilities	Redemption date	Currency	Nominal value
Tranche 1	05.08.2025	EUR	100 000
Tranche 2	03.12.2026	EUR	120 000
Tranche 3	22.05.2027	EUR	137 100
Tranche 4	05.04.2028	PLN	1 000 000

Movements in subordinated liabilities	31.12.2018	31.12.2017
As at the beginning of the period	**1 488 602**	**440 457**
Additions from:	**1 118 873**	**1 133 436**
- drawing of subordinated loan	-	-
- interest on subordinated loans	66 860	33 564
- FX differences	46 735	-
- reclassification *	1 005 278	1 099 872
Disposals from:	**(63 535)**	**(85 291)**
- interest repayment	(63 535)	(27 528)
- FX differences	-	(57 763)
As at the end of the period	**2 543 940**	**1 488 602**
Short-term	16 426	11 257
Long-term (over 1 year)	2 527 514	1 477 345

*Bonds issued by Bank and qualified with the consent of the Polish Financial Supervision Authority to subordinated liabilities.

Other details on these liabilities are disclosed in Note 4.

33. Debt securities in issue

Issuance of debt securities in 2018 (non-matured securities)	Nominal value	Currency	Redemption date
Series G bank securities	500 000	PLN	26.04.2019
Series H bank securities	500 000	PLN	27.09.2019
Series I bank securities	150 000	PLN	21.06.2019
Santander Bank Polska bonds 09/2018	500 000	EUR	20.09.2021

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

In thousands of PLN

Movements in debt securities in issue	31.12.2018	31.12.2017
As at the beginning of the period	**1 240 244**	**1 783 303**
Increase (due to:)	**4 325 756**	**2 049 345**
- debt securities in issue	4 290 794	1 988 788
- interest on debt securities in issue	30 567	44 327
- FX differences	4 395	16 230
Decrease (due to):	**(2 254 031)**	**(2 592 404)**
- debt securities redemption	(1 235 000)	(1 430 000)
- reclassification*	(1 005 278)	(1 099 872)
- FX differences	-	(21 786)
- interest repayment	(13 753)	(40 746)
As at the end of the period	**3 311 969**	**1 240 244**

*Bonds issued by Bank and qualified with the consent of the Polish Financial Supervision Authority to subordinated liabilities.

34. Provisions for off balance sheet credit facilities

Provisions for off balance sheet credit facilities	31.12.2018	31.12.2017
Provisions for financial liabilities to grant loans	43 833	15 069
Provisions for financial guarantees	12 821	8 755
Other provisions	1 489	1 560
Total	**58 143**	**25 384**

Change in provisions for off balance sheet credit facilities	31.12.2018
As at 31.12.2017	**25 384**
Impact of the implementation of IFRS 9	24 489
As at 1.01.2018 (restated)	**49 873**
Increases due to acquisition of demerged part of Deutsche Bank Polska SA	7 945
Provision charge	151 860
Utilization	301
Write back	(151 836)
As at the end of the period	**58 143**
Short-term	37 503
Long-term	20 640

Change in provisions for off balance sheet credit facilities	31.12.2017
As at the beginning of the period	**28 706**
Provision charge	43 265
Utilization	(517)
Write back	(46 070)
As at the end of the period	**25 384**
Short-term	18 425
Long-term	6 959

In thousands of PLN

35. Other provisions

Change in provisions for legal claims	31.12.2018	31.12.2017
As at the beginning of the period	**57 216**	**37 639**
Increases due to acquisition of demerged part of Deutsche Bank Polska SA	5 230	-
Provision charge	89 437	47 497
Utilization	(42 641)	(12 142)
Write back	(25 598)	(15 778)
As at the end of the period	**83 644**	**57 216**

36. Other liabilities

Other liabilities	31.12.2018	31.12.2017
Settlements of stock exchange transactions	17 039	25 851
Interbank settlements	267 632	946 867
Employee provisions	332 361	340 770
Other provisions	3 300	3 300
Sundry creditors	975 422	490 362
Other deferred and suspended income	160 901	168 180
Public and law settlements	101 926	79 254
Accrued liabilities	250 240	204 964
Total	**2 108 821**	**2 259 548**
of which financial liabilities *	1 845 994	2 012 114

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

	Employee provisions			
Change in provisions on 31.12.2018		of which: Provisions for retirement allowances	Other provisions	Total
As at the beginning of the period	**340 770**	***67 225***	**3 300**	**344 070**
Increases due to acquisition of demerged part of Deutsche Bank Polska SA	15 519	*1 439*	-	15 519
Provision charge	303 881	*9 480*	-	303 881
Utilization	(243 279)	*(3 875)*	-	(243 279)
Write back	(84 530)	*(39 918)*	-	(84 530)
Balance at the end of the period	**332 361**	***34 351***	**3 300**	**335 661**
Short-term	298 010	-	3 300	301 310
Long-term	34 351	*34 351*	-	34 351

In thousands of PLN

Change in provisions on 31.12.2017	Employee provisions	of which: Provisions for retirement allowances	Other provisions	Total
As at the beginning of the period	**311 687**	***55 737***	**3 300**	**314 987**
Provision charge	273 688	*13 358*	-	273 688
Utilization	(220 096)	-	-	(220 096)
Write back	(24 509)	*(1 870)*	-	(24 509)
Balance at the end of the period	**340 770**	***67 225***	**3 300**	**344 070**
Short-term	273 545	-	3 300	276 845
Long-term	67 225	*67 225*	-	67 225

Employee related provisions and accruals consists of items outlined in Note 50.

37. Share capital

31.12.2018

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
N	bearer	none	none	2 754 824	27 548
				102 088 305	**1 020 883**

Nominal value of one share is 10 PLN. Series N shares in the increased share capital have been allocated to Deutsche Bank AG in connection with the finalised acquisition of a demerged part of Deutsche Bank Polska SA by Santander Bank Polska SA.

The shareholder having minimum 5% of the total number of votes at the Santander Bank Polska SA General Meeting of Shareholders was Banco Santander with a controlling stake of 67.47%

In thousands of PLN

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 Santander Bank Polska S.A. General Meeting of Shareholders was Banco Santander with a controlling stake of 69.34%

38. Other reserve capital

Other reserve capital	31.12.2018	31.12.2017
General banking risk fund	649 810	649 810
Share premium	8 039 715	7 035 424
Other reserves of which:	9 461 473	8 490 949
Reserve capital	9 290 723	8 320 199
Supplementary capital	170 750	170 750
Total	**18 150 998**	**16 176 183**

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 31.12.2018 includes share scheme charge of PLN 130,869 k, as at 31.12.2017 of PLN 118,423 k.

Other movements of other reserve capital are presented in "movements on equity" for 2018 and 2017.

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 31.12.2018	Total gross	Deferred tax adjustment	Total net
Opening balance, of which:	**879 388**	**(167 085)**	**712 303**
Debt securities measured at fair value through other comprehensive income	292 932	(55 657)	237 275
Equity securities measured at fair value through other comprehensive income	698 932	(132 798)	566 134
Valuation of cash flow hedging instruments	(112 875)	21 447	(91 428)
Actuarial gains on retirement allowances	399	(77)	322
Impact of the implementation of IFRS 9, of which:	**(39 849)**	**7 571**	**(32 278)**
Equity securities measured at fair value through other comprehensive income	(39 849)	7 571	(32 278)
Change in valuation of debt securities measured at fair value through other comprehensive income	405 571	(77 058)	328 513
Transfer from revaluation reserve to profit and loss resulting from the sale of debt securities measured at fair value through other comprehensive income	(26 412)	5 018	(21 394)
Change in valuation of equity securities measured at fair value through other comprehensive income	10 412	(1 978)	8 434
Change in valuation of cash flow hedging instruments	30 274	(5 752)	24 522
Change in valuation of defined benefit plans	13 038	(2 477)	10 561
Closing balance, of which:	**1 272 422**	**(241 761)**	**1 030 661**
Debt securities measured at fair value through other comprehensive income	672 091	(127 697)	544 394
Equity securities measured at fair value through other comprehensive income	669 495	(127 205)	542 290
Valuation of cash flow hedging instruments	(82 601)	15 695	(66 906)
Actuarial gains on retirement allowances	13 437	(2 554)	10 883

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

In thousands of PLN

40. Hedge accounting

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

Fair value hedges

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

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

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

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

The tables below contain details about individual groups of hedge transactions for 31.12.2018 and the comparative period:

Nominal value of hedging instruments as at 31.12.2018	Distribution of nominal values of cash flows					
	up to 1 month	from 1 month to 3 months	from 3 months to 1 year	from 1 year to 5 years	over 5 years	Total
Assets representing derivative hedging	534 000	105 625	893 115	7 258 755	3 660 843	12 452 338
IRS	-	-	200 000	3 413 000	50 000	3 663 000
CIRS	-	-	-	-	43 000	43 000
CCIRS	534 000	105 625	693 115	3 845 755	3 567 843	8 746 338
Liabilities arising from derivative hedging	537 500	107 500	916 245	7 546 114	3 953 865	13 061 224
IRS	-	-	200 000	3 413 000	50 000	3 663 000
CIRS	-	-	-	-	43 000	43 000
CCIRS	537 500	107 500	716 245	4 133 114	3 860 865	9 355 224

Pricing parameters for hedging instruments as at 31.12.2018	up to 1 month	from 1 month to 3 months	from 3 months to 1 year	from 1 year to 5 years	over 5 years
Assets representing derivative hedging					
Average fixed interest rate	1,4650	1,3900	3,5107	1,8957	1,7278
Average exchange rate (CHF/PLN)	3,8166	3,8166	3,8166	3,8166	3,8166
Average exchange rate (EUR/PLN)	4,3000	4,3000	4,3000	4,3000	4,3000
Liabilities arising from derivative hedging					
Average fixed interest rate	(0,3173)	(0,3180)	0,9013	2,4170	(0,4621)
Average exchange rate (CHF/PLN)	3,8166	3,8166	3,8166	3,8166	3,8166
Average exchange rate (EUR/PLN)	4,3000	4,3000	4,3000	4,3000	4,3000

In thousands of PLN

Hedging instruments as at 31.12.2018 designated as fair value hedges	Hedged item: Fixed-coupon bonds	Hedged item: Fixed-rate loan portfolio
Nominal value of hedging instrument	1 856 000	275 000
Fair value measurement of a hedging instrument due to hedged risk including:	(115 874)	(1 359)
Receivables arising from hedging instruments	*-*	*296*
Liabilities arising from hedging instruments	*115 874*	*1 655*
Line item in the statement of financial position that includes the hedging instrument	Hedging derivatives (IRS and OIS)	Hedging derivatives (IRS and OIS)
Hedged risk	Interest rate risk	Interest rate risk
Period over which instruments have impact on the Bank's results	up to 2025	up to 2021

Items subject to fair value hedge accounting as at 31.12.2018	Fixed-coupon bonds	Fixed-rate loan portfolio
Carrying amount of the hedged item, including:		
Assets	*1 856 000*	*275 000*
Liabilities	-	-
Accumulated amount of fair value hedge adjustments on the hedged item included in the statement of comprehensive income and in the carrying amount, including:		
Assets	*118 750*	*1 336*
Liabilities	-	-
Line item in the statement of financial position that includes the hedged instrument	Investment securities	Loans and advances to customers

31.12.2017	Bonds	Loans
Nominal value of hedging instrument	1 979 709	425 000
Measurement to fair value of hedging instrument due to hedged risk	(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

Since January 2016, Santander Bank Polska SA 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 portfolio resulting from movements in market interest rates. Credit margin is excluded from the hedging relationship.

In December 2015, Santander Bank Polska SA 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 income statement account according to the tenors originally agreed for individual hedging relationships. PLN 1,199 k was recognised in the income statement for 2017 and PLN 262 k was reflected in the income statement for 2018.

Cash flow hedging

Santander Bank Polska uses hedge accounting for its future cash flows with respect to commercial and mortgage credit portfolios based on a variable interest rate, in PLN or denominated in EUR, USD and CHF with maximum maturity of 33 years.

The Bank's hedging strategies are designed to protect the Bank's exposures against the risk of changes in the value of future cash flows resulting from interest rate risk 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 and Cross-Currency Interest Rate Swaps. In order to measure hedge effectiveness 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.

Hedging instruments designed as cash flow hedges / hedges of a net investment in a foreign operation as at 31.12.2018	**Hedged item: Portfolio of floating interest rate loans denominated in PLN**	**Hedged item: Portfolio of floating interest rate loans denominated in EUR, USD and CHF**
Nominal value of hedging instrument	1 575 000	9 355 224
Fair value measurement of a hedging instrument due to hedged risk, including:	(8 364)	(91 566)
Receivables arising from hedging instruments	*38 202*	*(113 364)*
Liabilities arising from hedging instruments	*46 566*	*(21 798)*
Line item in the statement of financial position that includes the hedging instrument	Hedging derivatives (IRS, CIRS)	Hedging derivatives (IRS, CIRS)
Change in fair value of the hedging instrument used as the basis for recognising hedge ineffectiveness for the period	(8 364)	(71 527)
Balance of hedging gains or losses of the reporting period that were recognised in other comprehensive income	(8 364)	(91 566)
Value of hedge ineffectiveness recognised in profit or loss	-	20 039
Line item in the income statement that includes the recognised hedge ineffectiveness	Net trading income and revaluation	Net trading income and revaluation
Hedged risk	Interest rate risk	Interest rate risk
Period over which instruments have impact on the Bank's results	up to 2027	up to 2028

Items subject to cash flow hedge accounting as at 31.12.2018	**Portfolio of floating interest rate loans denominated in PLN**	**Portfolio of floating interest rate loans denominated in EUR, USD and CHF**
Change in value of the hedged item used as the basis for recognising hedge ineffectiveness for the period	(8 364)	(91 566)

As of 31.12.2017, the nominal value of the hedging item was PLN 11,457,807 k. Measurement to fair value of the hedging instrument was PLN (112,875) 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.

The non-effective portion of fair value of the cash flow hedge was PLN 10,378 k as of 31.12.2017.

41. Sell-buy-back and buy-sell-back transaction

Santander Bank Polska SA raises funds by selling financial instruments under agreements to repurchase these instruments at future dates at a predetermined price.

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

In thousands of PLN

	31.12.2018 Balance sheet value	31.12.2017 Balance sheet value
Liabilities valued at amortised cost (contains sell-buy-back)	8 233 994	1 479 667
Fair value of securities held as collateral for sell-buy-back/repo transactions	8 252 397	1 480 050
Buy-sell-back transactions	177 482	-
Fair value of securities held for buy-sell-back/reverse repo transactions	175 818	-

Sell-buy-back transactions	**31.12.2018**	**31.12.2017**
Sell-buy-back transactions from banks	173 078	11 379
Sell-buy-back transactions from customers	8 060 916	1 468 288
Total	**8 233 994**	**1 479 667**

Buy-sell-back transactions	**31.12.2018**	**31.12.2017**
Buy-sell-back transactions from banks	177 482	-
Buy-sell-back transactions from customers	-	-
Total	**177 482**	**-**

Securities being the subject of repo and sell-buy-back transactions constituting the Bank's portfolio are not removed from the balance sheet, because the Bank retains all rewards (i.e. interest income on pledged securities) and risks (interest rate risk and the issuer's credit risk) attaching to these assets.

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

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

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

Financial assets which are subject to reverse repo and buy-sell-back transactions represent a security cover accepted by the Bank which the Bank may sell or pledge.

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.

42. 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.

In thousands of PLN

ASSETS	31.12.2018		31.12.2017	
	Book Value	Fair Value	Book Value	Fair Value
Cash and balances with central banks	8 841 902	8 841 902	4 114 801	4 114 801
Loans and advances to banks	2 859 479	2 859 479	2 012 118	2 012 118
Financial assets held for trading	9 776 705	9 776 705	3 421 547	3 421 547
Hedging derivatives	52 554	52 554	146 724	146 724
Loans and advances to customers	117 492 490	118 318 342	90 537 003	91 349 827
- measured at amortised cost	116 056 599	116 882 451	-	-
- measured at fair value through other comprehensive income	366 751	366 751	-	-
- measured at fair value through profit or loss	1 069 140	1 069 140		
Financial assets available for sale	-	-	28 415 812	28 415 812
Investment securities incl.:	36 372 113	36 372 113	6 429 850	6 429 850
- debt securities measured at fair value through other comprehensive income	35 439 836	35 439 836	-	-
- debt securities measured at fair value through profit and loss	131 005	131 005	-	
- equity securities measured at fair value through other comprehensive income	801 272	801 272	-	-
LIABILITIES				
Deposits from banks	1 039 979	1 039 979	2 783 083	2 783 083
Hedging derivatives	903 170	903 170	578 798	578 798
Financial liabilities held for trading	1 238 002	1 238 002	1 237 704	1 237 704
Deposits from customers	139 469 776	139 478 610	111 481 135	111 496 805
Subordinated liabilities	2 543 940	2 531 230	1 488 602	1 500 989

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

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

The Bank has financial instruments which in accordance with the IFRS are not carried at fair value in the 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 III 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.

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

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

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

As at 31.12.2018 and in the comparable periods the Bank made the following classification of its financial instruments measured at fair value in the statement of financial position:

Level I (active market quotations): debt, equity and derivative financial instruments which at the balance sheet date were measured using the prices quoted in the active market. The Bank allocates to this level fixed-rate State Treasury bonds, treasury bills, 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. This level includes also part of credit cards portfolio and loans and advances subject to underwriting, i.e. portion of credit exposures that are planned to be sold before maturity for reasons other than increase in credit risk.

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.

Sensitivity analysis of the credit cards portfolio

The analysis covered the population of credit cards measured at fair value as at the end of 2018 for the interest rate changes.

	Fair value in respective scenarios				
in PLN m	**baseline**	**1 p.p. decrease in interest rates**	**2 p.p. decrease in interest rates**	**1 p.p. increase in interest rates**	**2 p.p. increase in interest rates**
Total	962,8	961,0	958,5	962,9	963,1

The fair value of the credit card portfolio was calculated for individual scenarios, taking into account the modified interest rate projections used both for calculating interest and for discounting cash flows.

As at 31.12.2018 and in the comparable periods the Bank classified its financial instruments to the following fair value levels:

In thousands of PLN

31.12.2018	Level I	Level II	Level III	Total
Financial assets				
Financial assets held for trading	8 688 624	1 088 081	-	9 776 705
Hedging derivatives	-	52 554	-	52 554
Loans and advances to customers measured at fair value through other comprehensive income	-	-	366 751	366 751
Loans and advances to customers measured at fair value through profit or loss	-	90 300	978 840	1 069 140
Debt securities measured at fair value through OCI	35 412 566	-	27 270	35 439 836
Debt securities measured at fair value through profit and loss	-	-	131 005	131 005
Equity securities measured at fair value through OCI	-	-	801 272	801 272
Total	**44 101 190**	**1 230 935**	**2 305 138**	**47 637 263**
Financial liabilities				
Financial liabilities held for trading	175 689	1 062 313	-	1 238 002
Hedging derivatives		903 170	-	903 170
Total	**175 689**	**1 965 483**	**-**	**2 141 172**

31.12.2017	Level I	Level II	Level III	Total
Financial assets				
Financial assets held for trading	2 189 111	1 231 989	447	3 421 547
Hedging derivatives	-	146 724	-	146 724
Financial investment assets - debt securities	24 856 947	-	32 532	24 889 479
Financial investment assets - equity securities	-	-	894 550	894 550
Total	**27 046 058**	**1 378 713**	**927 529**	**29 352 300**
Financial liabilities				
Financial liabilities held for trading	-	1 263 859	-	1 263 859
Hedging derivatives	-	578 798	-	578 798
Total	**-**	**1 842 657**	**-**	**1 842 657**

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					
31.12.2018	Financial assets held for trading	Loans and advances to customers measured at fair value through profit and loss	Loans and advances to customers measured at fair value through OCI	Debt securities measured at fair value through other comprehensive income	Debt securities measured at fair value through profit and loss	Equity securities measured at fair value through other comprehensi ve income
As at the beginning of the period	**447**	**-**	**-**	**32 532**	**-**	**894 550**
Impact of the implementation of IFRS 9	**-**	**1 067 920**	**-**	**-**	**90 175**	**(15 718)**
Profit or losses						
recognised in income statement	*(26)*	*15 355*	-	*-*	*12 120*	*-*
recognised in equity (OCI)	*-*	*-*	-	*-*	*-*	*45 472*
Purchase	-	17 294	366 751	-	20 013	2 604
Sale	(421)	-	-	-	-	(316)
Matured	-	(18 368)	-	(5 262)	-	-
Transfer	-	(90 300)	-	-	-	(125 320)
Other	-	(13 061)	-	-	8 697	-
As at the end of the period	**-**	**978 840**	**366 751**	**27 270**	**131 005**	**801 272**

In thousands of PLN

Level III	Financial assets			Financial liabilities
31.12.2017	**Financial assets held for trading**	**Financial investment assets - debt securities**	**Financial investment assets - equity securities**	**Financial liabilities held for trading**
As at the beginning of the period	**251**	**38 240**	**842 647**	**-**
Profit or losses				
recognised in income statement	*(29)*	-	-	-
recognised in equity	-	-	*68 267*	-
Purchase	1 057	-	2 036	-
Sale	(832)	-	(18 400)	-
Matured	-	-	-	-
Impairment	-	-	-	-
Other	-	(5 708)	-	-
As at the end of the period	**447**	**32 532**	**894 550**	**-**

43. Contingent liabilities

Significant court proceedings

As at 31.12.2018, no proceedings were instituted by court or by state administration agencies with relation to liabilities or receivables made by or against the Bank amounting to a minimum of 10% of the Bank's equity.

The value of all litigation amounts to PLN 882,136 k, which is ca. 3.7% of the Bank's equity. This amount includes PLN 387,362 k claimed by the Bank, PLN 494,774 k in claims against the Bank. There were no litigations for bankruptcy or arrangement.

On 20.10.2017, Santander Bank Polska SA received a notice of a class action instituted by the borrowers who had loans indexed to the CHF, originated by the former Kredyt Bank SA. The total value of the claim, estimated based on available documents as at 31.12.2017, was PLN 32.3 m. On 27.02.2018, Bank received a notice of broaden a class action by next groups of borrowers and the total value of the claim increased to PLN 47.0 m. The Bank responded to the claim. At the date of preparing the Financial Statements, we were waiting for the court to decide if the case can be heard as a class action.

In 2018 the amount of significant court proceedings which had been completed amounted to PLN 166,553 k.

As at 31.12.2018, the value of provisions for legal risks, for court cases against Santander Bank Polska SA was PLN 83,644 k. In 37 cases against the Bank, where the claim value was high, a provision of PLN 37,340 k was raised and in 1 case claimed by the Bank, a provision of PLN 26,245 k was raised.

As at 31.12.2017, no proceedings were instituted by court or by state administration agencies with relation to liabilities or receivables made by or against the Bank amounting to a minimum of 10% of the Bank's equity.

The value of all litigation amounts to PLN 684,502 k, which is ca. 3.28% of the Bank's equity. This amount includes PLN 371,189 k claimed by the Bank, PLN 313,313 k in claims against the Bank. There were no litigations for bankruptcy or arrangement.

In 2017 the amount of significant court proceedings which had been completed amounted to PLN 195,733 k.

As at 31.12.2017, the value of provisions for legal risks, for court cases against Santander Bank Polska SA was PLN 57,216 k. In 10 cases against the Bank, where the claim value was high, a provision of PLN 40,983 k was raised.

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.

In thousands of PLN

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	Stage 1	Stage 2	Stage 3	31.12.2018	31.12.2017
Liabilities sanctioned					
- financial	**26 792 453**	**303 656**	**76 549**	**27 172 658**	**21 409 105**
- credit lines	22 634 188	273 974	70 886	22 979 048	17 718 025
- credit cards debits	3 358 077	17 927	5 663	3 381 667	3 049 456
- import letters of credit	788 817	11 755	-	800 572	633 773
- term deposits with future commencement term	11 371	-	-	11 371	7 851
- guarantees	**7 432 336**	**141 102**	**27 530**	**7 600 968**	**4 948 545**
Provision for off-balance sheet liabilities	**(15 733)**	**(10 013)**	**(32 397)**	**(58 143)**	**(25 384)**
Total	**34 209 056**	**434 745**	**71 682**	**34 715 483**	**26 332 266**

44. 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, Santander Bank Polska SA applied 0.50% (i.e 0,55% in 2017) of funds deposited in all accounts with the bank, being the basis for calculating the obligatory reserve.

As at 31.12.2018, assets allocated to that end totalled PLN 618 586 k compared with PLN 561 897 k a year before.

In 2018, deposits opened with financial institutions to secure the value of transactions totalled PLN 1 239 687 (PLN 798,350k as at 31.12.2017).

In 2018, the Santander Bank Polska SA accepted PLN 148 118 k worth of deposits securing transactions (vs. PLN 348 808 k in 2017).

Other assets pledged and liabilities accepted as collateral are disclosed in Notes 31 and 41.

45. Finance and operating leases

Santander Bank Polska SA acts as a lessee in finance lease agreements where the lessor side is represented by Santander Bank Polska leasing subsidiaries.

Finance leases

Finance leases gross liabilities - maturity	31.12.2018	31.12.2017
less than 1 year	26 608	13 615
between 1 and 5 years	30 437	40 043
over 5 years	133 908	(27)
Total	**190 953**	**53 631**

Present value of minimum lease payments - maturity	31.12.2018	31.12.2017
less than 1 year	26 391	13 419
between 1 and 5 years	29 003	38 035
over 5 years	111 419	-
Total	**166 813**	**51 454**

In thousands of PLN

Reconciliation between the finance lease receivables and the present value of minimum lease payments	31.12.2018	31.12.2017
Finance leases gross liabilities	190 953	53 631
Unrealised financial costs	(24 140)	(2 177)
Present value of minimum lease payments	**166 813**	**51 454**

Financial leaseback

Finance leaseback gross liabilities - maturity	31.12.2018	31.12.2017
less than 1 year	1 954	424
between 1 and 5 years	1 708	1 697
over 5 years	30 584	30 415
Total	**34 246**	**32 536**

Present value of minimum lease payments - maturity	31.12.2018	31.12.2017
less than 1 year	1 951	420
between 1 and 5 years	1 632	1 621
over 5 years	26 394	26 225
Total	**29 977**	**28 266**

Reconciliation between the finance lease receivables and the present value of minimum lease payments	31.12.2018	31.12.2017
Finance leaseback gross liabilities	34 246	32 536
Unrealised financial costs	(4 269)	(4 270)
Present value of minimum lease payments	**29 977**	**28 266**

Operating leases

Santander Bank Polska SA leases offices in compliance with operational leasing agreements. As a standard, agreements are concluded for a period over 5 years. A small part of the offices is subleased outside the Bank. In 2018 and 2017 rentals totalled PLN 179,631 k and PLN 186,831 k, respectively. These payments are presented in the profit and loss account under "Operating expenses".

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

Lease payments - maturity	31.12.2018	31.12.2017
less than 1 year	173 513	176 091
between 1 and 5 years	455 702	451 979
over 5 years	143 595	384 471
Total	**772 810**	**1 012 541**

46. Statement of cash flows - additional information

The table below contains information on cash and cash equivalents in the cash flows statement of Santander Bank Polska SA.

In thousands of PLN

Cash and cash equivalents	31.12.2018	31.12.2017
Cash and balances with central banks	8 790 829	4 114 801
Receivables from interbank deposits*	2 936 161	2 011 387
Debt securities measured at fair value through other comprehensive income*	5 999 249	1 379 839
Cash and cash equivalents acquired in acquisition of demerged part of Deutsche Bank Polska SA and subordinated entities	51 488	-
Total	**17 777 727**	**7 506 027**
The impact of changes in currency exchange rates during the financial year on cash and cash equivalents	39 697	(89 985)

* financial assets with initial maturity below three months

Santander Bank Polska SA has restricted cash in the form of a mandatory reserve held on account with the Central Bank.

In the periods presented in the financial statement of Santander Bank Polska SA has received and made interest payments in the following amounts:

Interests received and interests paid	01.01.2018-31.12.2018	01.01.2017-31.12.2017
Interests received, including:	**5 200 626**	**4 697 242**
- operating activities	4 510 216	4 096 842
- investing activities	690 410	600 400
Interests paid, including:	**(1 232 843)**	**(894 898)**
- operating activities	(1 139 894)	(815 917)
- financing activities	(92 949)	(78 981)

The table below shows acquisition of demarged part of Deutsche Bank Polska SA:

Acquisition of organized part of Deutsche Bank Polska SA and subordinated entities net of cash acquired	09.11.2018
Price paid by cash for the acquisition of demerged part of Deutsche Bank Polska SA and subordinated entities	257 960
- including the acquisition of DB Securities SA	20 000
Cash and balances with central banks	(51 073)
Receivables from interbank deposits*	(415)
Total	**206 472**

* financial assets with initial maturity below three months

47. Related parties

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

In thousands of PLN

Transactions with subsidiaries	31.12.2018	31.12.2017
Assets	**9 462 343**	**8 867 211**
Loans and advances to banks	110 434	28 948
Financial assets held for trading	6 855	5 438
Loans and advances to customers	9 342 562	8 816 531
Other assets	2 492	16 294
Liabilities	**708 452**	**479 234**
Deposits from banks	30 595	129 461
Financial liabilities held for trading	4 742	26 169
Deposits from customers	476 177	154 529
Other liabilities	196 938	169 075
Income	**251 091**	**351 121**
Interest income	204 459	174 332
Fee and commission income	21 117	167 320
Other operating income	9 451	9 469
Net trading income and revaluation	16 064	-
Expenses	**9 261**	**52 376**
Interest expenses	7 383	4 850
Fee and commission expenses	2 025	2 228
Net trading income and revaluation	-	45 195
Operating expenses incl.:	(147)	103
Bank's staff, operating expenses and management costs	*(229)*	*91*
Other	*82*	*12*
Contingent Liabilities	**5 495 274**	**1 185 390**
Sanctioned:	5 495 274	1 185 390
- financial	*3 499 375*	*1 121 936*
- guarantees	*1 995 899*	*63 454*
Derivatives' Nominal Values	**2 672 042**	**2 727 340**
FX swap – purchased amounts	-	89 180
FX swap – sold amounts	-	92 010
Cross-currency interest rate swap – purchased amounts	267 162	249 704
Cross-currency interest rate swap – sold amounts	270 900	270 900
Single-currency interest rate swap	2 132 111	2 025 546
Spot-purchased	934	-
Spot-sold	935	-

Transactions with associates	31.12.2018	31.12.2017
Liabilities	**105 519**	**120 146**
Deposits from customers	105 519	90 102
Sell-buy-back transactions	-	30 044
Income	**37 882**	**13 451**
Fee and commission income	37 882	13 451
Expenses	**3 239**	**3 713**
Interest expense	1 512	1 806
Fee and commission expense	113	79
Operating expenses incl.:	1 614	1 828
General and administrative expenses	*1 614*	*1 828*

In thousands of PLN

Transactions with Santander Group	with the parent company 31.12.2018	with the parent company 31.12.2017	with other entities 31.12.2018	with other entities 31.12.2017
Assets	**1 364 172**	**598 411**	**6 416**	**9 854**
Loans and advances to banks, incl:	955 508	308 691	6 398	9 831
Loans and advances	*583 784*	*95 993*	*-*	*-*
Current accounts	*371 724*	*212 698*	*6 398*	*9 831*
Financial assets held for trading	407 364	282 036	-	-
Hedging derivatives	1 085	7 469	-	-
Other assets	215	215	18	23
Liabilities	**784 526**	**403 807**	**127 015**	**86 398**
Deposits from banks incl.:	294 866	62 996	10 721	23 539
Current accounts	*294 866*	*62 996*	*10 721*	*23 539*
Hedging derivatives	8 634	-	-	-
Financial liabilities held for trading	477 638	322 933	-	-
Deposits from customers	-	-	100 130	52 577
Other liabilities	3 388	17 878	16 164	10 282
Income	**120 921**	**14 914**	**16 324**	**394**
Interest income	11 036	11 321	235	95
Fee and commission income	2 595	3 593	414	299
Other operating income	5	-	94	-
Net trading income and revaluation	107 285	-	15 581	-
Expenses	**23 674**	**94 960**	**43 102**	**73 404**
Interest expense	1 574	1 050	459	960
Fee and commission expense	1 222	1 171	5	1
Net trading income and revaluation	-	74 862	-	57 672
Operating expenses incl.:	20 878	17 877	42 638	14 771
Staff, Operating expenses and management costs	*20 877*	*17 877*	*42 636*	*14 763*
Other operating expenses	*1*	*-*	*2*	*8*
Derivatives' nominal values	**84 303 789**	**51 859 866**	**-**	**-**
Cross-currency interest rate swap (CIRS) – purchased	4 116 460	3 478 300	-	-
Cross-currency interest rate swap (CIRS) – sold	4 012 672	3 414 864	-	-
Single-currency interest rate swap	38 879 678	18 298 033	-	-
Forward rate agreement (FRA)	4 494 400	-	-	-
Options interest rate	6 543 672	8 001 216	-	-
FX swap – purchased amounts	7 211 538	4 719 697	-	-
FX swap – sold amounts	7 198 628	4 762 299	-	-
FX options -purchased CALL	2 535 591	2 010 291	-	-
FX options -purchased PUT	2 540 293	1 950 686	-	-
FX options -sold CALL	3 086 738	2 026 149	-	-
FX options -sold PUT	3 262 996	2 211 749	-	-
Spot-purchased	79 412	162 894	-	-
Spot-sold	79 374	163 182	-	-
Forward- purchased	100	138 027	-	-
Forward- sold	100	135 771	-	-
Capital derivatives contract - purchased	262 137	386 708	-	-

In thousands of PLN

Transactions with key management personnel

Remuneration of Santander Management Board Members, Supervisory Board Members and key management.

Loans and advances granted to key management personnel

As at 31.12.2018 and 31.12.2017 members of the Management Board were bound by the non-compete agreements which remain in force after they step down from their function. If a Member of the Management Board is removed from their function or not appointed for another term, he/she is entitled to a once-off severance pay. The severance pay does not apply if the person accepts another function in the Bank.

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

Remuneration of Management Board Members and Key Management	Management Board Members		Key Management	
	2018	2017	2018	2017
Renumeration	12 573	12 774	24 951	21 824
Additional benefits (e.g among others, life insurance cover without pension option, medical cover, travel expenses and school fees)	1 066	1 136	544	951
The awards paid in 2018 and 2017 *	9 940	8 186	13 859	8 906
Equivalent paid for unused annual leave	146	125	29	-
Additional compensation for termination of the contract and the non-competition clause	1 105	-	107	-
Loans and advances made by the Bank to the Members of the Management Board/Key Management and to their relatives	10 103	11 054	25 181	22 683
Deposits from The Management Board/Key management and their relatives	13 714	17 328	26 169	13 106
Provisions for retirement benefits and provision for unused holidays	1 184	797	1 868	1 119
The number of conditional rights to shares	27 220	34 670	38 732	37 274

* included part of the award for 2017, 2016, 2015 and 2014 which was conditional and deferred in time

The category of key management personnel includes the persons covered by the principles outlined in the "Santander Bank Polska Group Remuneration Policy".

Santander Bank Polska SA applies the "Santander Bank Polska Group Remuneration Policy". 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 2018, the total remuneration paid to the Supervisory Board Members of Santander Bank Polska totalled PLN 1,432 k (PLN 1,556 k in 2017). Mr John Power received remuneration for the supervision over acquisition of a carve-out business of Deutsche Bank Poland by Santander Bank Polska in the amount of PLN 853.5 k (84.0 k in 2017). Mr John Power received remuneration of PLN 37.3 k from subsidiaries for his membership in their Supervisory Boards (PLN 28.7 k in 2017).

48. Acquisitions and disposals of investments in subsidiaries and associates

Acquisition of a carve-out of Deutsche Bank Polska SA

On 09.11.2018, the transaction of acquisition of a carve-out of Deutsche Bank SA took place and taking control over a related entity Deutsche Bank Securities by Santander Bank Polska SA.

Details are described in Note 49.

Registration of Santander Leasing Poland Securitisation 01

On 30.08.2018, a subsidiary of Santander Leasing Poland Securitisation 01 Designated Company seated in Dublin was registered under Irish law. This is a special-purpose vehicle formed for the purpose of securitisation of the leasing and loans receivables. As the control criteria set out in IFRS 10.4 are met, the company is considered as an entity controlled by Santander Leasing SA.

Liquidation of Giełdokracja sp. z o.o.

On 05.03.2018 Giełdokracja sp. z o.o. was liquidated. Final settlement of the company's assets and liabilities was made, the loss on the liquidation of the company is PLN 65 k.

Contribution in kind of Santander F24 SA (formerly BZ WBK Nieruchomości SA) shares to Santander Finanse sp. z o.o.

On 24.11.2017, Santander Bank Polska SA made contribution in kind of Santander F24 SA (formerly BZ WBK Nieruchomości SA) shares to Santander Finanse sp. z o.o. to cover the acquisition of Santander Finanse sp. z o.o. shares by Santander Bank Polska SA.

In the second half of 2017, Santander F24 SA 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 Santander Bank Polska Group whereby Santander F24 SA 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 (KRS) was registered increase of share capital Santander 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 SA, 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. 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 Santander Leasing SA and BZWBK Lease SA.

On 28.02.2017, Santander Leasing SA and BZ WBK Lease SA merged.

The companies merged by way of absorption of BZ WBK Lease SA (the absorbed entity) by Santander Leasing SA (the absorbing entity). All the assets of BZ WBK Lease SA were transferred to Santander Leasing SA . In connection with the merger, BZ WBK Lease SA ceased to exist legally, while Santander Leasing SA ,being the absorbing entity, assumed, under the law, all the rights and obligations of the absorbed entity. As a result, Santander Leasing SA continues business operations which previously were carried out by BZ WBK Lease SA and assumed, under the law, all the rights and obligations of absorbed BZ WBK Lease SA.

In thousands of PLN

49. Acquisition of an organized part of the enterprise

Summary of acquisition

On 09 November 2018 the Santander Bank Polska (the Bank) acquired an organized part of business of Deutsche Bank Polska S.A. (DBPL) consisting of DBPL's retail and SME banking, private banking, business banking, as well as 100% of shares in DB Securities S.A. a brokerage house of DBPL group. Pursuant to the Transaction Agreement, the branch network along with the external sales channels - vendors and agents of DBPL has been integrated with Santander Bank's current network. Apart from that investment product distribution and asset management businesses were transferred along with the Acquired Business. Transaction excluded corporate and investment banking business and retail FX mortgages that will remain in DBPL.

Business rationales of the transaction

The acquisition of organized part of enterprise Deutsche Bank Polska S.A. enables Santander Bank Polska SA to improve its position in the Polish banking sector throughout of acquisition of attractive, low risk customer base and by increasing its presence in affluent customers, private banking, and SME segments. Provides also reinforcement of Bank's sales network in regions of strategical significance (e.g. Silesia). Moreover, in the opinion of the management, the business combination will effects in significant cost and income synergies mostly resulting from potential upside from cheaper funding and cross-selling opportunities.

After the acquisition Santander Bank Polska Group increased its loan market share to 12.0% (unaudited information) to PLN 137 bn of net loans and advances to customers. From the segmentation point of view, transaction provided inflow of attractive client base and highly complementary business franchise. It significantly improved the Bank's position in the growing Private Banking, Select and Mid Market segments (+95 k clients), and also in the mass segment with new 226 k clients. In addition, new 35 k SME clients have been acquired.

As a result exclusion from transaction perimeter FX denominated mortgages, transaction reduced Santander Bank Polska FX mortgage loans weighting to 9.2%.

Preliminary purchase price

According to the terms and conditions of the agreement signed on the 14th of December 2017, parties established the preliminary purchase price of PLN 1,289,799,000, which can be broken down into:

1. Transferred BD Business Preliminary Purchase Price of PLN 1,269,799,000; and
2. DB Securities Preliminary Purchase Price of PLN 20,000,000.

Transferred BD Business Preliminary Purchase Price of organized part of DB has been calculated based on its initial level of risk weighted assets multiplied by 13.875% and discounted by the agreed multiple of 0.60x.

The DB Securities S A. Preliminary Purchase Price of PLN 20,000,000 has been determined by the Parties on the basis of the DB Securities S.A. Financials and an agreed discount to the Base Equity.

Preliminary Purchase Price was paid in cash in the amount of PLN 257,959,800 representing 20% of total established price whereas the rest of consideration has been transferred in form of 2,754,824 Demerger Shares of Acquirer. The number of the shares issued as part of the consideration was based on their fair value, being an arithmetical average of daily prices weighted by trade volume of Acquiring Bank's shares which were traded on the Warsaw Stock Exchange during the period between 14 November 2017 and 13 December 2017, and totaled PLN 374.56.

Details of the purchase consideration are as follows:

Purchase consideration	
Cash paid	257 960
Oridinary shares issued	1 031 839
Total purchase consideration	**1 289 799**

In thousands of PLN

Final Purchase Price

Due to the fact that the date of the initial price determination was significantly distant from the date of transfer of balances being the subject of the contract, the parties agreed that the final payment price will be equal to the preliminary purchase price, adjusted by the final level of the RWA price component as well as the impact of changes in significant business volumes such as loans, customer deposits and customer funds under management. Conditional is, the final settlement of the price paid is expected by the end of March 2019.

Analysis of acquired assets and liabilities on a merger day

As at the date of issuance of the report, Santander Bank Polska S.A. performed valuation process related to the acquisition of an organized part of Deutsche Bank Polska S.A. and Deutsche Bank Securities S.A. The valuation included review of balance sheet items (such as loans and advances to customers, non-current assets, deposits from customers and banks) and contingent liabilities. Apart from that, during the acquisition Bank recognized additional assets that meet the conditions for recognition as intangible assets. These assets resulted from the revaluation of customer relationships created in DBPL on deposit products (PLN 142.2m) and investment and insurance products (PLN 50.4m). Details of approach used to calculate above mentioned balances are described in the section "Significant judgements and valuation assumptions".

The depreciation of the intangible assets shall be allocated to the profit and loss accounts on a non-linear basis over their useful lives, directly linked to life of underlying products.

The following table shows the fair value of acquired assets and liabilities.

as at: 09.11.2018	Organized part of the DB
ASSETS	
Cash and balances with central banks	51 073
Loans and advances to banks	405
Financial assets held for trading	24 049
Loans and advances to customers measured at amortised cost	18 781 513
- Mortgage loans	8 442 540
- Consumer loans	3 092 067
- Business loans	7 246 906
Acquired shares in DB Securities	20 000
Investment securities incl.:	83 090
- debt securities measured at fair value through other comprehensive income	63 077
- debt securities measured at fair value through profit and loss	20 013
Intangible assets	195 977
Property, plant and equipment	19 043
Net deferred tax assets	52 972
Other assets	37 017
Total assets	19 265 139
LIABILITIES	
Deposits from banks	4 430 226
Financial liabilities held for trading	12 122
Deposits from customers	13 041 354
Provisions for off balance sheet credit risk	7 945
Other provisions	5 230
Other liabilities	113 698
Total liabilities	17 610 575
Net assets acquired	**1 654 564**

Significant judgements and valuation assumptions

1. Recognized intangible assets

As a result of performed valuation process Santander Bank Polska recognized following acquisition intangible assets.

Core Deposit Intangible (CDI)

CDI is defined as a current value of the difference between the current account's cost of financing and the alternative cost of financing that a bank would have had to bear if it did not own such portfolio of accounts. The fair value of the CDI was estimated with income approach. Calculated cash flows reflecting the cost savings were based on the difference between the forecasted costs of the acquired accounts and the costs of alternative market funds during the average life period of acquired accounts. The cost of alternative funds was estimated on the basis of interest rates market benchmarks for PLN and EUR funding. Computed cash flows for subsequent years were discounted with the appropriate discount rate as of the acquisition date.

Customer relationships intangible - insurance & investments products

The value of customer relationships is result from by the fact that such relationships provide Santander Bank Polska with numerous benefits such as potentially reduced selling and marketing cost, enhanced logistic capabilities between the Bank and the customer, and a working rapport between the bank and the customer. The fair value of the intangible asset was estimated with income approach. The value was determined on the basis of discounted future cash flows, resulting from the surplus revenue, generated by the Bank holding the given intangible asset. The contributory amount of general expenses (including depreciation) and other charges is deducted from such defined cash flows for each year of expected relationship. The received cash flows for each year are then discounted at the cost of equity increased by an appropriate premium to constitute the fair the value of intangible asset.

2. Acquired loans and advances from customers

Fair value estimation as of the acquisition date was based on data of acquired portfolio transferred to Santander Bank Polska in the process of migration. Valuation of loans and advances to customers was conducted taking into account the risk characteristics of acquired portfolios.

Fair value adjustment on performing loans

The measurement of the fair value of non-performing loans coverd by portfolio and individual provisions takes place in accordance with the discounted cash flow method (DCF). Majority of adjustment resulted mainly from acquired Mortgage and SME portfolio, where contractual interest rate margins are lower than interest rates currently observed on the market. Newly acquired performing loans has been classified as Stage 1 portfolio.

Fair value adjustment on non-performing loans

The measurement of the fair value of non-performing loans coverd by portfolio and individual provisions takes place in accordance with the discounted cash flow method (DCF). For non-performing exposures assessed individually Santander Bank Polska estimated expected future cash flows on a case by case basis. In case of provisions, future value of recoveries resulting from nonperforming exposures subject to collective valuation were based on recovery rate curves. Expected cash flows for non-performing exposures have been discounted using appropriate discount rates. Acquired NPL loans have been classified as POCI portfolio.

On the transaction date, the amount of estimated contractual cash flows relating to the acquired credit receivables was PLN 19 549 631 k , while the estimated, non-discounted value of irrecoverable cash flows was PLN 602,584k

3. Significant acquisition related liabilities

Onerous lease contracts

Bank acquired rent agreements with conditions worse than the market rates as of the acquisition date, therefore additional liability resulting from such onerous contract had been recognized. Estimation of the fair value of rent agreements for properties (branches) rented by Demerged Bank has been conducted with an income approach based on differences between market rent fees per squared meter for particular locations and actual rent fees from agreements signed by Demerged Bank. Differences were then discounted by risk free rate to the acquisition date during the remaining rental contract period.

In thousands of PLN

Other liabilities recognized

Apart from the adjustment above Bank recognized a number of minor provisions or cost accruals connected with expected litigations, debt enforcement proceedings or differences in accounting estimates related to employee provisions and accruals. Value of liabilities was estimated on the basis of future expected outflow of funds. As recognized liabilities are short term in its nature, no discounting of cash flows were implied.

Non-controlling interest

Due to the fact that the business combination considered acquisition of an organized part of business, no non-controlling interests were recognized in the consolidated financial statements of Santander Bank Polska Group.

Calculation of the preliminary gain of the acquisition

As at the date of issuance of the report, Santander Bank Polska SA performed preliminary settlement of the acquisition of an organized part of business of Deutsche Bank Polska S.A. and DB Securities S.A. Table below presents calculation of the preliminary gain from acquisition, which is disclosed it the 'Gain on acquisition of enterprise' in the profit and loss accounts for the year ended 2018.

Preliminary gain from acquisition	
Consideration paid	1 289 799
less: fair value of identifiable net assets	(1 654 564)
Total	**(364 765)**

As part of the settlement of the transaction, the Bank identified a gain on acquisition of enterprise. In accordance with the requirements of IFRS 3, before recognizing the profit, the Bank again assessed the correctness of the identification of acquired assets and liabilities assumed. As a result of this analysis, it was found that all assets and liabilities that were identified at an earlier stage are complete and correctly identified. Then, the correctness of the procedures applied to the valuation of the possible for identification acquired assets and assumed liabilities as well as the consideration were re-assessed. Additionally Bank re-assessed the material parameters used in the fair value models, in particular the reference margins for the acquired credit base and the discount rates used in the models. As a result of the work carried out, in the opinion of the Management Board, the valuation appropriately reflects all information available as at the acquisition date, and as a result it is reasonable to recognize the gain on acquisition of enterprise.

Revenue and profit contribution

As a consequence of the purchase agreement for the organized part of Deutsche Bank Polska SA:

- Neither the opening balance data as at 01/01/2018, nor financial results of the separated part for the period ended 09/11/2018 were not available for the Buyer,
- It was not possible to prepare material accounting estimates affecting the results of the operation of a separated part of the enterprise for the period preceding the acquisition,
- There were significant differences in costs of funding allocated to Transferred DB business by the Seller, and potentially provided by Santander Bank Polska S.A.
- It was impossible to asses influence of significant operational aspects on the separate part of the enterprise,
- The relatively short time between the transaction date and the end of 2018, does not give reliable basis to use extrapolate this financial results on pre-acquisition period of 2018.

In view of the above restrictions, Santander Bank Polska SA was not able to determine and disclose the impact of the acquired operations on the pre-acquisition results of the current reporting period.

In thousands of PLN

Purchase consideration – impact on the cash flow statement

Outflow of cash to acquired assets and liabilities, net of cash acquired	
Cash consideration	(257 960)
less: Balances acquired	51 488
Cash	51 073
Current accounts	415
Other cash equivalents	-
Net outflow of cash, investing activities	**(206 472)**

Acquisition-related costs

In 2018 Santander Bank Polska SA incurred acquisition-related costs of PLN 108,870 k which were a result of a process of preparation of internal resources and capabilities to execute overnight data migration of customer records from demerged business. These costs were included in the administrative expenses in profit or loss accounts and in operating cash flows in the statement of cash flows. Table below presents an functional break down of the above mentioned costs:

Salaries and bonuses	26 529
Consulting fees	30 061
IT costs	10 330
Admitistrative expences	23 364
Marketing and communication	12 899
Other costs	5 687
Total	**108 870**

In addition, Santander Bank Polska SA recognized additional allowance for impairment receivables taken over in the purchase transaction for the amount of PLN 130,473 k.

50.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 Santander Bank Polska creates the following types of provisions:

Provisions for unused holidays

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

Provisions for employee bonuses

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

Provisions for retirement allowances

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

- retirement benefits,
- 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 and pension benefits and death-in-service benefits is dependent on length of service and amount of remuneration received by the employee. 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

In thousands of PLN

probability of an individual get to the retirement age or die while working is determined using the multiple decrement model, taking into consideration the following risks: possibility of dismissal from service, risk of total disability to work and risk of death.

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

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

The principal actuarial assumptions as at 31.12. 2018 are as follows:

- the discount rate at the level of 3.15% (3.3% as at 31.12.2017),
- the future salary growth rate at the level of 2.0% (2.0% as at 31.12.2017),
- the probable number of leaving employees calculated on the basis of historical data concerning personnel rotation in the Bank,
- the mortality adopted in accordance with Life Expectancy Tables for men and women, published the Central Statistical Office, adequately adjusted on the basis of historical data of the Bank.

Reconciliation of the present value of defined benefit plans obligations

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

	31.12.2018	31.12.2017
As at the beginning of the period	**67 225**	**55 737**
Provision acquired in a business combination	4 670	-
Current service cost	2 163	308
Prior service cost	(28 356)	-
Interest expense	1 687	1 916
Actuarial gains and losses	(13 038)	9 264
Balance at the end of the period	**34 351**	**67 225**

Sensivity 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 percentage point as at 31.12.2018.

Defined benefit plan obligations	1 percent increase	1 percent decrease
Discount rate	13,13%	9,06%
Future salary growth rate	-3,57%	13,26%

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 percentage point as at 31.12.2017.

Defined benefit plan obligations	1 percent increase	1 percent decrease
Discount rate	9,00%	-9,78%
Future salary growth rate	-9,91%	7,04%

In thousands of PLN

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	31.12.2018	31.12.2017
Provisions for unused holidays	45 948	45 297
Provisions for employee bonuses	239 134	213 451
Provisions for retirement allowances	34 351	67 225
Other staff-related provisions	12 928	14 797
Total	**332 361**	**340 770**

Detailed information about movements on employee provisions have been presented in Note 36.

51. Share based incentive scheme

The fifth edition of the Santander Bank Polska SA 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 Santander Bank Polska SA approved three-year Incentive Scheme no. VI which participants are employees of the Santander Bank Polska Group (including Members of the Management Board), however not more than 250 individuals. On 26.06.2017 the Supervisory Board approved the list of entitled individuals ("grant date").

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

In every single year annual award not exceeding one third on total award will be considered. Shares will vest on a linear pattern between 25% and 100% contingent on profit after tax (PAT) growth and on RORWA ratio growth. The range of the scale requires PAT growth between "lower level" set to 80% of assumed level of realization in 2017 and "upper level" of nominal growth at 17.8% in first year and between "lower level" set to 80% of assumed level of realization in 2018 and 2019 and "upper level" of nominal growth at 13,4% in second and third year of duration of scheme. The range of the scale requires RORWA ratio growth between "lower level" set to 80% of assumed level of realization in 2017 and "upper level" of nominal growth at 2.24% in first year, between "lower level" set to 80% of assumed level of realization in 2018 and "upper level" of nominal growth at 2.37% in second year and between "lower level" set to 80% of assumed level of realization in 2019 and "upper level" of nominal growth at 2.5% in third year of duration of scheme.

Additionally the qualitative factors will be taken into account – participants are entitled to annual award depending on the level of 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.

In thousands of PLN

Share based payments granted in 2017:

	2017
Number of share based payments	131 262
Share price (PLN)	350
Excercise 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 (PLN)	323.36
Dividend yield	1.71%

The following table summarizes the share based payments activity:

	12 months of 2018	12 months of 2017
	Number of share based payments	Number of share based payments
Outstanding at 1 January	**129 799**	**157 254**
Granted	-	131 912
Exercised	-	(100 233)
Forfeited	(9 113)	(3 958)
Expired	-	(55 176)
Outstanding at 31 December	**120 686**	**129 799**
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 31.12.2018 and as at 31.12.2017 the average remaining contractual life is approximately 1.5 years and 2.5 year respectively.

The expenses of sixth edition of equity settled share-based payments scheme recognized in profit and loss account for 12 months of 2018 and 2017 amounts to PLN 12,025 k and PLN 6,957 k respectively.

The table below presents information about the number of conditional rights to shares vested in Santander Bank Polska Management Board members under the 5th Incentive Scheme and the 6th Incentive Scheme launched in 2017. The rights may be exercised only in part depending on the future performance of the Group. Information about the rights exercised in full or in part will be provided in the future reports.

No. of awards	2018	2017
Outstanding at 1 January	**34 670**	**17 671**
Granted	-	35 687
Expired	-	(6 053)
Exercised	-	(10 541)
Resignation from the function	(7 450)	(2 094)
As at 31 December	**27 220**	**34 670**

In thousands of PLN

The table below presents information about the number of conditional rights to shares vested in Santander Bank Polska Key Management.

No. of awards	2018	2017
Outstanding at 1 January	**37 274**	**28 615**
Granted	-	40 214
Expired	-	(8 451)
Exercised	-	(17 849)
Change due to inclusion in key management personnel	9 366	-
Change due to exclusion from key management personnel	(7 908)	-
Resignation from the function	-	(5 255)
As at 31 December	**38 732**	**37 274**

52. Dividend per share

As of the date of publication of this report, the Management Board of Santander Bank Polska SA has not finalised its analysis in respect of recommendation on dividend payout for 2018.

The proposal regarding dividend 2016. Dividend pay – out date for 14 .06.2018.

On 17.04.2018 The Management Board of Santander Bank Polska SA informs that in full compliance with the individual recommendation issued by the Polish Financial Supervision Authority on 16.03.2018, has adopted a resolution which recommend not to allocate to dividend any part of the net profit for 2017. The Supervisory Board also approved that recommendation. At the same time, taking into account a good capital position of the Bank and Group, the Bank's Management Board tabled the following proposal, that has been approved by the Supervisory Board, to allocate PLN 307,627k from the Bank's undivided net profit for 2016 to dividend for shareholders, for which means that dividend per share was PLN 3.10.

Regarding dividend 2014 and 2015. Dividend pay – out date for 14 .06.2017

On 17.05.2017 Annual General Meeting of Santander Bank Polska SA 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.

53. Operating segments reporting

Operating segments reporting were presented in “Consolidated Financial Statement of Santander Bank Polska Group for 2018” released on 22.02.2019.

54. Events which occurred subsequently to the end of the reporting period

Conclusion of an agreement with trade unions on collective redundancies

Management Board of Santander Bank Polska SA informed that on 31st January 2019 the Bank concluded an agreement defining the principles of collective redundancies with all trade unions operating at the Bank.

The parties to the agreement agreed, among others selection criteria for employees whose employment contracts will be terminated as part of collective redundancies, severance pay conditions and additional compensation and the scope of the assistance program for dismissed employees. It was also agreed that collective redundancies will be carried out from February 2019 to 31st December 2019 and will not cover more than 1,400 employees.

The Bank estimates the costs amount of collective redundancies for PLN 70-90 million and due to this the restructuring provision will be created in the Bank's accounting books.

The Polish Financial Supervision Authority letter regarding individual criteria for the dividend policy 2019 for Santander Bank Polska SA

The Management Board of Santander Bank Polska SA informed that on 18th January 2019 has received the letter from the Polish Financial Supervision Authority referring to the criteria for the dividend policy for 2019.

Criteria for dividend payment up to 75% from the profit earned in the previous year are identical to criteria published on 15th January 2019 in the PFSA statement of the supervisory body regarding the criteria for the dividend policy of commercial banks, cooperative and associative banks, insurance and reinsurance companies, brokerage houses, investment fund companies and general pension societies in 2019.

Criteria for dividend payment up to 100% from the profit earned in the previous year, additionally take into account the bank's sensitivity to the unfavorable macroeconomic scenario.

The PFSA informed the Bank that as a result of stress tests conducted, the individual add-on (ST) measuring the sensitivity of the Bank to unfavorable macroeconomic scenario, after reduction by the conservation buffer at the level applied from January 2019, was set at 0.92 p.p. for Santander Bank Polska SA.

Bank's sensitivity to an unfavorable macroeconomic scenario is defined as the difference between total capital ratio (TCR) in the baseline scenario and TCR in the stress scenario (at the end of forecast - 2020). The results of stress tests, including supervisory adjustments, were taken into account for determining the ST indicator. Due to the assumption regarding the stability of the balance sheet, in this year the ST indicator is additionally reduced by the conservation buffer at the level in force from January 2019, i.e. 2.5 p.p.

Indended collective redundancies

The Management Board of Santander Bank Polska SA informed that on 10 January 2019, as per the Act of 13 March 2003 on special rules of terminating employment contracts for reasons not attributable to the employees, they adopted a resolution on the intended collective redundancies and the start of the consultation procedure for collective redundancies.

The intention of the Management Board of the Bank is to make up to 1,400 employees of the Bank redundant, i.e. approx. 11% of all employed at the Bank as at 31 December 2018, between February and 31 December 2019.

The Bank will publish another announcement on collective redundancies on completion of the consultations with the trade unions, as required by applicable laws, which will include information about the estimated provision to be raised for restructuring of employment at the Bank which will be fully charged to the Bank's financial results. The final amount of the provision and the impact of the employment restructuring on the Bank's financial performance will be disclosed in the financial statements.

In thousands of PLN

Signatures of the persons representing the entity

Date	Name	Function	Signature
21.02.2019	Michał Gajewski	President	
21.02.2019	Andrzej Burliga	Vice-President	
21.02.2019	Michael McCarthy	Vice-President	
21.02.2019	Juan de Porras Aguirre	Vice-President	
21.02.2019	Arkadiusz Przybył	Vice-President	
21.02.2019	Feliks Szyszkowiak	Vice-President	
21.02.2019	Carlos Polaino Izquierdo	Member	
21.02.2019	Maciej Reluga	Member	
21.02.2019	Dorota Strojkowska	Member	

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

Date	Name	Function	Signature
21.02.2019	Wojciech Skalski	Financial Accounting Area Director	