

Annual report of Santander Bank Polska Group for 2018



Dear All,

2018 was a momentous year in the history of Santander Bank Polska Group (previously Bank Zachodni WBK Group). 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 as a leading financial Group in Poland.

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 are 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 Group incorporated the demerged part of Deutsche Bank Polska S.A.

The growth of Santander Bank Polska Group 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 Group among the top tier of the domestic financial institutions are a testimony to our development strategy.

Macroeconomic environment

2018 was one of the best years for the Polish economy in the last decade. GDP growth averaged 5.1%, consumption, investments and wages were growing rapidly and the employment rate hit record highs. The housing market was on a steep upward trend. The solid economic performance prompted the rating agency S&P to upgrade Poland's credit rating to A- (from BBB+), while throughout the year other rating agencies and financial institutions revised upwards their forecasts for Poland. The local economy benefited from the good economic situation in the eurozone and from an increase in the absorption of EU funds. At the same time, despite the rapid growth, the economy did not show any indication of imbalance: inflation remained low and the current account balance was almost in equilibrium. The Polish zloty was extremely stable against the main currencies, even despite the increased market volatility due to serious problems of some emerging economies. The main challenge facing Polish companies in 2018 was difficulties in finding skilled workforce, which translated into a strong surge in salaries and the search for employees abroad.

However, the global economy is faced with big threats: the rise of protectionism in international trade, social tensions in Europe and the still unresolved issue of Britain's exit from the European Union are increasingly weighing down on trading performance. In addition, tensions between EU countries may delay the development of a coherent economic policy, as was the case in 2010–2013. The weaker external environment will have an adverse effect on the economic growth in Poland in 2019.

Sector and Santander Bank Polska Group

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 Group incorporated a 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 Group acquired almost 400,000 customers, who immediately gained access to the full range of the bank's products and services. The transaction strengthened the Group'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 Group posted attributable profit of PLN 2.4 billion. Total income was PLN 8.7 billion, up 11,9% YoY. Gross loans and advances to customers increased by 26% YoY, and deposits grew by 34% YoY. The Group's assets increased by a significant 35% to PLN 206 billion. At present, the Group serves nearly 7 million customers.

Security and Innovation

Through the "Bank As You Want It" strategy, the Group 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 Group'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 Group is the development of payment solutions that create huge potential for increasing customer satisfaction and loyalty. For this reason, the Group 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.

2018 was also successful for other companies from the Polish Santander family. Santander Leasing S.A. financed assets worth almost PLN 5.4 billion net, achieving record-high results in all segments and product lines. The Group's factoring company is ranked third in the market with a turnover of PLN 27.3 billion, and is a leader in supplier financing. Santander Brokerage Poland has increased its share in the retail and institutional segment amid falling market turnover, and has

expanded its offer for private banking customers to include structured products issued in the form of private placements. Specialising in consumer finance, Santander Consumer Bank Group is a market leader in this segment.

The transformation of Santander Bank Polska Group 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 Group 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 Group 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 Group 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 Santander Foundation 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 CJI 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 the brand promise of our Group: 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	
Consolidated financial statements of Santander Bank Polska Group					
I	Net interest income	5 742 405	5 276 897	1 345 803	1 243 173
II	Net fee and commission income	2 057 802	2 013 126	482 271	474 268
III	Profit before tax	3 426 152	3 335 221	802 960	785 738
IV	Net profit attributable to owners of Santander Bank Polska SA	2 365 222	2 213 054	554 319	521 369
V	Total net cash flows	10 349 939	(4 176 431)	2 425 634	(983 917)
VI	Total assets	205 852 860	152 674 444	47 872 758	36 604 676
VII	Deposits from banks	2 832 928	2 783 083	658 820	667 262
VIII	Deposits from customers	149 616 658	111 481 135	34 794 572	26 728 316
IX	Total liabilities	179 184 649	129 330 815	41 670 849	31 007 892
X	Total equity	26 668 211	23 343 629	6 201 910	5 596 785
XI	Non-controlling interests in equity	1 564 184	1 436 409	363 764	344 388
XII	Profit of the period attributable to non-controlling	333 791	305 460	78 228	71 963
XIII	Number of shares	102 088 305	99 333 481		
XIV	Net book value per share in PLN/EUR	261,23	235,00	60,75	56,34
XV	Capital ratio	15,98%	16,69%		
XVI	Profit per share in PLN/EUR	23,72	22,29	5,56	5,25
XVII	Diluted earnings per share in PLN/EUR	23,68	22,25	5,55	5,24
XVIII	Declared or paid dividend per share in PLN/EUR*	3,10	5,40	0,73	1,27

* Detailed information are described in Note 54.

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.

Consolidated Financial Statement of
Santander Bank Polska Group
for 2018

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I. Consolidated income statement

for reporting period:		01.01.2018- 31.12.2018	01.01.2017- 31.12.2017
Interest income and similar to income		7 213 796	6 529 307
Interest income on financial assets measured at amortised cost		6 345 132	-
Interest income on financial assets measured at fair value through other comprehensive income		733 378	-
Income similar to interest on financial assets measured at fair value through profit or loss		135 286	-
Interest expense		(1 471 391)	(1 252 410)
Net interest income	Note 6	5 742 405	5 276 897
Fee and commission income		2 526 572	2 476 209
Fee and commission expense		(468 770)	(463 083)
Net fee and commission income	Note 7	2 057 802	2 013 126
Dividend income	Note 8	100 116	76 816
Net gains/(losses) on subordinated entities		(65)	3 757
Net trading income and revaluation	Note 9	144 539	194 974
Gains (losses) from other financial securities	Note 10	37 480	47 502
Other operating income	Note 11	213 842	150 587
Gain on acquisition of enterprise	Note 51	387 733	-
Impairment losses on loans and advances	Note 12	(1 085 068)	(690 473)
Operating expenses incl.:		(3 768 969)	(3 372 414)
-Staff, operating expenses and management costs	Note 13,14	(3 242 758)	(2 939 432)
-Depreciation/amortisation		(333 470)	(318 933)
-Other operating expenses	Note 15	(192 741)	(114 049)
Share in net profits (loss) of entities accounted for by the equity method		62 667	58 264
Tax on financial institutions		(466 330)	(423 815)
Profit before tax		3 426 152	3 335 221
Corporate income tax	Note 16	(727 139)	(816 707)
Consolidated profit for the period		2 699 013	2 518 514
of which:			
-attributable to owners of Santander Bank Polska SA		2 365 222	2 213 054
-attributable to non-controlling interests		333 791	305 460
Net earnings per share	Note 17		
Basic earnings per share (PLN/share)		23,72	22,29
Diluted earnings per share (PLN/share)		23,68	22,25

Notes presented on pages 10 – 169 constitute an integral part of this Financial Statement.

II. Consolidated statement of comprehensive income

	01.01.2018-	01.01.2017-
	for reporting period:	
	31.12.2018	31.12.2017
Consolidated profit for the period	2 699 013	2 518 514
Other comprehensive income which can be transferred to the profit and loss account:	333 945	452 578
Available-for sale financial assets valuation gross	-	533 774
Deferred tax	-	(101 417)
Valuation of cash flow hedging instruments gross	29 991	24 964
Deferred tax	(5 698)	(4 743)
Valuation of debt securities measured at fair value through other comprehensive income gross	382 287	-
Deferred tax	(72 635)	-
Other comprehensive income which can't be transferred to the profit and loss account:	15 576	(7 622)
Valuation of equity securities measured at fair value through other comprehensive income gross	6 702	-
Deferred tax	(1 273)	-
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	12 688	(9 410)
Deferred tax	(2 411)	1 788
Other comprehensive income for the period net of income tax	349 521	444 956
TOTAL COMPREHENSIVE INCOME FOR THE PERIOD	3 048 534	2 963 470
Total comprehensive income attributable to:		
Owners of Santander Bank Polska SA	2 714 256	2 651 427
Non-controlling interests	334 278	312 043

Notes presented on pages 10 – 169 constitute an integral part of this Financial Statement.

III. Consolidated statement of financial position

	as at:	31.12.2018	31.12.2017
ASSETS			
Cash and balances with central banks	Note 18	8 907 552	4 146 222
Loans and advances to banks	Note 19	2 936 214	2 136 474
Financial assets held for trading	Note 20	9 769 851	3 416 108
Hedging derivatives	Note 21	73 221	218 061
Loans and advances to customers incl.:	Note 22	137 460 378	107 839 897
- measured at amortised cost		135 643 297	-
- measured at fair value through other comprehensive income		366 751	-
- measured at fair value through profit or loss		1 450 330	-
Buy-sell-back transactions		177 482	-
Financial assets available for sale		-	28 415 812
Investment securities incl.:	Note 23	39 179 100	-
- debt securities measured at fair value through other comprehensive income		38 221 051	-
- debt securities measured at fair value through profit and loss		136 511	-
- equity securities measured at fair value through other comprehensive income		821 538	-
Investments in associates	Note 24	891 952	889 372
Intangible assets	Note 25	819 409	490 327
Goodwill	Note 26	1 712 056	1 712 056
Property, plant and equipment	Note 27	986 384	930 717
Net deferred tax assets	Note 28	1 760 121	1 414 227
Assets classified as held for sale	Note 29	12 145	103
Other assets	Note 30	1 166 995	1 065 068
Total assets		205 852 860	152 674 444
LIABILITIES AND EQUITY			
Deposits from banks	Note 31	2 832 928	2 783 083
Hedging derivatives	Note 21	912 482	578 798
Financial liabilities held for trading	Note 20	1 233 713	1 237 704
Deposits from customers	Note 32	149 616 658	111 481 135
Sell-buy-back transactions	Note 43	9 340 788	2 650 846
Subordinated liabilities	Note 33	2 644 341	1 488 602
Debt securities in issue	Note 34	9 368 617	5 895 814
Current income tax liabilities		288 300	192 925
Provisions for off balance sheet credit facilities	Note 35	81 048	50 652
Other provisions	Note 36	132 881	102 482
Other liabilities	Note 37	2 732 893	2 868 774
Total liabilities		179 184 649	129 330 815
Equity			
Equity attributable to owners of Santander Bank Polska S.A.		25 104 027	21 907 220
Share capital	Note 38	1 020 883	993 335
Other reserve capital	Note 39	18 969 482	16 920 129
Revaluation reserve	Note 40	1 019 373	714 466
Retained earnings		1 729 067	1 066 236
Profit for the current period		2 365 222	2 213 054
Non-controlling interests in equity	Note 41	1 564 184	1 436 409
Total equity		26 668 211	23 343 629
Total liabilities and equity		205 852 860	152 674 444

Notes presented on pages 10 – 169 constitute an integral part of this Financial Statement.

IV. Consolidated statement of changes in equity

Consolidated statement of changes in equity	Equity attributable to equity holders of parent entity				Total	Non-controlling interests	Total equity
	Share capital	Other reserve capital	Revaluation reserve	Retained earnings and profit for the period			
Note	38	39	40			41	
Equity as at 31.12.2017	993 335	16 920 129	714 466	3 279 290	21 907 220	1 436 409	23 343 629
Impact of the implementation of IFRS 9*	-	-	(44 047)	(210 407)	(254 454)	-	(254 454)
Equity as at 1.01.2018 (restated)	993 335	16 920 129	670 419	3 068 883	21 652 766	1 436 409	23 089 175
Coverage of negative impact of IFRS 9	-	-	-	222 905	222 905	-	222 905
Total comprehensive income	-	-	349 034	2 365 222	2 714 256	334 278	3 048 534
<i>Consolidated profit for the period</i>	-	-	-	2 365 222	2 365 222	333 791	2 699 013
<i>Other comprehensive income</i>	-	-	349 034	-	349 034	487	349 521
Issue of shares **	27 548	-	-	-	27 548	-	27 548
Agio	-	1 004 291	-	-	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	-	1 032 851	-	(1 032 851)	-	-	-
Profit allocation to dividends	-	-	-	(307 627)	(307 627)	(206 503)	(514 130)
Profit allocation to cover negative impact of IFRS 9 implementation*	-	-	-	(222 905)	(222 905)	-	(222 905)
Share scheme charge	-	12 445	-	-	12 445	-	12 445
Equity adjustment due to merger and liquidation of subsidiaries and controlling stake at the other subsidiaries	-	(234)	(210)	792	348	-	348
As at 31.12.2018	1 020 883	18 969 482	1 019 373	4 094 289	25 104 027	1 564 184	26 668 211

*General Meeting of Santander Bank Polska SA and Santander Factoring Sp. z o.o. decided to allocate part of the retained earnings to cover the negative impact of the implementation of IFRS 9 respectively in the amount PLN 218,466 k and PLN 4,439 k.

** 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 1,019,373 k comprises valuation of debt securities and valuation of equity securities of PLN 553,743 k and PLN 518,983 k respectively and additionally valuation of cash flow hedge activities of PLN (64,190) k and accumulated actuarial gains - provision for retirement allowances of PLN 10,837 k.

Equity attributable to equity holders of parent entity

Consolidated statement of changes in equity	Equity attributable to equity holders of parent entity				Total	Non-controlling interests	Total equity
	Share capital	Other reserve capital	Revaluation reserve	Retained earnings and profit for the period			
Note	38	39	40			41	
Equity as at 1.01.2017	992 345	15 791 555	276 093	2 720 834	19 780 827	1 237 649	21 018 476
Total comprehensive income	-	-	438 373	2 213 054	2 651 427	312 043	2 963 470
<i>Consolidated profit for the period</i>	-	-	-	2 213 054	2 213 054	305 460	2 518 514
<i>Other comprehensive income</i>	-	-	438 373	-	438 373	6 583	444 956
Issue of shares *	990	-	-	-	990	-	990
Profit allocation to other reserve capital	-	1 123 497	-	(1 123 497)	-	-	-
Profit allocation to dividends	-	-	-	(535 866)	(535 866)	(110 962)	(646 828)
Share scheme charge	-	(2 512)	-	-	(2 512)	-	(2 512)
Equity adjustment due to merger and liquidation of subsidiaries and controlling stake at the subsidiaries	-	7 589	-	4 765	12 354	(2 321)	10 033
As at 31.12.2017	993 335	16 920 129	714 466	3 279 290	21 907 220	1 436 409	23 343 629

*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.

As at the end of the period revaluation reserve in the amount of PLN 714,466 k comprises valuation of debt securities and valuation of equity securities of PLN 245,104 k and PLN 557,499 k respectively and additionally valuation of cash flow hedge activities of PLN (88,574) k and accumulated actuarial gains - provision for retirement allowances of PLN 437 k.

V. Consolidated statement of cash flows

	for the period	01.01.2018- 31.12.2018	01.01.2017- 31.12.2017
Profit before tax		3 426 152	3 335 221
Total adjustments:			
Share in net profits of entities accounted for by the equity method		(62 667)	(58 264)
Depreciation/amortisation		333 470	318 933
Gain on acquisition of enterprise		(387 733)	-
Impairment losses (reversal)		12 959	8 765
Profit from investing activities		(79 107)	(62 297)
		3 243 074	3 542 358
Changes:			
Provisions		32 586	23 006
Trading portfolio financial instruments		(6 345 807)	(1 506 362)
Hedging derivatives		478 524	(1 594 962)
Loans and advances to banks		151 667	(95)
Loans and advances to customers		(11 063 294)	(4 771 359)
Deposits from banks		(4 094 278)	110 032
Deposits from customers		23 883 844	(781 067)
Buy-sell/ Sell-buy-back transactions		6 689 942	1 018 233
Other assets and liabilities		(400 553)	277 134
		9 332 631	(7 225 440)
Interest accrued excluded from operating activities		(369 152)	(414 692)
Dividends		(98 989)	(76 270)
Paid income tax		(947 002)	(693 049)
Net cash flows from operating activities		11 160 562	(4 867 093)
Inflows		6 309 947	4 461 677
Sale/maturity of financial assets available for sale		-	3 673 594
Sale/maturity of investment securities		5 358 065	-
Sale of intangible assets and property, plant and equipment		105 615	45 342
Dividends received		98 989	76 270
Interest received		747 278	666 471
Outflows		(11 671 083)	(4 206 618)
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		-	(3 792 409)
Purchase of investment securities		(10 883 425)	-
Purchase of intangible assets and property, plant and equipment		(581 186)	(414 209)
Net cash flows from investing activities		(5 361 136)	255 059
Inflows		11 102 519	4 983 948
Debt securities in issue		7 430 794	3 562 288
Proceeds from issuing/shares		-	990
Drawing of loans		3 671 725	1 420 670
Outflows		(6 552 006)	(4 548 345)
Debt securities buy out		(2 975 000)	(2 095 000)
Repayment of loans		(2 781 861)	(1 568 408)
Dividends and other payments to shareholders		(514 130)	(646 828)
Interest paid		(281 015)	(238 109)
Net cash flows from financing activities		4 550 513	435 603
Total net cash flows		10 349 939	(4 176 431)
Cash and cash equivalents at the beginning of the accounting period		7 662 368	11 838 799
Cash and cash equivalents at the end of the accounting period		18 012 307	7 662 368

Cash, cash equivalents and other additional information regarding the statement of cash flows are presented in Note 48.

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

Notes presented on pages 10 – 169 constitute an integral part of this Financial Statement.

VI. Additional notes to consolidated financial statement

1. General information about issuer

Santander Bank Polska SA 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.

Consolidated financial statement of Santander Bank Polska Group includes Bank's financial information as well as information from its subsidiaries and shares in associated entities (all together called Group).

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

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

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

Santander Bank Polska Group consists of the following entities:

Subsidiaries:

Subsidiaries	Registered office	[%] of votes on AGM at 31.12.2018	[%] of votes on AGM at 31.12.2017
1. Santander Finanse sp. z o.o. (formerly BZ WBK Finanse sp. z o.o.)	Poznań	100%	100%
2. Santander Factoring sp. z o.o. (formerly BZ WBK Faktor sp. z o.o.)	Warszawa	100% of AGM votes are held by Santander Finanse sp. z o.o.	100% of AGM votes are held by Santander Finanse sp. z o.o.
3. Santander Leasing S.A. (formerly BZ WBK Leasing S.A.)	Poznań	100% of AGM votes are held by Santander Finanse sp. z o.o.	100% of AGM votes are held by Santander Finanse sp. z o.o.
4. Santander Leasing Poland Securitization 01 ¹⁾	Dublin	subsidiary of Santander Leasing S.A.	-
5. Santander Inwestycje sp. z o.o. (formerly BZ WBK Inwestycje sp. z o.o.)	Warszawa	100%	100%
6. Giełdokracja sp. z o.o. ²⁾	Poznań	-	100%
7. Santander F24 S.A. (formerly BZ WBK F24 S.A.)/ BZ WBK Nieruchomości S.A. ³⁾	Poznań	100% of AGM votes are held by Santander Finanse sp. z o.o.	100% of AGM votes are held by Santander Finanse sp. z o.o.
8. Santander Securities S.A. ⁴⁾	Warszawa	100%	-
9. Santander Towarzystwo Funduszy Inwestycyjnych S.A. (formerly BZ WBK Towarzystwo Funduszy Inwestycyjnych S.A.) ⁵⁾	Poznań	50%	50%
10. Santander Consumer Bank S.A.	Wrocław	60%	60%
11. Santander Consumer Finanse sp. z o.o.	Warszawa	100% of AGM votes are held by Santander Consumer Bank S.A.	100% of AGM votes are held by Santander Consumer Bank S.A.
12. PSA Finance Polska sp. z o.o. ⁶⁾	Warszawa	Santander Consumer Bank S.A. and 50% of AGM votes are held by Banque PSA Finance S.A.	Santander Consumer Bank S.A. and 50% of AGM votes are held by Banque PSA Finance S.A.
13. PSA Consumer Finance Polska sp. z o.o. ⁶⁾	Warszawa	100% of AGM votes are held by PSA Finance Polska sp. z o.o.	100% of AGM votes are held by PSA Finance Polska sp. z o.o.
14. Santander Consumer Multirent sp. z o.o.	Warszawa	100% of AGM votes are held by Santander Consumer Bank S.A.	100% of AGM votes are held by Santander Consumer Bank S.A.
15. S.C. Poland Consumer 15-1 sp.z o.o. ⁷⁾	Warszawa	subsidiary of Santander Consumer Bank S.A.	subsidiary of Santander Consumer Bank S.A.
16. S.C. Poland Consumer 16-1 sp.z o.o. ⁷⁾	Warszawa	subsidiary of Santander Consumer Bank S.A.	subsidiary of Santander Consumer Bank S.A.

- 1) Foundation of Santander Leasing Poland Securitization 01 as part of securitization transaction. Details in note 50.
 2) Giełdokracja sp. z o.o. was liquidated. Details in note 50.
 3) On 18.10.2017, BZ WBK Nieruchomości SA with its registered office in Zakrzewo changed name to Santander F24 SA (formerly BZ WBK F24 SA) with its registered office in Poznań. 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 On 12.01.2018 in the Nation Court Register was registered increase of share capital Santander Finanse sp. z o.o. to PLN 1,630 k. Share capital was fully paid.
 4) Acquisition of Santander Securities S.A. Details in note 51.
 5) As at 31.12.2018, Santander Bank Polska was a co-owner of Santander Towarzystwo Funduszy Inwestycyjnych SA, together with Banco Santander SA Both owners are members of Santander Group and each holds an equal stake of 50% in the company's share capital. In practice, Santander Bank Polska exercises control over the subsidiary Santander Towarzystwo Funduszy Inwestycyjnych SA because though it, Banco Santander implements its policy in Poland. Consequently, the company is treated as a subsidiary.
 6) According to Santander Bank Polska Group Management Board, investing in PSA Finance Polska Sp. z o.o., a subsidiary company, resulted from the need to prepare consolidated financial statements due to the fact that Santander Consumer Bank S.A has a direct control and Santander Bank Polska SA has indirect control over the investment.
 7) SC Poland Consumer 15-1 sp. z o.o. SC Poland Consumer 16-1 sp. z o.o. set up for the purpose of securitisation of a part of the loan portfolio; its shareholder is polish legal entity who has no ties with the Group; the company is controlled by Santander Consumer Bank, in accordance with the control criteria set out in IFRS 10.7.

Associates:

Associates	Registered office	[%] of votes on AGM at 31.12.2018	[%] of votes on AGM at 31.12.2017
1. POLFUND - Fundusz Poręczeń Kredytowych S.A.	Szczecin	50%	50%
2. Santander - Aviva Towarzystwo Ubezpieczeń S.A.	Poznań	49%	49%
3. Santander - Aviva Towarzystwo Ubezpieczeń na Życie S.A.	Poznań	49%	49%

2. Basis of preparation of consolidated financial statement

2.1. Statement of compliance

This consolidated financial statement of Santander Bank Polska S.A. Group was prepared in accordance with the International Financial Reporting Standards (IFRS) adopted by the European Union, which are applied on a consistent basis, as at 31 December 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.

This consolidated financial statement has been approved for publication by the Management Board of Santander Bank Polska S.A. on 21 February 2019.

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

IFRS	Nature of changes	Effective from	Influence on Santander Bank Polska S.A. Group
Conceptual Framework for Financial Reporting	<p>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.</p> <p>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:</p> <ul style="list-style-type: none"> • 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 <p>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.</p>	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	<p>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.</p>	1 January 2019	The amendment will not have a significant impact on financial statement.
IFRS 16 Leases	<p>The new standard establishes principles for the recognition, measurement, presentation and disclosure of leases. All lease transactions results in the lessee's right to use the assets and the obligation to make a payment. Accordingly, the classification of leases into operating lease and finance lease as per IAS 17 no longer applies under IFRS 16, as the new standard introduces a single model for accounting for leases by the lessee. The lessee will be required to present the following: (a) assets and liabilities in respect of all leases executed for more than 12 months, except where an asset is of low quality; and (b) depreciation charge for the leased asset separately from the interest expense on the lease liability in the statement of profit or loss and other comprehensive income.</p> <p>The principles of accounting for leases by the lessee established in IFRS 16 are largely the same as in IAS 17. As a consequence, the lessee continues to use the classification into operating lease and finance lease and accounts for them accordingly.</p>	1 January 2019	Standard's implementation progress is described below.

Amendments to IAS 28 Long-term Interests in Associates and Joint Ventures *	<p>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.</p> <p>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.</p> <p>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.</p>	1 January 2019	The amendment will not have a significant impact on financial statement.
Improvements to IFRS 10 and IAS 28 *	<p>Improvements to IFRS 10 and IAS 28 cover sales or contributions of assets between an investor and its associate/joint venture. The improvements eliminate the inconsistencies between IFRS 10 and IAS 28. The accounting treatment hinges on whether the non-monetary assets sold or contributed to an associate/joint venture constitute a business.</p> <p>Should the assets constitute a business, the investor shall recognize the profit or loss in full. Should the assets not constitute a business, the profit or loss shall be recognised only to the extent of unrelated investors' interests in the associate or joint venture.</p> <p>The improvements were published on 11 September 2014.</p>	The International Accounting Standards Board has not established the validity date of the amended regulations.	The amendment will not have a significant impact on financial statement.
IFRS 17 Insurance Contracts*	<p>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, reinsurance 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.</p>	1 January 2021	The standard will not have a significant impact on financial statement.
IFRIC 23 Uncertainty over Income Tax Treatments*	<p>Interpretation clarifies how the recognition and measurement requirements of IAS 12 "Income taxes" are applied where there is uncertainty over income tax treatments. An uncertain tax treatment is any tax treatment applied where there is uncertainty over whether that treatment will be accepted by the tax authority.</p> <p>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.</p> <p>The impact of the uncertainty should be measured using the method that best predicts the resolution of the uncertainty - either the most likely amount method or the expected value method when measuring an uncertainty.</p>	1 January 2019	The amendment will not have a significant impact on financial statement.
IAS 19, Plan Amendment, Curtailment or Settlement*	<p>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.</p>	1 January 2019	The amendment will not have a significant impact on financial statement.

2015-2017 Cycle	<p>Following is a summary of the amendments from the 2015-2017 annual improvements cycle:</p> <p>IFRS 3 Business Combinations - Previously held Interests in a joint operation</p> <ul style="list-style-type: none"> • 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. <p>IFRS 11 Joint Arrangements - Previously held Interests in a joint operation</p> <ul style="list-style-type: none"> • 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	<p>Following is a summary of the amendments from the 2015-2017 annual improvements cycle:</p> <p>IAS 12 Income Taxes - Income tax consequences of payments on financial instruments classified as equity</p> <ul style="list-style-type: none"> • 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. <p>IAS 23 Borrowing Costs - Borrowing costs eligible for capitalisation</p> <ul style="list-style-type: none"> • 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. Group 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. Group 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. Group:

- 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. Group, 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. Group;
- 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. Group 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. Group 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. Group 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. Group, 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 such as warehouses;
- 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;
- lease of optical fibres for the purpose of data transfer between the locations of Santander Bank Polska S.A. Group; and
- operating lease of cars.

The groups of assets identified by Santander Bank Polska S.A. Group 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. Group 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. Group 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. Group, 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. Group, the lessee, is reasonably certain not to exercise that option.

In assessing whether Santander Bank Polska S.A. Group, 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. Group considered all relevant facts and circumstances that create an economic incentive for Santander Bank Polska S.A. Group 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. Group assumed the lease term equal to the term of the lease contract, unless Santander Bank Polska S.A. Group 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. Group, 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. Group's 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.

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

- PLN: 3.19%
- USD: 3.36%
- EUR: 1.24%.

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

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

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	Telecommunication lines	Other	TOTAL
TOTAL	20 412	739 074	4 822	2 859	4 128	767 167

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. Group is presented in Note 47.

The table below presents the difference between future fees under operating leases payable by Santander Bank Polska S.A. Group 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. Group as at 31 December 2018	904 342
Discount based on the incremental borrowing rate of Santander Bank Polska S.A. Group as the lessee	(100 207)
Lease liabilities classified as finance lease before initial application of IFRS 16	-
Value of contractual liabilities considering extension and termination options	11 963
Exclusion – short-term leases	(18 850)
Exclusion – leases of low-value assets	(3 930)
Lease liabilities as per IFRS 16 as at 1 January 2019 – TOTAL	793 319

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

- 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 8,397 k.

- 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 operating leases acquired as part of a business combination in amount PLN 21,578 k,
- decommissioning provision. As regards the lease contracts providing for the obligation of Santander Bank Polska S.A. Group to reinstate the leased asset to its original condition after termination of the lease, Santander Bank Polska S.A. Group 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. Group 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 of assets to their original condition is PLN 7,231 k and will be presented in the statement of financial position under “Other provisions”.
- other adjustments, including unsettled until the first application date cash incentives.

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

Description	Value
Right-of-use assets as per IFRS 16 as at 1 January 2019 , including:	771 295
- lease liabilities as per IFRS 16 as at 1 January 2019	793 318
- provisions for onerous contracts	(8 397)
- assets' adjustment related to assets and liabilities recognized in applying IFRS 3	(21 578)
- decommissioning provision	7 231
- other	721

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

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. Group 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. Group 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. Group 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. Group 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. Group 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. Group 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 Group 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. Group continued to classify all sublease contracts as operating leases.

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. Group
IFRIC 22 Foreign Currency Transactions and Advance Consideration *	IFRIC Interpretation 22 clarify the date of the transaction for the purpose of determining the exchange rate to use on initial recognition of the related asset, expense or income when an entity has received or paid advance consideration in a foreign currency. The Interpretation relates to the situation when the transaction is in foreign currency and the entity pays or receives consideration in advance in a foreign currency before the recognition of the related asset, expense or income.	1 January 2018	The amendment 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.
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. Group 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. Group 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:

Consolidated 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)	4 146 222	Amortized cost	4 146 222
Loans and advances to banks	Amortized cost (loans and advances)	2 136 474	Amortized cost	2 136 474
Financial assets held for trading	Fair value through profit and loss	3 416 108	Fair value through profit and loss	3 416 108
Hedging derivatives	Hedge accounting	218 061	Hedge accounting	218 061
Loans and advances to customers	Amortized cost (loans and advances)	106 225 778	Amortized cost	105 961 354
Loans and advances to customers	Amortized cost (loans and advances)	1 614 119	Fair value through profit and loss	1 595 372
Financial asstes available for sale - Debt instruments	Fair value through other comprehensive income	27 494 933	Fair value through other comprehensive income	27 494 933
Financial asstes available for sale - Equity instruments	Fair value through other comprehensive income	775 557	Fair value through other comprehensive income - option	775 557
Financial asstes available for sale - investment in VISA Inc.	Fair value through other comprehensive income	93 165	Fair value through profit and loss	93 165
Financial asstes available for sale - Equity instruments	Historical cost	52 157	Fair value through other comprehensive income - option	37 063
Other assets	Amortized cost (loans and advances)	1 065 068	Amortized cost	1 065 068
TOTAL		147 237 642		146 939 377

The table above illustrates changes in the classification and measurement of financial assets as at the effective date of IFRS 9, 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 PLN 175k including reversal of PLN 172,271k of allowances for expected credit losses and fair value measurement of the portfolio at PLN 172,446 k was taken to the current period profit.

Carrying amount - gross as at 01.01.2018	Losses for expected credit losses	Carrying amount - net	Fair value	Difference between carrying amount net and fair value
1 662 067	172 271	1 489 796	1 489 971	175

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

Consolidated financial statement's line for 2017	Measurement category	Carrying amount	Measurement category	Carrying amount
Liabilities				
Deposits from banks	Amortized cost	2 783 083	Amortized cost	2 783 083
Hedging derivatives	Hedge accounting	578 798	Hedge accounting	578 798
Financial liabilities held for trading	Fair value through profit and loss	1 237 704	Fair value through profit and loss	1 237 704
Deposits from customers	Amortized cost	111 481 135	Amortized cost	111 481 135
Sell-buy-back transactions	Amortized cost	2 650 846	Amortized cost	2 650 846
Subordinated liabilities	Amortized cost	1 488 602	Amortized cost	1 488 602
Debt securities in issue	Amortized cost	5 895 814	Amortized cost	5 895 814
Provisions for off-balance sheet liabilities subject to credit risk	IAS 37	50 652	IFRS 9	65 686
Other liabilities	Amortized cost	2 868 774	Amortized cost	2 868 774
TOTAL		129 035 408		129 050 442

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.

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

Reference to change No. description	Item	Carrying amount 01.01.2018 before amendments	Change of measurement category	Valuation update		Carrying amount 01.01.2018 after amendments
				Classification and measurement	Impairment	
Financial assets measured at amortised cost						
1	Loans and advances to customers					
	Closing balance	107 839 897	-	-	-	-
Adjustment 1a	ECL allowance	-	-	-	(240 637)	-
Adjustment 2	Change of recognition of interest income	-	-	-	(23 787)	-
Adjustment 3	Presentation adjustment – adjustment to impairment interest	-	-	210 585	(210 585)	-
Adjustment 1b and 4	Reclassification to the category of financial assets measured at fair value through profit or loss	-	(1 614 119)	-	-	-
	Closing balance after adjustments	-	-	-	-	105 961 354
	Financial assets measured at amortised cost – TOTAL	107 839 897	(1 614 119)	210 585	(475 009)	105 961 354
Financial assets measured at fair value through other comprehensive income						
2	Financial assets available for sale					
	Closing balance	28 415 812	-	-	-	-
Adjustment 6	Reclassification to the category of debt investment financial assets measured at fair value through other comprehensive income	-	(27 494 933)	-	-	-
Adjustment 6	Reclassification to the category of equity investment financial assets measured at fair value through other comprehensive income	-	(827 714)	-	-	-
Adjustment 7	Reclassification of investment in VISA Inc. to the category of debt investment financial assets measured at fair value through profit or loss	-	(93 165)	-	-	-
	Closing balance after adjustments	-	-	-	-	-
3	Investment securities, including:					
	Closing balance	-	27 494 933	-	-	-
	- debt investment financial assets measured at fair value through other comprehensive income	-	775 557	-	-	-
Adjustment 5	- equity investment financial assets measured at fair value through other comprehensive income – option	-	52 157	(31 271)	16 177	-
	- equity investment financial assets measured at fair value through other comprehensive income – option	-	-	-	-	-
Adjustment 7	Reclassification of investment in VISA Inc. to debt investment financial assets measured at fair value through profit or loss	-	93 165	-	-	-
	Closing balance after adjustments	-	-	-	-	28 400 718
	Financial assets measured at fair value through other comprehensive income – TOTAL	28 415 812	-	(31 271)	16 177	28 400 718
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 statement	-	1 489 796	(172 096)	172 271	-
	Closing balance after adjustments	-	-	-	-	1 595 372
	Financial assets measured at fair value through profit or loss – TOTAL	-	1 614 119	(252 825)	234 078	1 595 372
Deferred tax assets, net						
	Deferred tax assets, net					
	Closing balance	1 414 227	-	-	-	-
Adjustment 1b	Valuation update - retained earnings	-	-	21 280	37 740	-
	Valuation update - current's year income statement	-	-	32 698	(32 731)	-
	Closing balance after adjustments	-	-	-	-	1 473 214
	Deferred tax assets, net – TOTAL	1 414 227	-	53 978	5 009	1 473 214
	TOTAL ASSETS	137 669 936	-	(19 533)	(219 745)	137 430 658

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.

The table below presents the impact of IFRS 9 implementation on equity's components and liabilities as at 1.01.2018:

Reference to change No. description	Item	Carrying amount 01.01.2018 before amendments	Change of measurement category	Valuation update		Carrying amount 01.01.2018 after amendments
				Classification and measurement	Impairment	
Equity						
1	Revaluation reserve					
	Closing balance	714 466	-	-	-	-
Adjustment 8	Impact of implementing IFRS 9 – gross	-	-	(31 271)	-	-
	Impact of implementing IFRS 9 – deferred tax	-	-	5 942	-	-
Adjustment 7	Reclassification of investment in VISA Inc.	-	-	(18 718)	-	-
	Closing balance after adjustments	-	-	-	-	670 419
	Revaluation reserve - TOTAL	714 466	-	(44 047)	-	670 419
2	Retained earnings					
	Closing balance	1 066 236	-	-	-	-
Adjustment 8	Impact of implementing IFRS 9 – gross	-	-	(80 729)	(201 474)	-
	Impact of implementing IFRS 9 – deferred tax	-	-	15 339	37 739	-
Adjustment 7	Reclassification of investment in VISA Inc.	-	-	18 718	-	-
	Closing balance after adjustments	-	-	-	-	855 829
	Retained earnings - TOTAL	1 066 236	-	(46 672)	(163 735)	855 829
3	Profit for the period					
	Closing balance	-	-	-	-	-
Adjustment 1b	Impact of implementing IFRS 9 – gross	-	-	(172 096)	172 271	-
	Impact of implementing IFRS 9 – deferred tax	-	-	32 698	(32 731)	-
	Closing balance after adjustments	-	-	-	-	142
	Profit for the period - TOTAL	-	-	(139 398)	139 540	142
	Equity - TOTAL	1 780 702	-	(230 117)	(24 195)	1 526 390
Provisions						
4	Provisions					
	Closing balance	50 652	-	-	-	-
Adjustment 1a	Reclassification to "Provisions for off-balance sheet liabilities subject to credit risk"	-	(50 652)	-	-	-
	Closing balance after adjustments	-	-	-	-	-
	Provisions - TOTAL	50 652	(50 652)	-	-	-
Provisions for off-balance sheet liabilities subject to credit risk						
5	Provisions for off-balance sheet liabilities subject to credit risk					
	Closing balance	-	-	-	-	-
Adjustment 1a	Reclassification from "Provisions"	-	50 652	-	-	-
	Valuation update	-	-	-	15 034	65 686
	Closing balance after adjustments	-	-	-	-	-
	Provisions for off-balance sheet liabilities subject to credit risk - TOTAL	-	50 652	-	15 034	65 686
	TOTAL LIABILITIES AND EQUITY	1 831 354	-	(230 117)	(9 161)	1 592 076

The value of other liabilities and equity components presented in the consolidated 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. Group 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 (23,787)k PLN 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. Group 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 210,585 k PLN 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 Group 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 1,001,535 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 193,864 k, without the deferred tax effect, of which PLN 240,637k relates to balance sheet items, PLN 15,034k 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. Group 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. Group 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. Group recognised an interest income adjustment of PLN (23,787)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. Group treated the impairment interest adjustment as the element of exposure's gross carrying amount. Santander Bank Polska S.A. Group 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 210,585 k 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. Group 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. Group 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. Group 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. Group took an irrevocable decision to designate strategic equity investments from the portfolio of financial assets other than those held for trading as instruments measured at fair value through other comprehensive income. The equity investments for which Santander Bank Polska S.A. Group chose the option of fair value measurement through other comprehensive income were acquired to be maintained in the investment portfolio for a long term and strategically, without the intention to make a profit on selling them in the short or medium term. If the equity instrument designated to be measured at fair value through other comprehensive income is sold, the gain (loss) on the transaction is not recycled to profit or loss at the time of the sale. The adjustment to the fair-value measurement of equity instruments has been set at PLN (31,271) k and amount of reversed impairment charges at PLN 16,177 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. Group 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. Group 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 23,109 k and corresponding deferred income tax in the amount of PLN 4,391 k was transferred from revaluation capital to retained earnings.
- Adjustment 8: impact of IFRS 9 adoption on the equity of Santander Bank Polska S.A. Group. As at 1.01. 2018, the total value of the impact of IFRS 9 implementation PLN (313,474) k, and the deferred tax effect in the form of deferred net tax asset increase PLN 59,020 k decreased the balance of retained earnings and revaluation reserve by the amount of PLN (254,454) k.

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 implementation	714 466			
1	Reclassification of available-for-sale equity instruments measured at fair value through other comprehensive income - the effect of remeasuring to fair value	-	(31 271)	5 942	-
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	-	(23 109)	4 391	-
	Value as at 1 January 2018 taking into account the impact of implementing IFRS 9 - TOTAL	714 466	(54 380)	10 333	670 419
Retained earnings					
	Retained earning as at 1 January 2018 before IFRS 9 implementation	1 066 236			
1	Recognition of ECL allowances on financial assets and off-balance sheet liabilities subject to credit risk	-	(240 637)	45 180	-
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	-	16 177	(3 074)	-
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	-	(23 787)	4 520	-
6	Recognition of ECL allowances on off-balance sheet liabilities subject to credit risk	-	(15 034)	2 856	-
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	-	23 109	(4 391)	-
	Retained earnings taking into account the impact of implementing IFRS 9 - TOTAL	1 066 236	(259 094)	48 687	855 829
Current period profit or loss					
	Current period profit or loss as at 1 January 2018: before implementation of IFRS 9				
1	Change in measurement category of credit cards' portfolio recorded in current year's income statement	-	175	(33)	142
	Current period profit or loss as at 1 January 2018 including impact of IFRS 9 - TOTAL	-	175	(33)	142
	Impact of implementing IFRS 9 on the Santander Bank Polska Group's equity - TOTAL	1 780 702	(313 299)	58 987	1 526 390

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

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 interest impaired adjustment's presentation	ECL impairment charge reversal due to credit cards reclassification	Loss allowance under IFRS 9
Loans and receivables (IAS 39)/Financial assets at amortized cost (IFRS 9)						
Loans and advances from customers	4 846 130	(61 807)	240 637	210 585	(172 271)	5 063 274
Loans and receivables (IAS 39)/Financial assets at amortized cost (IFRS 9) - TOTAL	4 846 130	(61 807)	240 637	210 585	(172 271)	5 063 274
Provisions for off-balance sheet liabilities subject to credit risk (IAS 37)/Loss allowance for expected credit losses (IFRS 9)						
Provisions for off-balance sheet liabilities subject to credit risk (IAS 37)/Loss allowance for expected credit losses (IFRS 9)	50 652	-	15 034	-	-	65 686
Provisions for off-balance sheet liabilities subject to credit risk (IAS 37)/Loss allowance for expected credit losses (IFRS 9) - TOTAL	50 652	-	15 034	-	-	65 686
TOTAL	4 896 782	(61 807)	255 671	210 585	(172 271)	5 128 960

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 Group 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 1,001,535 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. Group. The total value of additional impairment charges recognised in retained earnings for previous years is PLN 193,864 k, without the deferred tax effect, of which PLN 240,637 k relates to balance sheet items, PLN 15,034 k the increase in provisions for off-balance sheet liabilities presented in the line „Provisions 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 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 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 Group has decided to apply the transitional arrangements provided for therein, which means that the full impact of the introduction of IFRS 9 will not be taken into account for the purpose of capital adequacy assessment of Santander Bank Polska Group.

Below, Santander Bank Polska S.A. Group 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	20 166 059
2	Common Equity Tier 1 (CET1) capital as if IFRS 9 or analogous ECLs transitional arrangements had not been applied	19 984 622
3	Tier 1 capital	20 166 059
4	Tier 1 capital as if IFRS 9 or analogous ECLs transitional arrangements had not been applied	19 984 622
5	Total capital	22 839 754
6	Total capital as if IFRS 9 or analogous ECLs transitional arrangements had not been applied	22 658 089
Risk-weighted assets (amounts)		
7	Total risk-weighted assets	142 927 860
8	Total risk-weighted assets as if IFRS 9 or analogous ECLs transitional arrangements had not been applied	142 852 541
Capital ratios		
9	Common Equity Tier 1 (as a percentage of risk exposure amount)	14,11%
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	13,99%
11	Tier 1 (as a percentage of risk exposure amount)	14,11%
12	Tier 1 (as a percentage of risk exposure amount) as if IFRS 9 or analogous ECLs transitional arrangements had not been applied	13,99%
13	Total capital (as a percentage of risk exposure amount)	15,98%
14	Total capital (as a percentage of risk exposure amount) as if IFRS 9 or analogous ECLs transitional arrangements had not been applied	15,86%
Leverage ratio		
15	Leverage ratio total exposure measure	212 258 409
16	Leverage ratio	9,50%
17	Leverage ratio as if IFRS 9 or analogous ECLs transitional arrangements had not been applied	9,42%

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. Group expects to be entitled in exchange for those assets.

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

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

As part of the analysis of the impact of IFRS 15 on the Santander Bank Polska S.A. Group, 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. Group as agreements where Santander Bank Polska S.A. Group 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. Group 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
- 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. Group 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. Group 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. Group applied the portfolio approach in the majority of the identified revenue categories indicated above.

Santander Bank Polska S.A. Group 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. Group 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. Group because revenue derived from financial instruments offered by Santander Bank Polska S.A. Group 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. Group.

Santander Bank Polska S.A. Group elected to use the IFRS 9 provisions which provide for exemption of the obligation to restate comparative information for prior periods in relation to the changes arising from classification, measurement and impairment. Differences in the carrying amount of financial assets and liabilities resulting from the application of IFRS 9 are reported in retained earnings in equity 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 2017, 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 changes were applied by the Bank to the data for 2017 to make them comparable.

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".

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	627 600	50 605	576 995
eBusiness & payments	627 600	50 605	576 995
Fee and commission expenses	(315 547)	50 605	(264 942)
eBusiness & payments	(225 707)	21 404	(204 303)
Insurance commissions	(17 523)	2 752	(14 771)
Other	(72 317)	26 449	(45 868)

The above changes are for presentation purposes only.

2.5. Basis of preparation of financial statement

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

The financial statement of Santander Bank Polska S.A. Group has been prepared in accordance with the International Financial Reporting Standards (IFRS) adopted in the European Union. Santander Bank Polska S.A. Group 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
Other investment securities (units) (since 01.01.2018)	Fair value through profit or loss
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.

The accounting principles have been applied uniformly by individual units of Santander Bank Polska S.A. Group.

Santander Bank Polska S.A. Group 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. Group

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 calculated 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 S.A. Group's credit risk evaluation or the Santander Bank Polska S.A. Group's 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. Group, 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. Group 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. Group, or
 - (ii) national or local economic conditions that correlated with defaults on the assets in the Santander Bank Polska S.A. Group.

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 Group 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 Group 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 Group 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.

Scenario as at 31 December 2018		Baseline		Best case		Worst case	
Likelihood		60%		20%		20%	
		average, next 3 2019		average, next 3 2019		average, next 3 2019	
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%	
		average, next 3 2018		average, next 3 2018		average, next 3 2018	
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 Group

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 24.1m, while in the best case scenario only, allowances would be lower by PLN 16.0m. The above estimates include the portfolio and scenarios as at 31 December 2018 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 65.47m, given the value of the portfolio as at 31 December 2018.

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 Group does not identify low credit risk exposures under IFRS 9 standard rules, which allows to recognize 12-month expected loss even in cease of significant increase of credit risk since initial recognition.

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

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 2.9. "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. Group, 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. Group's 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. Group 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. Group 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. Group 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. Group 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. Group 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. Group 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. Group 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:
 - condition 1: the exposure has been designated as measured at fair value (option) or
 - condition 2: the exposure may be settled net in cash or through another instrument or
 - condition 3: Santander Bank Polska S.A. Group sells the obligation immediately after its granting sanction or
 - condition 4: the obligation was sanctioned below the market conditions.

Santander Bank Polska S.A. Group 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. Group 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. Group 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. Group 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. Group 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. Group 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. Group 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. Group 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 44.

Classification of leases

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

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

Operating lease

In the case of lease contracts made by Santander Bank Polska S.A. Group 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. Group 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. Group 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. Group 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. Group 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. Group 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. Group, 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. Group 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 47 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. Group 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. Group determines their estimated economic life.

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

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

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

Other accounting estimates and judgements

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

See Note 52 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. Group assesses probability of the programme vesting which affects the programme value in the costs of the reporting period. Description of the share-based incentive scheme is contained in Note 53.

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 36.

Changes in judgements and estimates

In 2018, the scope of data covered by estimates changed in comparison with Santander Bank Polska S.A. Group's consolidated 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. Group, in addition to assessments that require estimates, makes various subjective assessments that may significantly affect the amounts recognized in financial statements.

Consolidation scope

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

According to the Management Board of Santander Bank Polska S.A. Group, investment in Santander Towarzystwo Funduszy Inwestycyjnych S.A. is an investment in a subsidiary for the purpose of preparation of the consolidated financial statement in the light of the strategy adopted by the ultimate parent entity. As at 31 December 2018, Santander Bank Polska S.A. co-owns Santander Towarzystwo Funduszy Inwestycyjnych S.A. with Banco Santander S.A. Both owners are members of Santander Bank Polska S.A. Group and each holds 50% of the shares in the company. In practice, Santander Bank Polska S.A. exercises control over the subsidiary company, Santander Towarzystwo Funduszy Inwestycyjnych S.A. due to the fact that:

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

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

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

- Santander Consumer Bank S.A. exercises control over PSA Finance Polska Sp. z o.o. as it has existing rights that give it the current ability to direct the relevant activities, namely the activities which materially influence the returns made by

PSA Finance Polska Sp. z o.o.. Taking into account the core business of PSA Finance Polska Sp. z o.o., which is leasing, activities supporting financial services, car lease and rental and activities of insurance agents and brokers, and the sector in which PSA Finance Polska Sp. z o.o. is active, Santander Bank Polska S.A. has decided that PSA Finance Polska Sp. z o.o. relevant activities are:

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

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

- As Santander Consumer Bank S.A. plays a key role in funding the activities of PSA Finance Polska Sp. z o.o., the former is exposed to variable returns from its investment into the investee and
- Santander Consumer Bank S.A. may use its power to affect returns from its investment into PSA Finance Polska Sp. z o.o. as the former does not act for or on behalf of another entity (acts as a principal rather than as an agent).

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

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

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

2.8. Basis of consolidation

Subsidiaries

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

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

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

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

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

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

Acquisition method

Santander Bank Polska S.A. Group applies the purchase method to account for acquisition of subsidiaries. Under this method, the acquirer has to:

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

The acquirer measures:

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

Joint ventures

Joint ventures are those entities over whose activities Santander Bank Polska S.A. Group has joint control, established by contractual agreement. In consolidated financial statements joint ventures are included using equity method.

Associates

Associates are those entities in which Santander Bank Polska S.A. Group has significant influence, but are not subsidiaries, neither joint ventures.

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

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

Transactions eliminated on consolidation

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

2.9. Accounting policies

With the exception of the changes described in point 2.3, the Santander Bank Polska S.A. Group 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. Group in relation to financial instruments, by December 31, 2017 they were described in point 2.10.

The accounting policies have been applied consistently by Santander Bank Polska S.A. Group entities.

Foreign currency

Foreign currency transactions

The Polish zloty (PLN) is the functional currency of the units which are members of Santander Bank Polska S.A. Group.

Transactions in foreign currencies are translated at the foreign exchange rate ruling at the date of the transaction. Resulting from these transactions monetary assets and liabilities denominated in foreign currencies, are translated at the foreign exchange rate ruling at the balance sheet date. Non-monetary assets and liabilities denominated in foreign currencies, which are stated at historical cost, are translated at the foreign exchange rate ruling at the date of the transaction. Non-monetary assets and liabilities denominated in foreign currencies that are stated at fair value are translated to the reporting currency at the foreign exchange rates ruling at the dates that the fair values were determined. Foreign exchange differences arising on translation are recognised in profit or loss except for differences arising on retranslation of 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. Group 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. Group 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. Group transfers a financial asset, and such operation meets the derecognition criteria specified further in this policy.

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

- Santander Bank Polska S.A. Group transfers contractual rights to the cash flows from that financial asset, or
- Santander Bank Polska S.A. Group 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. Group 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. Group 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. Group has no obligation to pay amounts to the eventual recipients unless it collects equivalent amounts from the original asset,
- Santander Bank Polska S.A. Group 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. Group 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. Group 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. Group 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. Group 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. Group transfers substantially all the risks and rewards of ownership, then it shall continue to recognise the financial asset;
- Santander Bank Polska S.A. Group 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. Group 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. Group 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. Group's 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. Group 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. Group 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. Group 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. Group derecognises a part of financial asset (or a group of similar financial assets).

Derecognition of financial liabilities

Santander Bank Polska S.A. Group 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. Group 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. Group repurchases a part of a financial liability, Santander Bank Polska S.A. Group 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. Group has made a prior decision to measure a financial asset at fair value through profit or loss, the Santander Bank Polska S.A. Group 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. Group 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 comprehensive income, it is measured at fair value through profit or loss.

Santander Bank Polska S.A. Group 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. Group measures at fair value through the profit or loss, unless Santander Bank Polska S.A. Group 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. Group 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. Group key management regarding a particular instrument.

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

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

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

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

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

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

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. Group:

- 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. Group 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. Group's stated objective for managing the financial assets is achieved and, specifically, how cash flows are realised. Santander Bank Polska S.A. Group 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. Group needs not hold all of those instruments until maturity. Thus, Santander Bank Polska S.A. Group's 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. Group 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. Group 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. Group 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. Group 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. Group manages the financial assets with the objective of realising cash flows through the sale of the assets. Santander Bank Polska S.A. Group 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. Group's objective will typically result in active buying and selling. Even though Santander Bank Polska S.A. Group 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. Group 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. Group 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. Group 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. Group as a result of external or internal changes and must be significant to the Santander Bank S.A. Polska Group's operations and demonstrable to external parties. Accordingly, a change in the business model of Santander Bank Polska S.A. Group will occur only when Santander Bank Polska S.A. Group 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. Group 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. Group with different business models.

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

If Santander Bank Polska S.A. Group 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. Group 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. Group has designated that financial asset to be measured at fair value through profit or loss.

For this purpose, Santander Bank Polska S.A. Group 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. Group 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. Group 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. Group since 1 August 2016;
- instruments providing for participation of Santander Bank Polska S.A. Group 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. Group.

Classification of financial liabilities

Santander Bank Polska S.A. Group 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. Group 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. Group (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. Group 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. Group 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. Group 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. Group 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. Group 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. Group 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. Group 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. Group 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. Group.

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

The calculation includes fees (e.g. arrangement, drawdown, renewal, restructure fees and fees for annexes which modify payments) transaction costs and all other premiums or discounts.

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

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. Group 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. Group 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. Group 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. Group 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. Group 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 undue 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. Group 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. Group 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. Group 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. Group 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.

Santander Bank Polska S.A. Group 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. Group 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. Group) 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 then recorded off balance sheet.

Impairment

General approach

Santander Bank Polska S.A. Group 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. Group 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. Group 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. Group 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. Group 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. Group 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. Group 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. Group measures the loss allowance at an amount equal to 12-month expected credit losses at the current reporting date.

Santander Bank Polska S.A. Group 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 Group for Impairment of Financial Instruments: "Measurement of the loss allowance for credit-impaired financial assets"), Santander Bank Polska S.A. Group 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. Group 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. Group 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. Group 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. Group 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. Group 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. Group 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. Group 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. Group continues using own estimates of risk parameters that are based on internal models, however with the necessary modifications in the context of IFRS 9 requirements (such as estimating the parameters over the lifetime of the exposure or taking into account future macroeconomic conditions). Santander Bank Polska S.A. Group 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. Group 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. Group 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. Group 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. Group 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. Group 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. Group, 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. Group 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. Group 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. Group 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. Group 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. Group presents a gain or loss on a financial liability that is designated as measured at fair value through profit or loss as follows:

- 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
- 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. Group.

If the requirements specified above would create or enlarge an accounting mismatch in the profit or loss of Santander Bank Polska S.A. Group, Santander Bank Polska S.A. Group 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. Group 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. Group 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. Group 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. Group 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. Group uses derivative financial instruments to hedge its exposure to FX risk and interest rate risk arising from Santander Bank Polska S.A. Group's 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. Group 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 the Santander Bank Polska S.A. Group's risk management objective and strategy for undertaking the hedge. The documentation includes identification of the hedging instrument, the hedged item or transaction and the nature of the risk being hedged. The Santander Bank Polska S.A. Group also documents, at inception and on ongoing basis, an assessment of the hedging instrument's effectiveness in offsetting the exposure to changes in the fair value of the hedged item.

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

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

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

1. 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
2. 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. Group discontinues hedge accounting. All profits or losses on the hedging instrument pertaining to the effective hedge recognised in other comprehensive income remains an element of equity until the forecast transaction occurs, when it is recognised in income statement.

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

Repurchase and reverse repurchase transactions

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

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

Subsequent expenditure

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

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.

Goodwill and Intangible assets

Goodwill

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

Licences, patents, licences and similar assets

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

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

Development costs

Santander Bank Polska S.A. Group 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. Group 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. Group:

- 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. Group 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. Group are stated at cost less accumulated amortisation and total impairment losses.

Expenditure on intangible assets

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

Amortisation

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

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

Other items of the statement of financial position

Fixed assets held for sale

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

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

Other trade and other receivables

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

Other liabilities

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

Equity

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

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

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

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

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

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

Revaluation reserve is comprised of adjustments relating to the valuation of 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.

Except for own equity, non-controlling interests are also recognised in Santander Bank Polska S.A. Group capital.

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. Group's assets and as such are not disclosed in the consolidated statement of financial position.

Capital payments (Dividends)

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

Provisions

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

Income statement

Net interest income

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

- The contract has been approved in writing, orally, or in accordance with other customary business practices and the parties are committed to perform their obligations in the contract.
- Santander Bank Polska S.A. Group can identify each party's rights regarding the assets.
- Santander Bank Polska S.A. Group 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. Group are expected to change as a result of the contract).
- It is probable that Santander Bank Polska S.A. Group will collect the consideration to which it will be entitled in exchange for the assets that will be transferred to the customer. In evaluating whether collectability of an amount of consideration is probable, Santander Bank Polska S.A. Group 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. Group 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. Group combines two or more contracts entered into at or near the same time with the same customer (or related parties of the customer), and accounts for the contracts as a single contract if one or more of the following criteria are met:

- the contracts are negotiated as a package with a single commercial objective;
- the amount of consideration to be paid in one contract depends on the price or performance of the other contract;
- 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. Group continues to apply IFRS 15 to the existing contract until the contract modification is approved.

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

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

Step 2: 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. Group is dealing with separate performance obligations.

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

- Santander Bank Polska S.A. Group does not provide a significant service of integrating the asset with other assets promised in the contract into a bundle of assets that represent the combined output for which the customer has contracted.
- The asset does not significantly modify or customise another 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. Group combines that asset with other promised assets until it identifies a bundle of assets that is distinct. In some cases, that would result in Santander Bank Polska S.A. Group 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. Group expects to be entitled to in exchange for assets promised. It represents the amount of the revenue that will be recognised as a result of performance of the contract. In addition to the amount of consideration, the transaction price should also reflect any highly 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. Group estimates the amount of consideration to which it will be entitled in exchange for transferring the promised assets to a customer. An amount of consideration can vary because of discounts, rebates, refunds, credits, price concessions, incentives, performance bonuses, penalties or other similar items.

Step 4: 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. Group, the indicators of the transfer of control include the following:

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

If any of the above criteria is satisfied, income 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.

Income from asset management is recognised in accordance with a 5-step model based on the value of assets provided to Santander Bank Polska Group for management. Pursuant to the agreements in place, Santander Bank Polska Group does not receive any upfront fees or additional commissions calculated after the end of the accounting year on the basis of factors beyond the Group's control.

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. Group splits realised income into a portion recognised as interest income according to effective interest rate method and a portion recognised as fee income. The Santander Bank Polska S.A. Group qualifies distributed insurance products as linked to loans in particular if the insurance product influences contractual provisions of a loan.

To determine what part of income is an integral part of the credit agreement recognised as interest income using effective interest rate, the Santander Bank Polska S.A. Group separates the fair value of the financial instrument offered and the fair

value of the intermediation service of insurance product sold together with such instrument. The portion that represents an element of the amortised cost of the financial instrument and the portion that represents remuneration for the agency services are split in proportion to the fair value of the financial instrument and the fair value of the agency service cost, respectively, relative to the sum of the two values.

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

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

Long-term employee benefits

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

Equity-settled share-based payment transactions

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

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

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

Cash-settled share-based payment transactions

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

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. Group and the amount of income can be measured reliably.

Profit on disposal of subsidiaries, associates and joint ventures

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

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

Gains on other financial instruments

Gains on other financial instruments include:

- gains and losses on disposal of equity instruments and debt instruments 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. Group uses fair value hedge accounting and cash flow hedge accounting. Details are presented in Note 42 "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. Group. These are primarily revenues and costs from the sale and liquidation of fixed assets, income from sale of other services, paid and received damages, penalties and fines.

Impairment losses on loans and advances

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

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

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. Group's cost in income statement on a straight-line basis over the lease term.

Finance lease payments

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

Tax on financial institutions

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

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

Corporate income tax

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

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

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. Group generates taxable profit allowing partial or wholly realisation of deferred tax assets. The carrying value of deferred tax assets is verified at the end of each reporting period. The Santander Bank Polska S.A. Group reduces the carrying amount of the deferred tax asset to the realizable value - that is, to the extent that it is probable that taxable income will be sufficient to partially or fully realize the deferred tax asset.

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

2.10. Accounting principles applicable until 31 December 2017

This section presents the accounting principles applied by Santander Bank Polska S.A. Group 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. Group 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:
 1. it was acquired or incurred principally for the purpose of selling or repurchasing in the near term;
 2. 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;
 3. 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. Group at fair value through profit and loss.

In 2017, Santander Bank Polska S.A. Group 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. Group 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. Group upon initial recognition designated as at fair value through profit or loss;
- those that Santander Bank Polska S.A. Group 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. Loans and receivables also included finance lease receivables of Santander Leasing S.A., Santander Consumer Multirent Sp. z o.o. and PSA Finance Polska Sp. z o.o. and factoring receivables of Santander Factoring Sp. z o.o.

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:

- (1) loans and receivables;
- (2) held-to-maturity investments;
- (3) financial assets measured at fair value through profit and loss.

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

- 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. Group, 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. Group 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. Group, or
 - (ii) national or local economic conditions that correlated with defaults on the assets in the Santander Bank Polska S.A. Group.

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. Group 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. Group 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. Group 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. Group 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. Group's credit risk evaluation or the Santander Bank Polska S.A. Group's 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. Group reviews regularly the methodology and assumptions used for estimating future cash flows in order to reduce any differences between estimates and actual impairment charge experience.

IBNR (Incurred But Not Reported) impairment charges 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. Group;
- 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.

Impairment calculation methods were standardised across the Santander Bank Polska S.A. Group.

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. Group 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. Group 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. Operating segments reporting

Presentation of information about business segments in Santander Bank Polska Group bases on management information model which is used for preparing of reports for the Management Board, which are used to assess performance of results and allocate resources. Operational activity of Santander Bank Polska Group has been divided into five segments: Retail Banking, Business & Corporate Banking, Corporate & Investment Banking (In 2nd quarter of 2018 the name of Global Corporate Banking was changed to Corporate and Investment Banking, the criteria of customers assignment to this business segment was maintained unchanged), ALM (Assets and Liabilities Management) and Centre, and Santander Consumer. They were identified based on customers and product types.

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

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

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

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

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

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

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

Santander Bank Polska Group focuses its operating activity on the domestic market.

In 2018 introduced the following changes:

- customer resegmentation between business segments; Once a year, Santander Bank Polska Group carry out the resegmentation / migration of customers between operating segments which results from the fact that customer meet the criteria of assignment for different operating segment than before. This change is intended to provide services at the highest level of quality and tailored to individual needs or the scale of customer operations;
- in the further product offer customization and improvement of services efficiency, process of portfolio management and providing services for medium companies, which have been presented in Retail Banking Segment yet, were transferred to Business & Corporate Banking on the 30.05.2018. Results from those clients for 01.01.2018-31.12.2018, balance sheet at the date 31.12.2018, as well as comparative figures involve the change described above.

Comparable data are adjusted accordingly.

On 9.11.2018 r. acquisition of organized part of Deutsche Bank Polska took place. Results, assets and liabilities of customers of acquired organized part of Deutsche Bank Polska were presented in Retail Banking segment and Business and Corporate Banking segment, according to the principles of segmentation and income and cost identification in Santander Bank Polska Group. Gain on acquisition of organized part of Deutsche Bank Polska and acquisition related costs were presented in ALM and Center segment.

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

Retail Banking

Retail Banking generates income from the sale of products and services to personal customers and small companies. In the offer for customers of this segment there are a wide range of savings products, consumer and mortgage loans, credit and debit cards, insurance and investment products, clearing services, brokerage house services, GSM phones top-ups, foreign payments and Western Union and private-banking services. For small companies, the segment provides, among others, lending and deposit taking services, cash management services, leasing, factoring, letters of credit and guarantees.

Furthermore, the Retail Banking segment generates income through offering asset management services within investment funds and private portfolios.

Business & Corporate Banking

Business & Corporate Banking segment covers products and activities targeted at business entities, local governments and the public sector, including medium companies. In addition to banking services covering lending and deposit activities, the segment provides services in the areas of cash management, leasing, factoring, trade financing and guarantees. It also covers insourcing services provided to retail customers based on mutual agreements with other banks and financial institutions.

Corporate & Investment Banking

In the Corporate & Investment Banking segment, Santander Bank Polska Group derives income from the sale of products and services to the largest international and local corporations, including:

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

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

ALM and Centre

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

Santander Consumer

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

Consolidated income statement by business segments

	Segment Retail Banking *	Segment Business and Corporate Banking	Segment Corporate & Investment Banking	Segment ALM and Centre	Segment Santander Consumer	Total
01.01.2018-31.12.2018						
Net interest income	2 646 474	683 621	219 913	671 991	1 520 406	5 742 405
incl. internal transactions	(129 645)	(62 862)	4 595	189 398	(1 486)	-
Net fee and commission income	1 300 304	385 062	242 136	910	129 390	2 057 802
incl. internal transactions	92 707	69 195	(173 905)	15 319	(3 316)	-
Other income	37 195	53 766	114 950	537 794	39 824	783 529
incl. internal transactions	(1 291)	47 164	(43 810)	14 509	(16 572)	-
Dividend income	-	-	1 127	98 963	26	100 116
Operating costs	(1 945 484)	(416 536)	(228 514)	(273 353)	(571 612)	(3 435 499)
incl. internal transactions	(10 775)	(1 642)	-	16 034	(3 617)	-
Depreciation/amortisation	(213 102)	(38 330)	(15 239)	(23 954)	(42 845)	(333 470)
Impairment losses on loans and advances	(613 739)	(157 730)	(20 679)	(21 396)	(271 524)	(1 085 068)
Share in net profits (loss) of entities accounted for by the equity	-	-	-	62 667	-	62 667
Tax on financial institutions	-	-	-	(427 069)	(39 261)	(466 330)
Profit before tax	1 211 648	509 853	313 694	626 553	764 404	3 426 152
Corporate income tax						(727 139)
Consolidated profit for the period						2 699 013
of which:						
attributable to owners of Santander Bank Polska SA						2 365 222
attributable to non-controlling interests						333 791

* Includes individual customers, small companies and Wealth Management (private banking and Santander TFI SA)

Consolidated statement of financial position by business segment

	Segment Retail	Segment Business and Corporate Banking	Segment Corporate&Investment Banking	Segment ALM and Centre	Segment Santander Consumer	Total
31.12.2018	Banking *	Banking	ent Banking	and Centre	Consumer	
Loans and advances to customers	72 010 663	36 321 090	13 347 595	-	15 781 030	137 460 378
Investments in associates	-	-	-	891 952	-	891 952
Other assets	9 485 823	2 426 090	10 651 081	40 872 849	4 064 687	67 500 530
Total assets	81 496 486	38 747 180	23 998 676	41 764 801	19 845 717	205 852 860
Deposits from customers	95 095 107	28 077 154	11 715 093	5 854 140	8 875 164	149 616 658
Other liabilities and equity	5 875 018	4 560 173	12 976 587	21 853 871	10 970 553	56 236 202
Total equity and liabilities	100 970 125	32 637 327	24 691 680	27 708 011	19 845 717	205 852 860

* includes individual customers, small companies and Wealth Management (private banking and Santander TFI SA)

Consolidated income statement by business segments

	Segment Retail Banking *	Segment Business and Corporate Banking	Segment Corporate&In vestment Banking	Segment ALM and Centre	Segment Santander Consumer	Total
01.01.2017-31.12.2017						
Net interest income	2 379 942	629 320	207 052	708 429	1 352 154	5 276 897
incl. internal transactions	(110 415)	(52 816)	1 138	161 563	530	-
Net fee and commission income	1 311 803	342 218	230 581	123	128 401	2 013 126
incl. internal transactions	77 641	62 569	(152 940)	14 729	(1 999)	-
Other income	69 278	77 643	86 728	96 484	66 687	396 820
incl. internal transactions	3 815	47 016	(46 825)	(45 447)	41 441	-
Dividend income	-	-	546	76 249	21	76 816
Operating costs	(1 813 598)	(387 788)	(217 900)	(88 653)	(545 542)	(3 053 481)
incl. internal transactions	(8 468)	(1 548)	-	14 015	(3 999)	-
Depreciation/amortisation	(191 650)	(29 689)	(16 680)	(45 617)	(35 297)	(318 933)
Impairment losses on loans and advances	(433 917)	(130 662)	(10 501)	(4 576)	(110 817)	(690 473)
Share in net profits (loss) of entities accounted for by the equity	-	-	-	58 264	-	58 264
Tax on financial institutions	-	-	-	(387 988)	(35 827)	(423 815)
Profit before tax	1 321 858	501 042	279 826	412 715	819 780	3 335 221
Corporate income tax						(816 707)
Consolidated profit for the period						2 518 514
of which:						
attributable to owners of Santander Bank Polska SA						2 213 054
attributable to non-controlling interests						305 460

* includes individual customers, small companies and Wealth Management (private banking and Santander TFI SA)

Consolidated statement of financial position (by business segment)

	Segment				Segment	
	Business and	Segment	Corporate	Segment	Santander	
	Retail	Corporate	& Investment	ALM	Consumer	Total
31.12.2017	Banking *	Banking	Banking	and Centre		
Loans and advances to customers	53 569 956	27 889 630	11 830 105	-	14 550 206	107 839 897
Investments in associates	-	-	-	889 372	-	889 372
Other assets	5 397 281	1 359 885	3 845 759	29 444 552	3 897 698	43 945 175
Total assets	58 967 237	29 249 515	15 675 864	30 333 924	18 447 904	152 674 444
Deposits from customers	69 496 656	21 246 416	8 128 154	4 454 999	8 154 910	111 481 135
Other liabilities and equity	4 591 627	3 362 391	5 357 993	17 588 304	10 292 994	41 193 309
Total equity and liabilities	74 088 283	24 608 807	13 486 147	22 043 303	18 447 904	152 674 444

* includes individual customers, small companies and Wealth Management (private banking and Santander TFI SA)

4. Risk management

Santander Bank Polska Group is exposed to a variety of risks in its ordinary business activities. The objective of risk management is to ensure that the Group 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 Group'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 Group modifies and develops risk management methods on an ongoing basis, taking into consideration changes in the Group'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 Group'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 Group. 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 Group, 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 Group, 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 Group 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 Group 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.

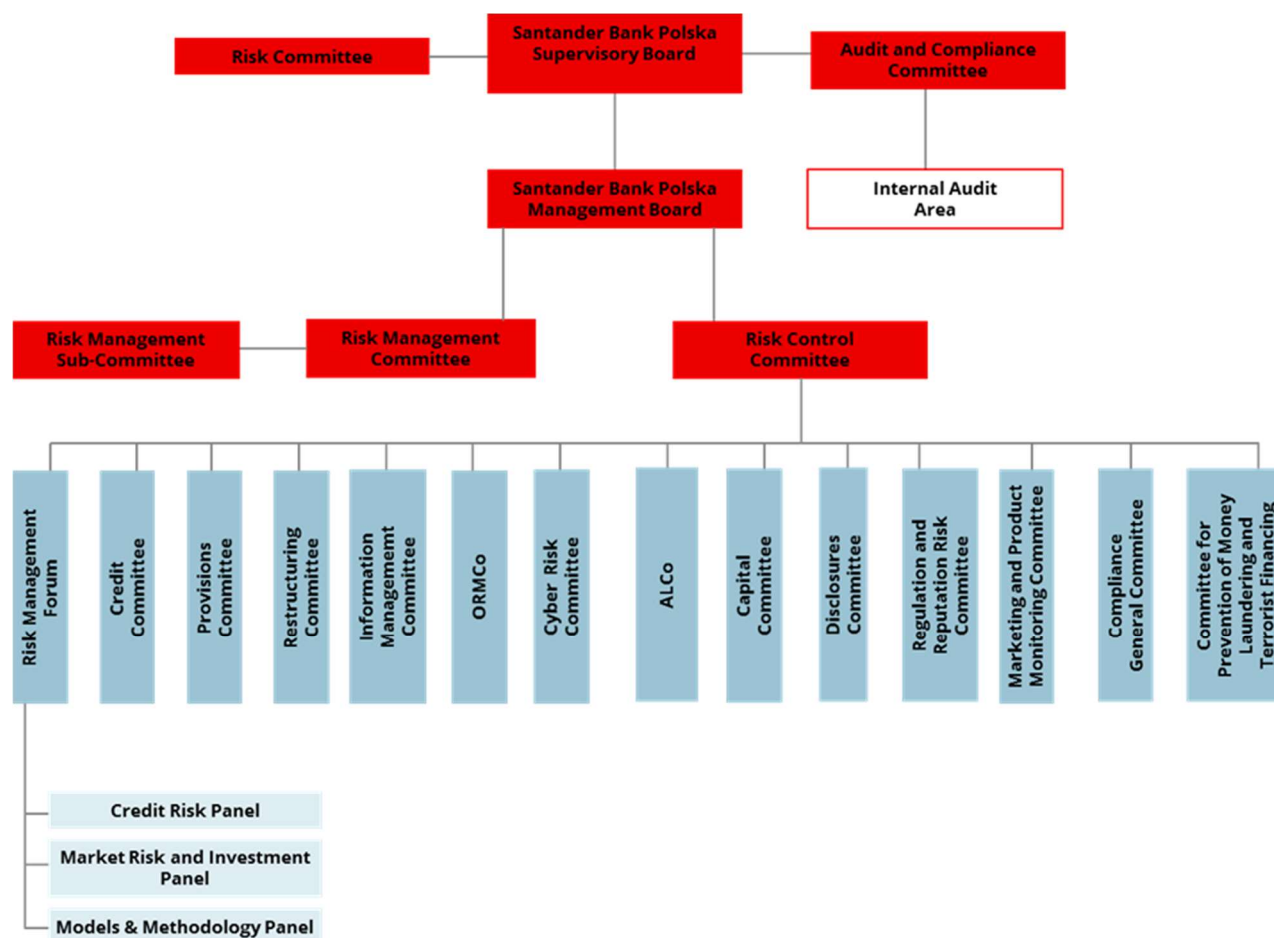
The **General Compliance Committee** is responsible for setting standards with respect to the management of compliance risk and the codes of conduct adopted by the Group.

The **Regulatory and Reputational Risk Committee** is responsible for monitoring and taking decisions on cases relating to the Group's compliance with law, regulatory guidelines and market/ industry standards relating to the Group'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 Group'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 Group, 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 Group is exposed to a variety of risks affecting its strategic goals. The Group continuously analyses the risks, identifies their sources, creates the relevant risk management mechanisms including among others the measurement, control, mitigation and reporting. The key risks the Group 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 Group companies are set out in relevant internal policies relating to the management of individual risk types.

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

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

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

Credit risk is defined as the possibility of suffering a loss as a result that a borrower will fail to meet its credit obligation, including interest and fees. Credit risk arises from the impairment of credit assets and contingent liabilities, resulting from worsening of the borrower's credit quality. Credit risk measurement is based on the estimation of credit risk weighted assets, with the relevant risk weights representing both the probability of default and the potential loss given default of the borrower.

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

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

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

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

The year 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 Group 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 Group 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 Group will continue this work also in 2019. In 2018, the Group improved its credit exposure monitoring tools to ensure faster identification of potential threats both at the portfolio level and at the level of individual exposures. At the same time, the Group modified its monitoring strategies, focusing on early measures designed to limit the effects of potential risk materialisation.

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

Risk Management Forum

The credit risk oversight in Santander Bank Polska Group is performed by Credit Policy Panel (CPP) operating within the Risk Management Forum. Its key responsibilities include development and approval of the best sectoral practice, industry analyses, credit policies as well as implementation of grading and assessment systems aimed at ensuring sustainable growth of the credit portfolio. To align the Group's management processes with the current strategic goals, three sub-

committees were established within the CPP with a responsibility for the key customer segments: retail segment, SME segment and the business/corporate segment. The oversight over the credit risk models is the responsibility of the Models and Methodology Panel.

Risk Management Division

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

Credit Policies

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

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

Credit Decision Making Process

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

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

Credit Grading

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

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

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

Credit Reviews

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

Collateral

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

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

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

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

Retail customers

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

Business customers

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

Collateral management process

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

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

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

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

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

Financial effect of the collateral

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

The table below present financial effect of collateral of Santander Bank Polska as at 31.12.2018:

Financial effect of collateral	Gross Amount	Financial effect of collateral
Loans and advances to customers		
housing loans	49 210 998	(287 283)
business	58 129 890	(950 337)
Total balance sheet	107 340 888	(1 237 621)
Total off-balance sheet	26 921 869	(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	24 642 271	(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 Group's condition. Stress tests are composed of assessment of potential changes in credit portfolio quality when faced with adverse conditions. The process also delivers management information about adequacy of agreed limit and internal capital allocation.

Impairment calculation

Santander Bank Polska Group 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 POCl (purchased or originated credit-impaired).

In the case of classification into stage 3, the Group applies objective indications of impairment, as defined in accordance with the Basel Committee's recommendations and Recommendation R. The Group did not introduce any material changes in respect of IFRS 9 implementation.

The Group estimates ECL 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 Group 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 Group's credit policies and recovery strategies, which is designed to ensure appropriate level of impairment allowances.

The tables below present Santander Bank Polska Group'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 assessed					
	up to 50%	-	-	1 176 551	1 176 551
	50% - 70%	-	-	323 594	323 594
	70% - 85%	-	-	85 467	85 467
	over 85%	-	-	485 744	485 744
Gross amount		-	-	2 071 356	2 071 356
Impairment					(796 150)
Net amount					1 275 206
Exposures classified to Stage 3-Collectively assessed					
	up to 50%	110 452	157 801	261 005	529 258
	50% - 70%	203 927	135 295	84 148	423 371
	70% - 85%	718 346	70 643	96 206	885 195
	over 85%	715 846	216 347	862 289	1 794 481
Gross amount		1 748 571	580 086	1 303 648	3 632 305
Impairment					(2 440 143)
Net amount					1 192 162
Exposures classified to Stage 2					
	up to 0.10%	880	824	351 289	352 993
	0.10%-0.30%	5 947	12 412	145 580	163 938
	0.30%-0.65%	13 091	49 430	235 301	297 822
	over 0.65%	1 407 661	1 155 804	2 317 873	4 881 338
Gross amount		1 427 579	1 218 470	3 050 043	5 696 092
Impairment					(530 276)
Net amount					5 165 816
Exposures classified to Stage 1					
	up to 0.10%	1 648 465	42 706 777	31 475 353	75 830 594
	0.10%-0.30%	3 772 891	1 751 336	13 445 781	18 970 009
	0.30%-0.65%	4 767 876	1 948 202	6 724 457	13 440 535
	over 0.65%	10 645 035	809 550	8 167 580	19 622 165
Gross amount		20 834 267	47 215 866	59 813 171	127 863 304
Impairment					(564 638)
Net amount					127 298 666
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		121 116	228 107	410 083	759 306
Impairment					(53 115)
Net amount					711 447
Loans and advances to customers measured at amortised cost					135 643 297

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

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 not held for trading mandatorily measured at fair value through profit or loss	Financial assets held for trading - debt securities
2 (A+ to A-)	1 873 359	-	-	37 958 096	134 741	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	195 372	324 895	106 374	27 270	-	951
Total	2 936 214	1 248 750	106 374	38 221 051	134 741	8 671 723

* according to Fitch

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

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). 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 Group adheres to the standards provided for in the Banking Law with regard to the concentration of risk bearing exposures to a single entity or a group of entities connected in terms of capital or organisation. As at 31.12.2018, pursuant to art. 71 of the Banking Law Act, the maximum limits for the Group amounted to:

- PLN 5,709,939 k (25% of Group's own funds).

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

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

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

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

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

Industry code (PKD)	Industry description	Total credit exposure	Balance sheet exposure incl. towards subsidiaries	Committed credit lines, guarantees, treasury limits and capital investments
61	TELECOMMUNICATION	1 716 665	1 553 263	163 402
35	POWER INDUSTRY	1 490 000	106 364	1 383 636
68	REAL ESTATE SERVICES	1 090 108	986 831	103 278
47	RETAIL	1 065 552	729 806	335 746
07	MINING	1 010 461	191 571	818 890
70	CONSULTING	984 490	760 018	224 472
06	MINING	828 520	253 495	575 025
35	POWER INDUSTRY	810 000	210 500	599 500
68	REAL ESTATE SERVICES	683 281	551 281	132 000
19	RAFINERY	671 031	150 500	520 531
64	OTHER FINANCIAL SERVICES	665 155	-	665 155
20	CHEMICAL INDUSTRY	619 796	581 781	38 014
41	CONSTRUCTION	602 177	531 872	70 305
41	CONSTRUCTION	547 789	8 789	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
70	CONSULTING	369 147	280 215	88 932
68	REAL ESTATE SERVICES	367 194	354 509	12 685
68	REAL ESTATE SERVICES	360 005	343 733	16 272
Total gross exposure		15 177 809	8 750 565	6 427 244

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

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

Industry concentration

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

As at 31.12.2018, the highest concentration level was recorded in the "distribution" sector (12% of the Santander Bank Polska Group exposure), "manufacturing" (11%) and "property" (7%).

Groups of PKD by industries:

Industry	Gross exposure	
	31.12.2018	31.12.2017
Distribution	17 200 457	14 535 418
Manufacturing	15 396 691	11 234 366
Property	9 787 588	7 958 554
Transportation	4 283 517	3 472 978
Energy	3 436 625	3 602 532
Agriculture	2 768 917	2 528 768
Construction	1 843 443	1 509 824
Financial sector	1 160 715	1 449 395
Other industries	10 220 993	8 562 299
A Total Business Loans	66 098 945	54 854 134
B Retail (including mortgage loans)	73 913 444	57 822 414
A+B Santander Bank Polska Group portfolio	140 012 390	112 676 548
C Other receivables (commercial bonds)	15 229	9 479
A+B+C Total Santander Bank Polska Group	140 027 619	112 686 027

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 Group on the existing contractual terms. The concession may involve a modification of the previous terms and conditions of a debt contract or its total or partial refinancing. The purpose of debt restructuring is to better align repayment terms with the current and projected financial standing of the customer, minimise default risk and/or maximise recovery.

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

The decision on granting a concession towards a customer with insufficient debt service ability is based on an analysis of its financial standing, assessment of repayment capacity under the new terms, analysis of existing collateral, assessment of the

willingness to repay and the relationship history. The concessions depend on the results of the assessment and may involve in particular: moratorium on payments, modification of repayment schedule (reduced payments), interest capitalisation, extension of maturity etc. Such solutions may be applied to both personal and business customers.

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

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

Accounting principles applicable to financial assets subject to forbearance are the same as in the case of other performing or 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).

	Carrying amount	
	31.12.2018	31.12.2017
Loans and advances to customers- gross amount		
under forbearance measure:	3 325 828	3 460 838
corporate exposures	2 016 956	1 972 878
mortgage exposures	852 271	1 227 239
individuals exposures	456 602	260 721
Allowance for impairment - forbearance clients	(1 080 111)	(847 582)
of which: individually impaired	(413 468)	(413 727)
Loans and advances to forbearance clients- net amount	2 245 718	2 613 256

Analysis of credit quality of financial assets subject to forbearance:

Loans and advances to customers under forbearance	Gross exposure		Collateral value		Allowance for impairment	
	31.12.2018	31.12.2017	31.12.2018	31.12.2017	31.12.2018	31.12.2017
Loans and advances -impaired	2 206 205	1 774 300	9 678 922	9 354 162	(940 789)	(793 791)
Loans and advances -unimpaired	1 119 623	1 686 538	3 727 276	3 079 351	(139 322)	(53 791)
non-overdue	873 881	1 316 773	3 357 096	2 488 941	(116 414)	(32 470)
from 1 to 30 days overdue	145 947	254 422	206 100	421 737	(10 913)	(13 531)
from 31 to 60 days overdue	69 451	76 150	123 320	113 030	(7 327)	(3 916)
from 61 to 90 days overdue	30 344	39 193	40 761	55 643	(4 668)	(3 874)
Total gross amount	3 325 828	3 460 838	13 406 198	12 433 513	(1 080 111)	(847 582)

Interest income on assets subject to forbearance was PLN 75,553 k as at 31 December 2018 and PLN 82,418k as at 31 December 2017.

**Loans and advances to customers under forbearance by geographical region
(gross amount)**

	31.12.2018	31.12.2017
Dolnośląskie	386 172	357 370
Kujawsko-Pomorskie	165 662	67 175
Lubelskie	52 473	50 461
Lubuskie	63 977	61 876
Mazowieckie	1 032 996	1 376 072
Małopolskie	152 488	222 240
Opolskie	38 151	30 244
Podkarpackie	51 390	34 630
Podlaskie	46 203	38 677
Pomorskie	201 938	180 989
Warmińsko-Mazurskie	46 792	41 277
Wielkopolskie	237 721	187 622
Zachodniopomorskie	99 952	76 702
Śląskie	636 155	574 185
Świętokrzyskie	30 191	76 776
Łódzkie	83 567	84 542
Total	3 325 828	3 460 838

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	193 056	192 709
Property	541 962	799 621
Manufacturing	232 664	169 215
Agriculture	26 344	69 065
Transportation	42 281	35 114
Individuals	1 308 872	1 487 960
Total	3 325 828	3 460 838

	31.12.2018	31.12.2017
Net carrying amount at beginning of the period	2 613 256	3 087 089
Allowance for impairment	(232 528)	107 013
Loans and advances derecognised during the period	(1 170 904)	(144 515)
Loans and advances recognised during the period	1 198 263	1 174 068
Other changes/repayments	(162 369)	(1 610 399)
Net carrying amount at the end of the period	2 245 718	2 613 256

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

The activity and strategies on market risk management are directly supervised by the Risk Management Forum 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 Group is to reduce the impact of variable market factors on the Group's profitability and to grow income within the strictly defined risk limits while ensuring the Group's liquidity and market value.

The market risk policies of Santander Bank Polska Group 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 Group'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 Group's trading activity is subject to a system of measures and limits, including Value at Risk, stop loss, position limits and sensitivity limits. These limits are approved by the Risk Management Forum, the bank's Management Board and the Supervisory Board.

The Financial Risk Department within the Risk Management Division is responsible for ongoing 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 Group. 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 Group 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 Group's banking book is the risk of adverse impact of interest rate changes on the Group's income and the value of its assets and liabilities. 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 Group 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 Group, 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 Group 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.

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 Group.

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.

1 day holding period	NII Sensitivity		MVE Sensitivity	
	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.

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

Interest rate risk	VAR	
	31.12.2018	31.12.2017
1 day holding period		
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 Group'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 Group does not maintain open positions on currency options. Transactions made with customers are immediately closed in the wholesale market thus limiting the Group'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	
	31.12.2018	31.12.2017
1 day holding period		
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 Group'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 Group'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 banks	8 357 459	356 755	25 593	77 185	90 560	8 907 552
Loans and advances to banks	477 266	1 514 273	6 225	682 633	255 817	2 936 214
Loans and advances to customers	106 938 091	18 778 050	10 514 721	1 212 066	17 450	137 460 378
Financial assets available for sale	36 950 810	1 468 753	-	759 538	-	39 179 101
Selected assets	152 723 626	22 117 831	10 546 539	2 731 422	363 827	188 483 245
LIABILITIES						
Deposits from banks	2 573 121	231 376	6 799	17 487	4 145	2 832 928
Deposits from customers	126 219 287	16 906 252	417 798	4 614 750	1 458 572	149 616 659
Subordinated liabilities	1 108 574	1 535 767	-	-	-	2 644 341
Selected liabilities	129 900 982	18 673 395	424 597	4 632 237	1 462 717	155 093 928

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

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	
	31.12.2018	31.12.2017
1 day holding period		
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 Group 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 Group;
- 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 Group 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 Group'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 Group's business by maintaining structural liquidity ratios at pre-defined levels.

The Group 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 Group carries out the Internal Liquidity Adequacy Assessment Process (ILAAP), which is designed to ensure that the Group can effectively control and manage liquidity risk. In particular, the ILAAP ensures that the Group:

- 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 Group in terms of liquid assets, prudent funding profile and the Group'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 Group 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;
- 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 Group 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 and Group 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)

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)	0
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.

Table 1:

Scope of consolidation (solo) Currency and units (PLN million)		Total unweighted value (average)				Total weighted value (average)			
		31.12.2018	30.09.2018	30.06.2018	31.03.2018	31.12.2018	30.09.2018	30.06.2018	31.03.2018
Quarter ending									
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	<i>Stable deposits</i>	43 839	43 066	42 619	42 151	2 192	2 153	2 131	2 108
4	<i>Less stable deposits</i>	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
<i>Operational deposits (all counterparties) and deposits in networks of</i>									
6	<i>cooperative banks</i>	5 646	5 379	5 341	5 223	1 409	1 343	1 333	1 304
7	<i>Non-operational deposits (all counterparties)</i>	21 655	18 384	16 877	15 958	11 014	9 564	8 965	8 534
8	<i>Unsecured debt</i>	103	124	167	209	103	124	167	209
9	Secured wholesale funding	0	0	0	0	0	0	0	0
10	Additional requirements	20 588	20 761	21 525	22 459	3 967	3 988	4 086	4 229
11	<i>Outflows related to derivative exposures and other collateral requirements</i>	1 209	1 366	1 398	1 462	1 209	1 365	1 398	1 463
12	<i>Outflows related to loss of funding on debt products</i>	0	0	0	0	0	0	0	0
13	<i>Credit and liquidity facilities</i>	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
<i>(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</i>									
EU-19a	<i>currencies)</i>					-	0	0	0
EU-19b	<i>(Excess inflows from a related specialised credit institution)</i>					-	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	<i>Fully exempt inflows</i>	0	0	0	0	0	0	0	0
EU-20b	<i>Inflows Subject to 90% Cap</i>	0	0	0	0	0	0	0	0
EU-20c	<i>Inflows Subject to 75% Cap</i>	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 Group uses secured instruments to fund its activity to a limited degree only. However, in accordance with the existing contractual provisions, if the Group'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 Group adopted the definition of operational risk as formulated by the Basel Committee: Operational risk is the risk of loss resulting from inadequate or failed internal processes, people and systems or from external events.

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

Santander Bank Polska Group has an integrated risk management framework ensuring that all risks having material impact on the bank's operations are identified, measured, monitored and controlled. Employees across Santander Bank Polska Group are involved in operational risk management – this process covers a number of interrelated concepts. Operational risk is inherent in all the Group's business processes, including outsourced functions or services delivered jointly with third parties.

Santander Bank Polska Group has drawn up 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 Group. ORMCo is the main forum for discussions on operational risk. It sets the strategic direction for operational risk management and determines and monitors objectives for managing operational risk, including business continuity, information security, outsourcing/ insourcing risk and money laundering risk. As part of ORMCo, there are dedicated forums which deal with specific operational risk aspects: the Fraud Prevention Forum and the Insurance Forum. The results of this work are reported to the Risk Control Committee.

In view of a growing cyber threat, the Cyber Risk Committee was set up as a forum for direct cooperation and communication among all organisational units involved in the processes related to cyber security in a broad sense. The Committee also supervises the adherence to the cyber security strategy at Santander Bank Polska S.A.

Santander Bank Polska Group uses the following operational risk management tools:

- Identification and assessment of operational risk

The primary tool for identification and assessment of operational risk is self-assessment. In the self-assessment process, Santander Bank Polska Group identifies the risks it may be exposed to when delivering its functions, assesses inherent and residual risks in terms of their likelihood and impact of potential threats, and evaluates the design and effectiveness of the existing control environment.

In addition, the process of identification and assessment of operational risk is supported by other tools dedicated to specific risk aspects, including: scenario analyses, business impact analyses and an analysis of risk in new initiatives.

- Reporting on operational risk events

Each organisational unit is required to report on operational risk events. Relevant operational risk events are escalated to senior management using a fast-track procedure. The Group maintains a database of operational risk events identified across Santander Bank Polska Group. The data are used to analyse the causes and consequences of operational risk events, facilitate the lessons learned process and implement remedial and preventive actions.

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

- Analysis of risk indicators

Operational risk indicators are the primary tool for monitoring operational risk. They provide an early warning of emerging threats and support the tracking of risks in the Group. The monitoring uses financial, operational and technological metrics.

- Defining risk mitigation actions

The process of managing operational risk mitigants is designed to eliminate or reduce operational risk. Risk mitigation measures are determined based on the results of analyses carried out using various operational risk tools (including operational risk 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 plan 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 Group that critical business processes may be restored at the required service level and within the agreed time frame. Santander Bank Polska Group has backup locations in place where critical processes can be restored and continued should an incident occur.

- Information security

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

Santander Bank Polska S.A. has the Information Security Management System in place which has a certificate of compliance with the ISO/IEC 27001:2013 standard. Information security management includes supervision over information security issues in the business environment of Santander Bank Polska Group and assessment of specific information and IT system security requirements.

- Insurance

For the purpose of operational risk mitigation, Santander Bank Polska Group also uses financial risks insurance, motor insurance, property insurance and professional indemnity insurance.

- Periodic reporting to the Risk Management Committee and the Supervisory Board

The aim of operational risk reporting is to provide up-to-date and adequate information to the management team. The reporting covers operational risk issues and includes information related to inter alia: operational risk events and losses, risk indicators and information on defined risk reduction activities.

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 and international regulations concerning the type of offered products and service delivery methods applied by the bank and the Santander Bank Polska Capital Group (in particular: the legislation on consumer and competition protection, capital markets, financial markets etc.);
- good practice codes and other regulations implemented by the Group, including in connection with among others 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 appropriate 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 test 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 Group is exposed to (with the focus on new products and services, prevention of using financial systems for 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;
- 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 and Risk Management Division in terms of managing of the reputational risk defined as the risk of deterioration of the Bank's and Santander Group's image perceived by the Bank's and Group's customers, employees, shareholders and communities arising from materialisation of other risks, including individual types of compliance risk.

Santander Bank Polska Group also has specialised committees supporting the management of the compliance risk in specific areas. These committees consist of the representatives of key business units and risk management units who are competent and duly authorised to make informed decisions and provide high-quality advice. The Compliance Area coordinates the following committees:

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

5. Capital management

Introduction

It is the policy of Santander Bank Polska Group 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. All decisions regarding any increase or decrease in capital are taken ultimately 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 S.A. were as follows:

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

for Santander Bank Polska Group, those ratios were as follows:

- Tier 1 capital ratio of 11.73%;
- total capital ratio of 13.85%.

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 S.A. 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 S.A. was set at 0.51 p.p. above the total capital ratio for Santander Bank Polska S.A. 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 S.A.) 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 S.A.). In turn, the value of additional capital requirement for Santander Bank Polska Group is 0.47 p.p. for the total capital ratio and 0.35 p.p. for the Tier 1 ratio and 0.26 p.p. for the Common Equity Tier 1 ratio.

- The capital buffer for Santander Bank Polska S.A. as other systemically important institution.

On 4 October 2017, the KNF identified Santander Bank Polska S.A. as other systemically important institution and imposed on it an additional capital buffer of 0.5 p.p. Santander Bank Polska Group maintains the capital buffer at the same level.

- 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%;

for Santander Bank Polska Group, those ratios will be as follows:

- Tier 1 capital ratio of 12.35%;
- total capital ratio of 14.47%.

Regulatory Capital

The capital requirement for Santander Bank Polska Group 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 Group 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.

The table below presents the calculation of the capital ratio for Santander Bank Polska Group 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:	11 434 229	9 520 249
Ia - due to credit risk & counterparty credit risk	10 202 471	8 361 481
Ib - due to market risk	83 135	107 752
Ic - due to credit valuation adjustment risk	24 918	42 400
Id - due to operational risk	1 123 705	1 008 616
II Total own funds*	25 266 004	22 314 566
III Reductions	2 426 250	2 454 088
IV Own funds after reductions (II-III)	22 839 754	19 860 478
V CAD [IV/(I*12.5)]	15,98%	16,69%
VI Tier I ratio	14,11%	15,28%

*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 the KNF's consent of 28 September 2018.

Internal Capital

Notwithstanding the regulatory methods for measuring capital requirements, Santander Bank Polska S.A. 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 Group 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 S.A. customers and the loss given default (LGD).

The Group performs an internal assessment of capital requirements, including under stressed conditions, taking into account different macroeconomic scenarios.

Internal capital estimation models are assessed and reviewed annually to adjust them to the scale and profile of the business of Santander Bank Polska S.A. 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 S.A. 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 33.

6. Net interest income

01.01.2018-31.12.2018				
Interest income and similar to interest	Interest income on			Total
	financial assets measured at amortised cost	financial assets measured at fair value through other comprehensive income	Income similar to interest - financial assets measured at fair value through profit or loss	
Loans and advances to enterprises	1 838 764	4 179	2 037	1 844 980
Loans and advances to individuals, of which:	3 909 097	-	119 554	4 028 651
Home mortgage loans	1 232 081	-	-	1 232 081
Debt securities incl.:	-	729 199	13 695	742 894
Investment securities	-	729 199	-	729 199
Trading portfolio	-	-	13 695	13 695
Leasing agreements	277 577	-	-	277 577
Loans and advances to banks	35 830	-	-	35 830
Loans and advances to public sector	9 794	-	-	9 794
Reverse repo transactions	72 952	-	-	72 952
Interest recorded on hedging IRS	201 118	-	-	201 118
Total	6 345 132	733 378	135 286	7 213 796

01.01.2018-31.12.2018				
Interest expenses	Interest expenses on			Total
	financial liabilities measured at amortised cost	financial liabilities measured at fair value through other comprehensive income	Expenses similar to interest - financial liabilities measured at fair value through profit or loss	
Deposits from individuals	(628 625)	-	-	(628 625)
Deposits from enterprises	(406 149)	-	-	(406 149)
Repo transactions	(81 680)	-	-	(81 680)
Deposits from public sector	(55 101)	-	-	(55 101)
Deposits from banks	(53 356)	-	-	(53 356)
Subordinated liabilities and issue of securities	(246 480)	-	-	(246 480)
Total	(1 471 391)	-	-	(1 471 391)
Net interest income	4 873 741	733 378	135 286	5 742 405

As at 31.12.2018 interest income on financial assets measured at amortised cost includes interest on impaired loans of PLN 254,504 k (as at 31.12.2017 - PLN 250,588 k).

	01.01.2017-
	31.12.2017
Interest income	
Loans and advances to enterprises	1 676 521
Loans and advances to individuals, of which:	3 602 440
<i>Home mortgage loans</i>	1 066 596
Debt securities incl.:	660 999
<i>Investment portfolio available for sale</i>	627 398
<i>Trading portfolio</i>	33 601
Leasing agreements	260 542
Loans and advances to banks	64 225
Loans and advances to public sector	6 376
Reverse repo transactions	27 342
Interest recorded on hedging IRS	230 862
Total	6 529 307
	01.01.2017-
	31.12.2017
Interest expenses	
Deposits from individuals	(558 060)
Deposits from enterprises	(342 180)
Repo transactions	(54 367)
Deposits from public sector	(54 061)
Deposits from banks	(46 645)
Subordinated liabilities and issue of securities	(197 097)
Total	(1 252 410)
Net interest income	5 276 897

7. Net fee and commission income

	01.01.2018- 31.12.2018	01.01.2017- 31.12.2017
Fee and commission income		
eBusiness & payments	574 695	576 995
Current accounts and money transfer	323 257	338 306
Asset management fees	310 378	306 474
Foreign exchange commissions	395 983	346 056
Credit commissions	367 178	316 125
Insurance commissions	190 912	213 572
Commissions from brokerage activities	68 451	88 129
Credit cards	174 262	169 548
Off-balance sheet guarantee commissions	70 522	60 303
Finance lease commissions	19 917	16 228
Issue arrangement fees	8 524	14 502
Distribution fees	4 791	9 730
Other commissions	17 702	20 241
Total	2 526 572	2 476 209
Fee and commission expenses		
eBusiness & payments	(188 264)	(204 303)
Distribution fees	(17 808)	(21 578)
Commissions from brokerage activities	(9 594)	(11 175)
Credit cards	(38 575)	(33 262)
Credit commissions paid	(113 486)	(98 335)
Insurance commissions	(8 469)	(14 771)
Finance lease commissions	(27 322)	(27 184)
Asset management fees and other costs	(6 968)	(6 607)
Other	(58 284)	(45 868)
Total	(468 770)	(463 083)
Net fee and commission income	2 057 802	2 013 126

Included above is fee and commission income on credits, credit cards, off-balance sheet guarantees and leases of PLN 631,879 k (31.12.2017: PLN 562,204 k) and fee and commission expenses on credit cards, leases and paid to credit agents of PLN (152,061) k (31.12.2017: PLN (158,781) k) other than fees included in determining the effective interest rate, relating to financial assets and liabilities not carried at fair value through profit and loss.

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

8. Dividend income

	01.01.2018- 31.12.2018	01.01.2017- 31.12.2017
Dividend income		
Dividends from equity financial assets available for sale	-	76 270
Dividends income from equity investment security	98 989	-
Dividends income from equity financial assets at fair value through profit or loss	1 127	546
Total	100 116	76 816

9. 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	150 153	196 713
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	(24 371)	-
Total	144 539	194 974

Net trading income and revaluation includes the change of the value of derivative instruments in the amount of PLN (1,776) k for 2018 and PLN (10,287) 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.

10. 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	-	26 464
Profit on sale of debt securities available for sale	-	20 824
Charge due to impairment losses	-	(461)
Profit on sale of debt securities measured at fair value through other comprehensive income	28 327	-
Profit on sale of debt securities mandatorily measured at fair value through profit or loss	(24)	-
Change in fair value of debt securities mandatorily measured at fair value through profit or loss	12 343	-
Total profit (losses) on financial instruments	40 646	46 827
Change in fair value of hedging instruments	(16 562)	23 760
Change in fair value of underlying hedged positions	13 396	(23 085)
Total profit (losses) on hedging and hedged instruments	(3 166)	675
Total	37 480	47 502

11. Other operating income

	01.01.2018- 31.12.2018	01.01.2017- 31.12.2017
Other operating income		
Income on sale of services	34 735	20 535
Reimbursements of BGF charges	-	433
Release of provision for legal cases and other assets	63 471	43 297
Settlements of leasing agreements	2 920	3 266
Recovery of other receivables	6 477	5 641
Profit on sales or liquidation of fixed assets, intangible assets and assets for disposal	51 374	11 543
Received compensations, penalties and fines	2 409	1 039
Other income from legal cases	-	24 238
Other	52 456	40 595
Total	213 842	150 587

12. 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	(125 484)	4 984	(1 029 942)	60 670	(1 089 772)
Recoveries of loans previously written off	-	-	11 889	-	11 889
Off-balance sheet credit related facilities	(5 024)	4 485	(6 580)	-	(7 119)
Total	(130 575)	9 469	(1 024 633)	60 670	(1 085 068)

	01.01.2017- 31.12.2017
Impairment losses on loans and advances	
Collective and individual impairment charge	(668 164)
Incurred but not reported losses charge	(65 420)
Recoveries of loans previously written off	43 534
Off-balance sheet credit related facilities	(423)
Total	(690 473)

13. Employee costs

	01.01.2018- 31.12.2018	01.01.2017- 31.12.2017
Employee costs		
Salaries and bonuses	(1 404 842)	(1 293 085)
Salary related costs	(233 376)	(216 933)
Staff benefits costs	(40 485)	(39 705)
Professional trainings	(20 870)	(18 730)
Retirement fund, holiday provisions and other employee costs	29 131	5 836
Total	(1 670 442)	(1 562 617)

14. 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	(346 205)	(348 290)
Marketing and representation	(189 318)	(133 906)
IT systems costs	(244 436)	(213 047)
Cost of BFG, KNF and KDPW	(219 816)	(224 168)
Postal and telecommunication costs	(64 696)	(52 911)
Consulting fees	(89 673)	(65 574)
Cars, transport expenses, carriage of cash	(71 463)	(67 356)
Other external services	(153 005)	(104 616)
Stationery, cards, cheques etc.	(32 709)	(27 280)
Sundry taxes and charges	(37 277)	(33 587)
Data transmission	(10 449)	(12 458)
KIR, SWIFT settlements	(31 037)	(28 480)
Security costs	(27 356)	(25 286)
Costs of repairs	(24 175)	(14 137)
Other	(30 701)	(25 719)
Total	(1 572 316)	(1 376 815)

15. 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	(125 313)	(59 540)
Impairment loss on property, plant, equipment and intangible assets	(13 054)	(8 397)
Costs of purchased services	(14 797)	(8 177)
Other membership fees	(983)	(992)
Paid compensations, penalties and fines	(1 864)	(3 091)
Donations paid	(4 735)	(4 876)
Other	(31 995)	(28 976)
Total	(192 741)	(114 049)

16. 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	(1 004 156)	(801 991)
Deffered tax	274 734	(14 885)
Adjustments from previous years	2 283	169
Total tax on gross profit	(727 139)	(816 707)

Corporate total tax charge information	01.01.2018- 31.12.2018	01.01.2017- 31.12.2017
Profit before tax	3 426 152	3 335 221
Tax rate	19%	19%
Tax calculated at the tax rate	(650 969)	(633 692)
Non-tax-deductible expenses	(37 522)	(20 954)
The fee to the Bank Guarantee Fund	(38 534)	(40 082)
Tax on financial institutions	(88 603)	(80 524)
The gain on acquisition of demerged part of enterprise	69 305	-
Sale of receivables	(6 108)	(52 237)
Non-taxable income (dividends)	18 851	14 423
Non-tax deductible bad debt provisions	(17 847)	(10 970)
Adjustment of prior year tax	2 283	169
Tax effect of consolidation adjustments	22 440	5 045
Other	(435)	2 115
Total tax on gross profit	(727 139)	(816 707)

Deferred tax recognised in other comprehensive income	31.12.2018	31.12.2017
Relating to equity securities available-for-sale	-	(130 767)
Relating to debt securities available-for-sale	-	(57 957)
Relating to valuation of debt investments measured at fair value through other comprehensive income	(130 592)	-
Relating to valuation of equity investments measured at fair value through other comprehensive income	(121 892)	-
Relating to cash flow hedging activity	14 810	20 508
Relating to valuation of defined benefit plans	(2 536)	(125)
Total	(240 210)	(168 341)

17. 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	2 365 222	2 213 054
Weighted average number of ordinary shares	99 725 949	99 275 197
Earnings per share (PLN)	23,72	22,29
Profit for the period attributable to ordinary shares	2 365 222	2 213 054
Weighted average number of ordinary shares	99 725 949	99 275 197
Weighted average number of potential ordinary shares	171 095	75 412
Diluted earnings per share (PLN)	23,68	22,28

The weighted average number of ordinary shares contains dilutive instruments in the form of share capital presented in note 38 and the share based incentive scheme included in note 53.

18. Cash and balances with central banks

Cash and balances with central banks	31.12.2018	31.12.2017
Cash	2 452 636	2 270 698
Current accounts in central banks	6 454 916	1 857 824
Term deposits	-	17 700
Total	8 907 552	4 146 222

Santander Bank Polska SA and Santander Consumer Bank SA hold an obligatory reserve in a current account in the National Bank of Poland. The figure is calculated at a fixed percentage of the monthly average balance of the customers' deposits, which in all the covered periods was 3.5%. In accordance with the applicable regulations, the amount of the calculated provision is reduced by the equivalent of EUR 500 k.

19. Loans and advances to banks

Loans and advances to banks	31.12.2018	31.12.2017
Loans and advances	1 159 923	850 541
Current accounts	1 776 358	1 285 933
Gross receivables	2 936 281	2 136 474
Allowance for impairment	(67)	-
Total	2 936 214	2 136 474

Fair value of loans and advances to banks is presented in Note 44.

Loans and advances to banks

Gross carrying amount	Stage 1	Stage 2	Stage 3	POCI	Total
Balance as at the beginning of the period	2 136 474	-	-	-	2 136 474
Transfers					-
Transfer to Stage 1	(12 373)	-	-	-	(12 373)
Transfer to Stage 2	-	-	-	-	-
Transfer to Stage 3	-	-	-	-	-
New financial assets registered	4 365 645	-	-	-	4 365 645
Changes in existing financial assets	(57)	-	-	-	(57)
Financial assets derecognised that are not write-offs	(3 579 952)	-	-	-	(3 579 952)
Write-offs	-	-	-	-	-
FX and others movements	26 544	-	-	-	26 544
Balance at the end of the period	2 936 281	-	-	-	2 936 281

20. Financial assets and liabilities held for trading

Financial assets and liabilities held for trading	31.12.2018		31.12.2017	
	Assets	Liabilities	Assets	Liabilities
Trading derivatives	1 081 227	1 058 024	1 226 551	1 237 704
Interest rate operations	553 999	545 393	307 344	275 046
Forward	65	6 640	-	68
Options	13 898	13 911	13 211	13 226
IRS	536 638	523 642	291 615	260 187
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	523 949	509 352	913 154	956 605
CIRS	192 484	201 758	282 186	253 890
Forward	40 065	61 233	41 175	160 814
FX Swap	192 760	147 938	493 265	444 919
Spot	585	375	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	9 769 851	1 233 713	3 416 108	1 237 704

Financial assets and liabilities held for trading - trading derivatives include the change in the value of counterparty risk in the amount of PLN (946) k as at 31.12.2018 and PLN 190 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.

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

Offsetting financial assets and financial liabilities	31.12.2018		31.12.2017	
	Financial assets	Financial liabilities	Financial assets	Financial liabilities
Fair value measurements of derivative instruments	1 154 438	1 970 506	1 444 612	1 816 502
Value of collateral accepted/provided	(159 619)	(1 293 617)	(378 412)	(532 439)
Maximum amount of potential set-off	(324 673)	(324 673)	(387 764)	(387 764)
Assets and liabilities not subject to set-offs	670 146	352 216	678 436	896 299

The table below presents derivatives' nominal values.

Derivatives' nominal values	31.12.2018	31.12.2017
1. Term derivatives (hedging)	23 562 563	25 301 383
a) Single-currency interest rate swap	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)	9 593 153	10 430 903
d) Macro cash flow hedge -sold (CIRS)	10 194 876	10 542 739
e) FX Swap cash flow hedge -purchased (FX)	34 185	176 806
f) FX Swap cash flow hedge-sold (FX)	34 349	171 226
2. Term derivatives (trading)	405 539 573	282 611 381
a) Interest rate operations	259 675 302	168 569 058
Single-currency interest rate swap	228 126 591	156 870 056
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	145 864 271	114 042 323
FX swap – purchased amounts	37 836 903	29 815 344
FX swap – sold amounts	37 779 343	29 745 471
Forward- purchased amounts	10 183 310	8 226 882
Forward- sold amounts	10 233 343	8 393 420
Cross-currency interest rate swap – purchased amounts	13 482 264	10 743 244
Cross-currency interest rate swap – sold amounts	13 497 872	10 720 212
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	1 600 252	2 894 072
Spot-purchased	800 242	1 446 853
Spot-sold	800 010	1 447 219
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	431 258 180	311 624 570

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

21. Hedging derivatives

Hedging derivatives	31.12.2018		31.12.2017	
	Assets	Liabilities	Assets	Liabilities
Derivatives hedging fair value	312	129 205	2 283	115 496
Derivatives hedging cash flow	72 909	783 277	215 778	463 302
Total hedging derivatives	73 221	912 482	218 061	578 798

As at 31.12.2018 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 and PLN (9,613) k as at 31.12.2017.

22. Loans and advances to customers

Loans and advances to customers	31.12.2018			31.12.2017
	Measured at amortised cost	Measured at fair value through other comprehensive income	Measured at fair value through profit or loss	
Loans and advances to enterprises	58 129 890	366 751	106 344	47 776 973
Loans and advances to individuals, of which:	73 352 431	-	1 343 986	57 822 414
<i>Home mortgage loans</i>	49 210 998	-	-	37 293 296
Finance lease receivables	8 204 296	-	-	6 848 960
Loans and advances to public sector	325 773	-	-	228 201
Other receivables	15 229	-	-	9 479
Gross receivables	140 027 619	366 751	1 450 330	112 686 027
Allowance for impairment *	(4 384 322)	-	-	(4 846 130)
Total**	135 643 297	366 751	1 450 330	107 839 897

* 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 1,248,750k, 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 1,406,129 k.

Finance lease receivables are presented in Note 47. Fair value of loans and advances to customers is presented in Note 44.

Loans and advances to customers

Gross carrying amount	Stage 1	Stage 2	Stage 3	POCI	Total
Balance at the beginning of the period	99 860 952	6 408 128	6 079 284	337 664	112 686 028
Transfers					
Transfer to Stage 1	2 637 083	(2 588 526)	(48 557)	-	-
Transfer to Stage 2	(4 231 245)	4 324 724	(93 479)	-	-
Transfer to Stage 3	(1 172 116)	(801 465)	1 973 581	-	-
New financial assets registered	51 578 940	-	-	422 909	52 001 849
Changes in existing financial assets	(6 585 939)	(764 242)	(85 764)	(23 101)	(7 459 046)
Financial assets derecognised that are not write-offs	(13 153 943)	(523 462)	(623 667)	(231 773)	(14 532 845)
Write-offs	-	-	(903 234)	-	(903 234)
FX and others movements	(1 070 429)	(359 065)	(594 502)	258 863	(1 765 133)
Balance at the end of the period	127 863 303	5 696 092	5 703 662	764 562	140 027 619

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	(444 870)	(531 570)	(3 085 299)	(4 061 739)
Transfers				-
Transfer to Stage 1	(10 623)	108 205	16 011	113 593
Transfer to Stage 2	171 698	(316 334)	55 022	(89 614)
Transfer to Stage 3	156 838	129 473	(961 171)	(674 860)
New financial assets registered	(786 921)	(11 850)	(4 999)	(803 770)
Changes in credit risk of existing financial assets	65 310	58 826	(424 092)	(299 956)
Changes in models and risk parameters	22 481	5 338	21 995	49 814
Financial assets derecognised that are not write-offs	126 598	30 190	380 207	536 995
Write-offs	-	-	898 166	898 166
FX and others movements	134 850	(2 553)	(132 134)	163
Balance at the end of the period	(564 639)	(530 275)	(3 236 294)	(4 331 208)

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	(53 364)
Write off/Sale of receivables	-
Transfer	-
F/X differences	250
Stan na koniec okresu	(53 114)

Loans and advances to enterprises

Gross carrying amount	Stage 1	Stage 2	Stage 3	POCI	Total
Balance at the beginning of the period	41 034 334	3 345 069	3 291 090	106 480	47 776 973
Transfers					
Transfer to Stage 1	1 754 211	(1 750 652)	(3 559)	-	-
Transfer to Stage 2	(2 096 111)	2 116 025	(19 914)	-	-
Transfer to Stage 3	(509 742)	(343 360)	853 102	-	-
New financial assets registered	19 873 844	-	-	328 863	20 202 707
Changes in existing financial assets	(1 144 887)	(378 963)	(69 322)	(10 548)	(1 603 720)
Financial assets derecognised that are not write-offs	(7 098 510)	(430 474)	(67 032)	(151 666)	(7 747 682)
Write-offs	-	-	(358 866)	-	(358 866)
FX and others movements	131 253	(149 810)	(257 588)	136 623	(139 522)
Balance at the end of the period	51 944 392	2 407 835	3 367 911	409 752	58 129 890

Movements on impairment losses on loans and advances to enterprises measured at a 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	(184 099)	(210 061)	(1 556 984)	(1 951 144)
Transfers				
Transfer to Stage 1	(4 431)	46 920	2 008	44 497
Transfer to Stage 2	51 192	(95 085)	13 001	(30 892)
Transfer to Stage 3	41 077	38 913	(325 380)	(245 390)
New financial assets registered	(207 693)	(4 181)	(1 617)	(213 491)
Changes in credit risk of existing financial assets	20 941	29 573	(59 661)	(9 147)
Changes in models and risk parameters	20 168	(3 582)	1 552	18 138
Financial assets derecognised that are not write-offs	31 252	23 003	21 521	75 776
Write-offs	-	-	359 547	359 547
FX and others movements	(15 217)	(3 869)	(55 309)	(74 395)
Balance at the end of the period	(246 810)	(178 369)	(1 601 322)	(2 026 501)

Loans and advances to individuals

Gross carrying amount	Stage 1	Stage 2	Stage 3	POCI	Total
Balance at the beginning of the period	52 169 331	2 775 546	2 657 088	220 449	57 822 414
Transfers					
Transfer to Stage 1	775 273	(732 403)	(42 870)	-	-
Transfer to Stage 2	(1 660 281)	1 732 152	(71 871)	-	-
Transfer to Stage 3	(628 181)	(428 588)	1 056 769	-	-
New financial assets registered	27 986 147	-	-	93 613	28 079 760
Changes in existing financial assets	(3 855 806)	(281 847)	6 398	(12 278)	(4 143 533)
Financial assets derecognised that are not write-offs	(5 562 685)	(76 313)	(543 754)	(78 808)	(6 261 560)
Write-offs	-	-	(537 883)	-	(537 883)
FX and others movements	(1 187 403)	(204 759)	(341 562)	126 957	(1 606 767)
Balance at the end of the period	68 036 395	2 783 788	2 182 315	349 933	73 352 431

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	(252 556)	(311 580)	(1 445 601)	(2 009 737)
Transfers				-
Transfer to Stage 1	(6 745)	60 278	13 839	67 372
Transfer to Stage 2	119 647	(215 861)	41 067	(55 147)
Transfer to Stage 3	116 161	90 375	(620 544)	(414 008)
New financial assets registered	(570 781)	-	(170)	(570 951)
Changes in credit risk of existing financial assets	45 670	26 491	(353 705)	(281 544)
Changes in models and risk parameters	2 432	9 499	14 827	26 758
Financial assets derecognised that are not write-offs	94 758	6 931	352 703	454 392
Write-offs	-	-	532 135	532 135
FX and others movements	150 231	1 086	(76 863)	74 454
Balance at the end of the period	(301 183)	(332 781)	(1 542 312)	(2 176 276)

Finance lease receivables

	Stage 1	Stage 2	Stage 3	POCI	Total
Gross carrying amount					
Balance at the beginning of the period	6 419 606	287 513	131 106	10 735	6 848 960
Transfers					
Transfer to Stage 1	107 597	(105 470)	(2 127)	-	-
Transfer to Stage 2	(474 852)	476 547	(1 695)	-	-
Transfer to Stage 3	(34 194)	(29 516)	63 710	-	-
New financial assets registered	3 615 627	-	-	432	3 616 059
Changes in existing financial assets	(1 585 246)	(103 432)	(22 839)	(275)	(1 711 792)
Financial assets derecognised that are not write-offs	(492 749)	(16 675)	(12 881)	(1 298)	(523 603)
Write-offs	-	-	(6 485)	-	(6 485)
FX and others movements	(14 278)	(4 496)	4 648	(4 717)	(18 843)
Balance at the end of the period	7 541 511	504 471	153 437	4 877	8 204 296

Movements on impairment losses on finance lease receivables 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	(8 215)	(9 929)	(82 713)	(100 857)
Transfers				-
Transfer to Stage 1	554	1 007	165	1 726
Transfer to Stage 2	859	(5 388)	954	(3 575)
Transfer to Stage 3	(400)	186	(15 248)	(15 462)
New financial assets registered	(8 447)	(7 669)	(3 212)	(19 328)
Changes in credit risk of existing financial assets	(1 301)	2 762	(10 726)	(9 265)
Changes in models and risk parameters	(120)	(579)	5 615	4 916
Financial assets derecognised that are not write-offs	587	255	5 983	6 825
Write-offs	-	-	6 484	6 484
FX and others movements	(165)	229	38	102
Balance at the end of the period	(16 648)	(19 126)	(92 660)	(128 434)

Movements on impairment losses on loans and advances to customers	31.12.2017
Individual and collective impairment	
As at the beginning of the period	(4 187 798)
Charge/write back of current period	(668 164)
Write off/Sale of receivables	735 191
Transfer	(16 960)
F/X differences	30 137
Balance at the end of the period	(4 107 594)
IBNR	
As at the beginning of the period	(691 083)
Charge/write back of current period	(65 420)
Sale of receivables	3 429
Transfer	940
F/X differences	13 598
Balance at the end of the period	(738 536)
Allowance for impairment	(4 846 130)

The Santander Bank Polska Group/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 423,770 k.

Description of transactions

Santander Consumer Bank (SCB) securitized the instalment loan portfolio in September 2015. The transaction is a traditional, revolving one and consisted in transferring the right to securitized receivables to a special purpose vehicle SC Poland Consumer Sp. z o.o. 15-1 (SPV2), with its registered seat in Poland. On the basis of the securitized assets, the aforesaid company issued bonds secured in the form of a registered pledge on the assets of SPV2. SCB granted the company a subordinated loan to support the transaction.

In August 2016 SCB performed a transaction of securitization of cash loans portfolio. The concluded transaction is a traditional and revolving securitization including transfer of ownership rights to securitized receivables for the benefit of the special purpose vehicle SC Poland Consumer 16-1 Sp. z o.o. (SPV3) with its registered seat in Poland. This Company issued, on the basis of securitized assets, bonds secured with a registered pledge on the property of SPV3. In order to support funding of the transaction SCB granted a subordinated loan to SPV3.

SCB carried out a comprehensive analysis of the transaction and concluded that in accordance with IAS 39, the terms and conditions of the transaction do not require SCB to derecognize the securitized assets from its financial statements, as, when granting subordinated loans, SCB retains basically the whole risk and benefits related to the given loans. These loans, in line with the expectations, will absorb the whole volatility of cash flows from the portfolios of securitized loans. Therefore, SCB bears this risk of volatility, as well as is exposed to residual risk which will remain after repayment of the bonds to external investors, which means that the subordinated loan will not be repaid totally or SCB will exercise its right to repurchase the portfolio from SPV, and therefore will remain exposed to further risk related with that portfolio. Therefore, SCB recognizes the liability due to securitization towards SPV2 and SPV3.

Securitisation portfolio description

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

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

SCB granted SPV2 a subordinated loan of PLN 297,851 k as at 31 December 2018. The loan is subordinated to preference and secured bonds. Loan interest repayment is included in the cascading payments i.e. realized in a specified sequence, made from the funds of SPV2, whereas the principal will be repaid after full redemption of bonds. The interest is fixed.

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

This Company issued, on the basis of securitized assets, bonds of the total value of PLN 1,225,000 k, secured with a registered pledge on the property of SPV3. The bonds bear an interest rate comprising 1M WIBOR and margin. As a result of the securitization SCB obtained funding of its activity in exchange for giving rights to future flows arising from the securitized loans portfolio. The maximum period for redemption of the bonds is 16 September 2026 but SCB estimated that it shall take place within 3 years from the transaction date.

In order to support funding of the transaction SCB granted a subordinated loan to SPV3 in the amount of PLN 37,388 k as of 31 December 2018. This loan is subordinated against preference and secured bonds. Interests from the loan are paid in a form of cascade payments, i.e. realized in a predefined sequence from funds held by SPV3, and the principle amount will be repaid after total redemptions of the bonds. The loan interest rate is based on a fixed rate.

In the light of provisions of the IFRS 9, the contractual terms and conditions of the securitization transaction do not require SCB to derecognize the securitized assets from its financial statements. Consequently, at 31 December 2018, SCB recognizes securitized assets under Loans and advances granted to clients in the net amount of PLN 2,176,405 k. The fair value of net securitized assets measured as of 31 December 2018 amounted respectively to PLN 2,209,805 k. At the same time SCB recognizes liabilities in respect of securitization cash flows under Liabilities to clients in the amount of PLN 2,614,322 k as at 31 December 2018.

At 31 December 2018, SCB recognizes also receivables in respect of current settlements with SPVs in the net amount of PLN 144,292 k under Other assets.

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

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

In August 2018, the bank signed an annex to the agreement of 2016, extending the replenishment period for the revolving securitization receivables. This resulted in the extension of the transaction effective maturity by 6 months.

In December 2018 Santander Leasing S.A. make settlement of the transaction of securitization with regard to receivables resulting from leasing settlement and loans agreements. The concluded transaction is a traditional and revolving securitization including transfer of ownership rights to securitized receivables for the benefit of the special purpose vehicle Santander Leasing Poland Securitization 01 DAC with its registered seat in Ireland. This Company issued, on the basis of securitized assets, bonds of the total value of EUR 230m. The bonds bear an interest rate comprising 1M EURIBOR and margin. The maximum period for redemption of the bonds is December 2032, but the Company estimated that it shall take place within 4 years from the transaction date.

The tranche in EUR was launched in December 2018, while the part expressed in PLN is planned to be launch in the first quarter of 2019. The Company plans to obtain an equivalent of EUR 270m in PLN.

The purpose of the securitization is to implement a special instrument allowing the Company to obtain funds before maturity of the receivables, by means of financing provided by SPV based on security in the form of receivables. Securitization, being an alternative financing method, will improve the financial liquidity of Santander Leasing S.A.

In the light of provisions of the IFRS 9, the contractual terms and conditions of the securitization transaction do not require Santander Leasing S.A. to derecognize the securitized assets from its financial statements. The Group retains all the risks related to the securitised receivables. Consequently, at 31 December 2018, Santander Leasing S.A. recognizes securitized assets under Loans and advances to clients in the amount of PLN 1,204,210 k.

Taking into account the fact that securitisation of exposures of leasing companies took place in December 2018, the carrying amount of the securitised assets and recognised liabilities at the year-end is similar to the value of transfers.

23. Investment securities

Investment securities	31.12.2018
Debt securities measured at fair value through other comprehensive income	38 221 051
Government securities:	30 403 130
- bonds	30 403 130
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	136 511
Equity securities measured at fair value through other comprehensive income	821 538
- listed	16 720
- unlisted	804 818
Total	39 179 100

Financial assets available for sale	31.12.2017
Debt securities	27 494 933
Government securities:	24 025 353
- bonds	24 025 353
Central Bank securities:	1 379 839
- bills	1 379 839
Other securities:	2 089 741
-bonds	2 089 741
Equity securities	920 879
- listed	19 329
- unlisted	901 550
Total	28 415 812

As at 31.12.2018 fixed interest rate debt securities measured at fair value through other comprehensive income amount to PLN 26,107,752 k, variable interest rate securities amount to PLN 12,113,299 k.

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

As at 31.12.2018 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 44.

Movements on investment securities	Debt securities		Equity securities	Total
	measured at fair value through other comprehensive income	Debt securities measured at fair value through profit and loss	measured at fair value through other comprehensive income	
As at 31.12.2017	27 494 933	-	920 879	28 415 812
Impact of the implementation of IFRS 9	-	93 165	(108 259)	(15 094)
As at 1.01.2018 (restated)	27 494 933	93 165	812 620	28 400 718
Increases due to acquisition of demerged part of Deutsche Bank Polska SA	63 077	20 013	271	83 361
Additions	163 242 587	5 200	2 519	163 250 306
Disposals (sale and maturity)	(153 073 943)	(3 200)	(316)	(153 077 459)
Fair value adjustment	394 032	12 343	6 444	412 819
Movements on interest accrued	19 064	-	-	19 064
FX differences	81 301	8 990	-	90 291
As at 31.12.2018	38 221 051	136 511	821 538	39 179 100

Movements on financial assets available for sale	Financial instruments		Total
	Debt securities	representing equity rights	
As at 1.01.2017	28 423 828	884 050	29 307 878
Additions	60 756 329	2 536	60 758 865
Disposals (sale and maturity)	(62 053 423)	(9 193)	(62 062 616)
Fair value adjustment	463 913	43 486	507 399
Movements on interest accrued	19 756	-	19 756
FX differences	(115 470)	-	(115 470)
As at 31.12.2017	27 494 933	920 879	28 415 812

24. Investments in associates

Balance sheet value of associates	31.12.2018	31.12.2017
Polfund - Fundusz Poręczeń Kredytowych S.A.	44 703	43 570
Santander - Aviva Towarzystwo Ubezpieczeń S.A. and Santander - Aviva Towarzystwo Ubezpieczeń na Życie S.A.	847 249	845 802
Total	891 952	889 372

Movements on investments in associates	01.01.2018-31.12.2018	01.01.2017-31.12.2017
Balance as at 01.01.	889 372	871 491
Share of profits/(losses)	62 667	58 264
Dividends	(60 695)	(44 861)
Other	608	4 478
As at the end of the period	891 952	889 372

Fair value of „Investment in associates” is presented in Note 44.

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

Name of associate	Country of incorporation and place of business	The Group's share in capital / voting power		Valuation method	Scope of business
		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

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

	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	25 035	19 142	35 660	25 719

* data are based on estimates of companies

2017 data are based on audited financial report of companies Santander - Aviva Towarzystwo Ubezpieczeń na Życie S.A. and Santander - Aviva Towarzystwo Ubezpieczeń S.A.

Data published in Annual Report 2017 were based on estimates of companies. Difference between estimates and real data are irrelevant.

25. Intangible assets

Intangible assets Year 2018	Licences, patents etc.	Other	Expenditure on intangible assets	Total
Gross value - beginning of the period	1 488 796	441 140	198 521	2 128 457
Intangible assets recognised on acquisition of a demerged part of Deutsche Bank Polska S.A.	8 067	192 628	1 781	202 476
Additions from:				
- purchases	-	-	302 934	302 934
- intangible assets taken for use	212 245	7 704	-	219 949
- transfers	22	-	-	22
Disposals from:				
- liquidation	(8 588)	(101)	(81)	(8 770)
- intangible assets taken for use	-	-	(219 949)	(219 949)
- transfers	-	(11)	-	(11)
Gross value - end of the period	1 700 542	641 360	283 206	2 625 108
Accumulated depreciation - beginning of the period	(1 267 430)	(370 700)	-	(1 638 130)
Accumulated depreciation recognised on acquisition of a demerged part of Deutsche Bank Polska S.A.	(5 459)	-	-	(5 459)
Additions/disposals from:				
- current year amortization	(143 373)	(27 393)	-	(170 766)
- liquidation, sale	8 555	101	-	8 656
- transfers	-	-	-	-
Write down/Reversal of impairment write down	-	-	-	-
Accumulated depreciation- end of the period	(1 407 707)	(397 992)	-	(1 805 699)
Balance sheet value				
Purchase value	1 700 542	641 360	283 206	2 625 108
Accumulated depreciation	(1 407 707)	(397 992)	-	(1 805 699)
As at 31 December 2018	292 835	243 368	283 206	819 409

Intangible assets Year 2017	Licences, patents etc.	Other	Expenditure on intangible assets	Total
Gross value - beginning of the period	1 387 288	429 893	195 384	2 012 565
Additions from:				
- purchases	-	-	174 088	174 088
- intangible assets taken for use	145 582	13 338	-	158 920
- transfers	13	-	-	13
- others	2 890	-	-	2 890
Disposals from:				
- liquidation	(44 085)	(2 091)	(669)	(46 845)
- intangible assets taken for use	-	-	(158 920)	(158 920)
- transfers	(2)	-	(11 362)	(11 364)
- others	(2 890)	-	-	(2 890)
Gross value - end of the period	1 488 796	441 140	198 521	2 128 457
Accumulated depreciation - beginning of the period	(1 174 777)	(351 026)	-	(1 525 803)
Additions/disposals from:				
- current year amortization	(136 738)	(30 798)	-	(167 536)
- liquidation, sale	44 085	2 090	-	46 175
- transfers	-	9 034	-	9 034
Write down/Reversal of impairment write down	-	-	-	-
Accumulated depreciation- end of the period	(1 267 430)	(370 700)	-	(1 638 130)
Balance sheet value				
Purchase value	1 488 796	441 140	198 521	2 128 457
Accumulated depreciation	(1 267 430)	(370 700)	-	(1 638 130)
As at 31 December 2017	221 366	70 440	198 521	490 327

26. Goodwill

As at 31 December 2018 and in the corresponding period, the goodwill covered in the amount of PLN 1,712,056 k the following items:

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

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 achieved in 2018.

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.

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

The bank conducted a test for impairment of goodwill arising from the final settlement of acquisition of shares of PSA Finance Polska sp. z o.o. and, indirectly, PSA Consumer Finance Polska sp. z o.o. by Santander Consumer Bank S.A. The test results showed an excess of the value of non-controlling interests (70%) and the payment made over the carrying amount of the identified net assets. As a result, no goodwill impairment was identified.

The test was prepared using the income approach.

As at 31 December 2018, no goodwill impairment was identified.

27. Property, plant and equipment

Property, plant & equipment Year 2018	Land and buildings	IT Equipment	Transportation means	Other fixed assets	Capital expenditures	Total
Gross value - beginning of the period	943 286	806 328	155 536	263 265	168 839	2 337 254
Property, plant & equipment recognised on acquisition of a demerged part of Deutsche Bank Polska S.A.	14 359	6 343	171	1 503	-	22 376
Additions from:						
- purchases	-	-	-	-	278 252	278 252
- leasing	-	-	11 959	-	-	11 959
- fixed assets taken for use	120 436	105 761	55 737	16 504	-	298 438
- transfers	1	494	11 493	184	234	12 406
Disposals from:						
- sale, liquidation, donation	(105 910)	(27 068)	(41 740)	(39 321)	(3)	(214 042)
- fixed assets taken for use	-	-	-	-	(298 439)	(298 439)
- transfers	(35 803)	(50)	(26 997)	(221)	(494)	(63 565)
Gross value - end of the period	936 369	891 808	166 159	241 914	148 389	2 384 639
Accumulated depreciation - beginning of the period	(630 972)	(516 251)	(39 473)	(219 841)	-	(1 406 537)
Accumulated depreciation recognised on acquisition of a demerged part of Deutsche Bank Polska S.A.	(237)	(2 519)	(119)	(333)	-	(3 208)
Additions/disposals from:						
- current year amortization	(34 953)	(90 135)	(22 766)	(14 850)	-	(162 704)
- sale, liquidation, donation	84 470	26 712	10 873	38 285	-	160 340
- transfers	20 646	(120)	6 091	196	-	26 813
Write down/Reversal of impairment write down	(13 014)	-	55	-	-	(12 959)
Accumulated depreciation- end of the period	(574 060)	(582 313)	(45 339)	(196 543)	-	(1 398 255)
Balance sheet value						
Purchase value	936 369	891 808	166 159	241 914	148 389	2 384 639
Accumulated depreciation	(574 060)	(582 313)	(45 339)	(196 543)	-	(1 398 255)
As at 31 December 2018	362 309	309 495	120 820	45 371	148 389	986 384

Property, plant & equipment Year 2017	Land and buildings	Equipment	Transportation means	Other fixed assets	Capital expenditures	Total
Gross value - beginning of the period	960 363	699 615	145 207	278 394	152659	2 236 238
Additions from:						
- purchases	-	-	-	-	240 121	240 121
- leasing	-	-	9 062	-	-	9 062
- fixed assets taken for use	27 253	136 875	45 940	15 842	-	225 910
- transfers	-	146	2 436	10	2 280	4 872
- merger	28	381	-	53	-	462
Disposals from:						
- sale, liquidation, donation	(44 330)	(30 308)	(31 572)	(30 919)	(225)	(137 354)
- fixed assets taken for use	-	-	-	-	(225 910)	(225 910)
- transfers	-	-	(15 537)	(62)	(86)	(15 685)
- merger	(28)	(381)	-	(53)	-	(462)
Gross value - end of the period	943 286	806 328	155 536	263 265	168839	2 337 254
Accumulated depreciation - beginning of the period	(621 431)	(468 323)	(32 154)	(236 032)	-	(1 357 940)
Additions/disposals from:						
- current year amortization	(36 634)	(77 772)	(22 934)	(14 056)	-	(151 396)
- sale, liquidation, donation	35 380	29 812	9 048	30 008	-	104 248
- transfers	17	32	6 568	239	-	6 856
Write down/Reversal of impairment write down	(8 304)	-	(1)	-	-	(8 305)
Accumulated depreciation- end of the period	(630 972)	(516 251)	(39 473)	(219 841)	-	(1 406 537)
Balance sheet value						
Purchase value	943 286	806 328	155 536	263 265	168 839	2 337 254
Accumulated depreciation	(630 972)	(516 251)	(39 473)	(219 841)	-	(1 406 537)
As at 31 December 2017	312 314	290 077	116 063	43 424	168 839	930 717

28. 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	870 763	-	203 795	203 795	666 968
Valuation of derivative financial instruments	390 826	-	26 394	26 394	364 432
Valuation of cash flow hedges instruments	14 811	(5 698)	-	(5 698)	20 509
Other provisions	176 074	-	12 582	12 582	163 492
Deferred income	538 276	-	29 231	29 231	509 045
Differences between carrying and tax value of lease	482 809	-	109 147	109 147	373 662
Unrealised interest expenses on loans, deposits and securities	199 557	-	72 938	72 938	126 619
Other negative temporary differences	11 856	-	(13 386)	(13 386)	25 242
including impact of the implementation of IFRS 9	49 843				
Total assets of deferred tax	2 684 972	(5 698)	440 701	435 003	2 249 969
Deferred tax liabilities	31.12.2018	Changes to equity*	Changes to financial result	Changes in temporary differences	31.12.2017
Valuation of investment securities	(259 563)	(73 908)	3 253	(70 655)	(188 908)
Provisions for retirement allowances	(2 537)	(2 411)	-	(2 411)	(126)
Valuation of derivative financial instruments	(216 336)	-	45 281	45 281	(261 617)
Unrealised interest income on loans, securities and interbank deposits	(202 651)	-	(23 278)	(23 278)	(179 373)
Prepayments regarding amortization of applied investment relief	(1 597)	-	154	154	(1 751)
Difference between balance sheet and taxable value of non-financial assets	(28 735)	-	(37 201)	(37 201)	8 466
Unrealised FX translation differences from b/s valuation of receivables and liabilities	(9 196)	-	(423)	(423)	(8 773)
Valuation of shares / interests in subsidiaries	(140 421)	-	6 545	6 545	(146 966)
Other positive temporary differences	(63 815)	-	(7 121)	(7 121)	(56 694)
including impact of the implementation of IFRS 9	9 177				
Total liabilities deferred tax	(924 851)	(76 319)	(12 790)	(89 109)	(835 742)
Net deferred tax assets	1 760 121	(82 017)	427 911	345 894	1 414 227

*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.

	31.12.2017	Changes to equity*	Changes to financial result	Changes in temporary differences	31.12.2016
Deferred tax assets					
Provisions for impairment of loans and advances	666 968	-	16 536	16 536	650 432
Valuation of derivative financial instruments	364 432	-	(353 780)	(353 780)	718 212
Valuation of cash flow hedges instruments	20 509	(4 743)	-	(4 743)	25 252
Other provisions	163 492	-	17 352	17 352	146 140
Deferred income	509 045	-	66 633	66 633	442 412
Differences between carrying and tax value of lease	373 662	-	76 007	76 007	297 655
Unrealised interest expenses on loans, deposits and securities	126 619	-	35 007	35 007	91 612
Other negative temporary differences	25 242	-	12 223	12 223	13 019
Total assets of deferred tax	2 249 969	(4 743)	(130 022)	(134 765)	2 384 734
Deferred tax liabilities					
Revaluation of financial instruments available for sale	(188 908)	(101 417)	-	(101 417)	(87 491)
Provisions for retirement allowances	(126)	1 788	-	1 788	(1 914)
Valuation of derivative financial instruments	(261 617)	-	105 928	105 928	(367 545)
Unrealised interest income on loans, securities and interbank deposits	(179 373)	-	31 125	31 125	(210 498)
Prepayments regarding amortization of applied investment relief	(1 751)	-	125	125	(1 876)
Difference between balance sheet and taxable value of non-financial assets	8 466	-	3 340	3 340	5 126
Unrealised FX translation differences from b/s valuation of receivables and liabilities	(8 773)	-	509	509	(9 282)
Valuation of shares / interests in subsidiaries	(146 966)	-	816	816	(147 782)
Other positive temporary differences	(56 694)	-	(27 544)	(27 544)	(29 150)
Total liabilities deferred tax	(835 742)	(99 629)	114 299	14 670	(850 412)
Net deferred tax assets	1 414 227	(104 372)	(15 723)	(120 095)	1 534 322

*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.

Movements on net deferred tax	31.12.2018	31.12.2017
As at the beginning of the period	1 414 227	1 534 322
Impact of the implementation of IFRS 9	59 020	-
Changes recognised in income statement	274 734	(14 885)
Changes recognised in other comprehensive income	(82 017)	(104 372)
Changes on deferred tax as a result of a business combination	94 428	-
Other	(271)	(838)
Balance at the end of the period	1 760 121	1 414 227

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.

29.Assets classified as held for sale

Assets classified as held for sale	31.12.2018	31.12.2017
Land and buildings	11 123	8
Other fixed assets	1 022	95
Total	12 145	103

30.Other assets

Other assets	31.12.2018	31.12.2017
Interbank and interbranch settlements	59 407	142 701
Sundry debtors	897 695	756 662
Prepayments	160 633	128 892
Repossessed assets	6 849	103
Settlements of stock exchange transactions	33 512	31 711
Other	8 899	4 999
Total	1 166 995	1 065 068
of which financial assets *	990 614	931 074

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

31.Deposits from banks

Deposits from banks	31.12.2018	31.12.2017
Term deposits	144 906	64 023
Loans received from banks	1 733 724	1 994 759
Current accounts	954 298	724 301
Total	2 832 928	2 783 083

As at 31.12.2018 fair value adjustment for hedged deposit totaled PLN nil (as at 31.12.2017 – PLN nil).

Fair value of "Deposits from banks" is presented in Note 44.

Movements in loans received from banks	31.12.2018	31.12.2017
As at the beginning of the period	1 994 759	1 945 101
Increase (due to):	1 802 458	985 114
- loans received	1 739 540	953 810
- interest on loans received	37 776	31 304
- FX differences and other changes	25 142	-
Decrease (due to):	(2 063 493)	(935 456)
- repayment of loans	(2 024 290)	(841 644)
- interest repayment	(39 203)	(31 700)
- FX differences and other changes	-	(62 112)
As at the end of the period	1 733 724	1 994 759

32. Deposits from customers

Deposits from customers	31.12.2018	31.12.2017
Deposits from individuals	88 211 366	64 987 719
Term deposits	32 715 078	21 911 544
Current accounts	55 308 995	42 948 226
Other	187 293	127 949
Deposits from enterprises	57 493 542	42 170 092
Term deposits	24 690 631	17 486 056
Current accounts	27 274 603	20 481 778
Loans	4 751 949	3 552 388
Other	776 359	649 870
Deposits from public sector	3 911 750	4 323 324
Term deposits	1 290 086	2 085 917
Current accounts	2 617 635	2 233 410
Other	4 029	3 997
Total	149 616 658	111 481 135

As at 31.12.2018 deposits held as collateral totaled PLN 436,634 k (as at 31.12.2017 - PLN 271,147 k).

Fair value of "Deposits from customers" is presented in Note 44.

Movements in loans received from other financial institutions	31.12.2018	31.12.2017
As at the beginning of the period	3 552 388	4 075 897
Increase (due to):	1 978 326	483 022
- loans received	1 832 185	466 860
- interest on loans received	26 810	16 162
- FX differences and other changes	119 331	-
Decrease (due to):	(778 765)	(1 006 531)
- repayment of loans	(757 571)	(726 764)
- interest repayment	(21 194)	(16 513)
- FX differences and other changes	-	(263 254)
As at the end of the period	4 751 949	3 552 388

33.Subordinated liabilities

Subordinated liabilities	Redemption date	Currency	Nominal value
Tranche 1	05.08.2025	EUR	100 000
Tranche 2	03.12.2026	EUR	120 000
Tranche 3	22.05.2027	EUR	137 100
Tranche 4	05.04.2028	PLN	1 000 000
SCF Madrid	18.05.2028	PLN	100 000

Movements in subordinated liabilities	31.12.2018	31.12.2017
As at the beginning of the period	1 488 602	440 457
Additions from:	1 221 067	1 133 436
- drawing of subordinated loan	100 000	-
- interest on subordinated loans	69 071	33 564
- FX differences	46 718	-
- reclassification *	1 005 278	1 099 872
Disposals from:	(65 328)	(85 291)
- interest repayment	(65 328)	(27 528)
- FX differences	-	(57 763)
As at the end of the period	2 644 341	1 488 602
Short-term	16 827	11 257
Long-term (over 1 year)	2 627 514	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 5.

34. 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
Series C bonds of Santander Factoring	850 000	PLN	18.04.2019
Senior bonds of Santander Leasing Poland Securitization 01	230 000	EUR	30.12.2034
SCB00042	100 000	PLN	05.03.2021
SCB00043	60 000	PLN	29.03.2022
SCB00044	156 000	PLN	14.05.2021
SCB00045	90 000	PLN	18.05.2021
SCB00046	45 000	PLN	18.05.2021

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

Movements in debt securities in issue	31.12.2018	31.12.2017
As at the beginning of the period	5 895 814	5 529 187
Increase (due to:)	7 608 371	3 745 653
- debt securities in issue	7 430 794	3 562 288
- interest on debt securities in issue	173 182	167 135
- FX differences	4 395	16 230
Decrease (due to):	(4 135 568)	(3 379 026)
- debt securities redemption	(2 975 000)	(2 095 000)
- reclassification*	(1 005 278)	(1 099 872)
- FX differences	-	(21 786)
- interest repayment	(155 290)	(162 368)
As at the end of the period	9 368 617	5 895 814

*Bonds issued by Bank and qualified with the consent of the Polish Financial Supervision Authority to subordinated liabilities

35.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	67 044	40 574
Provisions for financial guarantees	13 514	9 518
Other provisions	490	560
Total	81 048	50 652

Change in provisions for off balance sheet credit facilities	31.12.2018
As at 31.12.2017	50 652
Impact of the implementation of IFRS 9	15 034
As at 1.01.2018 (restated)	65 686
Increases due to acquisition of demerged part of Deutsche Bank Polska SA	7 945
Provision charge	182 843
Utilization	301
Write back	(175 782)
Other changes	55
As at the end of the period	81 048
Short-term	60 407
Long-term	20 641

Change in provisions for off balance sheet credit facilities	31.12.2017
As at the beginning of the period	50 746
Provision charge	77 447
Utilization	(517)
Write back	(77 024)
As at the end of the period	50 652
Short-term	43 693
Long-term	6 959

36. Other provisions

Other provisions	31.12.2018	31.12.2017
Provisions for legal claims	132 382	99 463
Provisions for restructuring	499	3 019
Total	132 881	102 482

Change in other provisions on 31.12.2018	Provisions for legal claims	Provisions for restructuring	Total
As at the beginning of the period	99 463	3 019	102 482
Increases due to acquisition of demerged part of Deutsche Bank Polska SA	5 230	-	5 230
Provision charge	100 990	-	100 990
Utilization	(42 214)	-	(42 214)
Write back	(31 087)	(2 520)	(33 607)
As at the end of the period	132 382	499	132 881

Change in other provisions on 31.12.2017	Provisions for legal claims	Provisions for restructuring	Total
As at the beginning of the period	74 396	4 986	79 382
Provision charge	63 742	4 754	68 496
Utilization	(12 142)	-	(12 142)
Write back	(26 533)	(6 721)	(33 254)
As at the end of the period	99 463	3 019	102 482

37. Other liabilities

Other liabilities	31.12.2018	31.12.2017
Settlements of stock exchange transactions	17 039	25 851
Interbank settlements	267 844	952 192
Employee provisions	404 342	407 722
Other provisions	3 300	3 300
Sundry creditors	978 115	511 537
Other deferred and suspended income	240 637	249 880
Public and law settlements	109 853	84 971
Accrued liabilities	567 220	532 117
Finance lease related settlements	139 232	99 306
Other	5 311	1 898
Total	2 732 893	2 868 774
of which financial liabilities *	2 377 092	2 532 025

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

	Employee provisions			Total
		of which: Provisions for retirement allowances	Other provisions	
Change in provisions on 31.12.2018				
As at the beginning of the period	407 722	72 726	3 300	411 022
Increases due to acquisition of demerged part of Deutsche Bank Polska SA	19 046	1 532	-	19 046
Provision charge	364 674	10 549	-	364 674
Utilization	(258 436)	(3 875)	-	(258 436)
Write back	(128 664)	(40 074)	-	(128 664)
Balance at the end of the period	404 342	40 858	3 300	407 642
Short-term	363 484	-	3 300	366 784
Long-term	40 858	40 858	-	40 858

	Employee provisions			Total
		of which: Provisions for retirement allowances	Other provisions	
Change in provisions on 31.12.2017				
As at the beginning of the period	375 959	60 397	3 300	379 259
Provision charge	330 771	14 270	-	330 771
Utilization	(232 256)	-	-	(232 256)
Write back	(66 675)	(1 941)	-	(66 675)
Other changes	(77)	-	-	(77)
Balance at the end of the period	407 722	72 726	3 300	411 022
Short-term	334 996	-	3 300	338 296
Long-term	72 726	72 726	-	72 726

Employee related provisions and accruals consists of items outlined in Note 52.

38.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 General Meeting of Shareholders was Banco Santander with a controlling stake of 67.47% stake.

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 General Meeting of Shareholders was Banco Santander with a controlling stake of 69.34% stake.

39. 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:	10 279 957	9 234 895
<i>Reserve capital</i>	9 951 065	8 953 176
<i>Supplementary capital</i>	985 126	937 954
<i>Adjustment to equity from acquisition/loss of controlling interest in subsidiaries</i>	(656 234)	(656 234)
Total	18 969 482	16 920 129

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

Other movements of other reserve capital are presented in "movements on consolidated 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.

40.Revaluation reserve

Revaluation reserve 31.12.2018	Total gross	Deferred tax adjustment	Total net
Opening balance, of which:	882 058	(167 592)	714 466
Debt securities measured at fair value through other comprehensive income	302 597	(57 493)	245 104
Equity securities measured at fair value through other comprehensive income	688 273	(130 774)	557 499
Valuation of cash flow hedging instruments	(109 351)	20 777	(88 574)
Actuarial gains on retirement allowances	539	(102)	437
Impact of the implementation of IFRS 9, of which:	(54 380)	10 333	(44 047)
Equity securities measured at fair value through other comprehensive income	(54 380)	10 333	(44 047)
Change in valuation of debt securities measured at fair value through other comprehensive income	407 448	(77 415)	330 033
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	6 828	(1 297)	5 531
Change in valuation of cash flow hedging instruments	30 104	(5 720)	24 384
Change in valuation of defined benefit plans	12 840	(2 440)	10 400
Closing balance, of which:	1 258 486	(239 113)	1 019 373
Debt securities measured at fair value through other comprehensive income	683 633	(129 890)	553 743
Equity securities measured at fair value through other comprehensive income	640 721	(121 738)	518 983
Valuation of cash flow hedging instruments	(79 247)	15 057	(64 190)
Actuarial gains on retirement allowances	13 379	(2 542)	10 837

Revaluation reserve 31.12.2017	Total gross	Deferred tax adjustment	Total net
Opening balance, of which:	340 856	(64 763)	276 093
Debt and equity securities	465 234	(88 396)	376 838
Valuation of cash flow hedging instruments	(134 282)	25 514	(108 768)
Actuarial gains on retirement allowances	9 904	(1 881)	8 023
Change in valuation of debt and equity securities available for sale	549 139	(104 336)	444 803
Transfer from revaluation reserve related to sale of investments	(23 503)	4 465	(19 038)
Change in valuation of cash flow hedging instruments	24 931	(4 737)	20 194
Change in valuation of defined benefit plans	(9 365)	1 779	(7 586)
Closing balance, of which:	882 058	(167 592)	714 466
Debt and equity securities	990 870	(188 267)	802 603
Valuation of cash flow hedging instruments	(109 351)	20 777	(88 574)
Actuarial gains on retirement allowances	539	(102)	437

41. Non - controlling interests

Name of the subsidiary	Country of incorporation and place of business	Percentage share of non-controlling interests in share capital / voting rights		Net profit for the period attributable to non-controlling interests		Accumulated non-controlling interests	
		31.12.2018	31.12.2017	31.12.2018	31.12.2017	31.12.2018	31.12.2017
Santander Towarzystwo Funduszy Inwestycyjnych S.A.	Poland	50,00	50,00	94 960	33 252	104 216	42 507
Santander Consumer Bank S.A.	Poland	40,00	40,00	238 831	272 208	1 459 968	1 393 902
Total				333 791	305 460	1 564 184	1 436 409

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

	Santander Towarzystwo Funduszy Inwestycyjnych SA		Santander Consumer Bank SA	
	31.12.2018	31.12.2017	31.12.2018	31.12.2017
Loans and advances to banks	225 383	79 045	63 781	130 022
Loans and advances to customers	-	-	14 880 930	13 891 179
Investments in subsidiaries	-	-	154 775	154 775
Investment securities	1 770	-	2 784 951	2 608 443
Net deferred tax assets	2 457	2 234	453 018	468 338
Other items	31 308	36 351	354 310	394 258
Total assets	260 918	117 630	18 691 765	17 647 015
Deposits from banks	-	-	48 046	152 739
Deposits from customers	-	-	11 556 090	10 846 837
Sell-buy-back transactions	-	-	1 106 793	1 171 179
Debt securities in issue	-	-	1 938 491	1 676 559
Other items	52 485	32 617	745 214	609 632
Total liabilities	52 485	32 617	15 394 634	14 456 946
Income	314 123	314 031	2 047 370	1 944 552
Profit (loss) for the period	189 921	66 503	559 042	649 136
Dividends paid to Santander Bank Polska SA	33 251	37 546	173 251	73 416

42. Hedge accounting

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

Fair value hedges

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

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

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

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

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 profit & loss account according to the terms originally agreed for individual hedging relationships. PLN 1,199 k was recognised in the income statement for 2017 and PLN 262 k was reflected in the income statement for 2018.

Details of the hedging transactions of Santander Bank Polska SA as at 31.12.2018 and in the corresponding period are presented in the tables below:

Nominal value of hedging instruments as at 31.12.2018	Distribution of nominal values of cash flows					Total
	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 instruments	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 instruments	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 instruments					
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 instruments					
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

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)
<i>Receivables arising from hedging instruments</i>	-	296
<i>Liabilities arising from hedging instruments</i>	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:		
<i>Assets</i>	1 856 000	275 000
<i>Liabilities</i>	-	-
Accumulated amount of fair value hedge adjustments on the hedged item included in the statement of comprehensive income and in the carrying amount, including:		
<i>Assets</i>	118 750	1 336
<i>Liabilities</i>	-	-
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 hedging 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

As at 31.12.2018, Santander Leasing SA had three derivative instrument - IRS (Interest Rate Swap), designated to hedge accounting of fair value, which hedges the company against the interest rate.

Details of this transactions o as at 31.12.2018 and at comparative period are presented in tables below:

Nominal value of hedging instruments as at 31.12.2018	Distribution of nominal values of cash flows					Total
	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 instruments	-	95 422	149 172	508 699	-	753 293
IRS	-	95 422	149 172	508 699	-	753 293
Liabilities arising from derivative hedging instruments	-	95 422	149 172	508 699	-	753 293
IRS	-	95 422	149 172	508 699	-	753 293

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 instruments					
Average fixed interest rate	(0,2672)	(0,2674)	(0,2653)	(0,2521)	-
Average exchange rate (EUR/PLN)	4,3000	4,3000	4,3000	4,3000	-
Liabilities arising from derivative hedging instruments					
Average variable interest rate	(0,3684)	(0,3684)	(0,3684)	(0,3684)	-
Average exchange rate (EUR/PLN)	4,3000	4,3000	4,3000	4,3000	-

Hedging instruments as at 31.12.2018 designated as fair value hedges	Hedged item: Received fixed-rate loans
Nominal value of hedging instrument	753 293
Fair value measurement of a hedging instrument due to hedged risk including:	(153)
<i>Receivables arising from hedging instruments</i>	28
<i>Liabilities arising from hedging instruments</i>	181
Line item in the statement of financial position that includes the hedging instrument	Hedging derivatives (IRS)
Hedged risk	Interest rate risk
Period over which instruments have impact on the Santander Leasing results	up to 2022

Items subject to fair value hedge accounting as at 31.12.2018	Received fixed-rate loans
Carrying amount of the hedged item, including:	
<i>Assets</i>	-
<i>Liabilities</i>	753 293
Accumulated amount of fair value hedge adjustments on the hedged item included in the statement of comprehensive income and in the carrying amount, including:	
<i>Assets</i>	-
<i>Liabilities</i>	3
Line item in the statement of financial position that includes the hedged instrument	Deposits from banks

31.12.2017

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

Cash flow hedging

Santander Bank Polska Group uses hedge accounting for its future cash flows with respect to commercial and mortgage credit portfolios based on a variable interest rate, denominated in PLN or in EUR, USD and CHF with maximum maturity of 33 years.

The hedging strategies used by Santander Bank Polska Group are designed to protect the Group'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.

Hedging relationships are created using Interest Rate Swaps, FX 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)
<i>Receivables arising from hedging instruments</i>	38 202	(113 364)
<i>Liabilities arising from hedging instruments</i>	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 December 2017, the nominal value of the hedging item was PLN 12,117,739 k. Measurement to fair value of the hedging instrument was PLN (109,351) k; the same amount, less deferred tax, is recognised in comprehensive income and accumulated in the Bank's equity during the period and are presented in note 40.

The non-effective portion of measurement of the cash flow hedge was PLN (10,703) k as of 31.12.2017.

43. Sell-buy-back and buy-sell-back transaction

Santander Bank Polska Group raises funds by selling financial instruments under agreements to repurchase these instruments at future dates at a predetermined price.

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

	31.12.2018	31.12.2017
	Balance sheet	Balance sheet
	value	value
Liabilities valued at amortised cost (contains sell-buy-back)	9 340 788	2 650 846
Fair value of securities held as collateral for sell-buy-back/repo transactions	9 617 866	2 990 774
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	1 070 003	986 398
Sell-buy-back transactions from customers	8 270 785	1 664 448
Total	9 340 788	2 650 846

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

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

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

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

Financial assets which are subject to reverse repo and buy-sell-back transactions represent a security cover accepted by the Group which the Group 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.

44. Fair value

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

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

ASSETS	31.12.2018		31.12.2017	
	Book Value	Fair value	Book Value	Fair value
Cash and balances with central banks	8 907 552	8 907 552	4 146 222	4 146 222
Loans and advances to banks	2 963 214	2 963 214	2 136 474	2 136 474
Financial assets held for trading	9 769 851	9 769 851	3 416 108	3 416 108
Hedging derivatives	73 221	73 221	218 061	218 061
Loans and advances to customers	137 460 378	138 231 719	107 839 897	108 488 102
- measured at amortised cost	135 643 297	136 414 638	-	-
- measured at fair value through other comprehensive income	366 751	366 751	-	-
- measured at fair value through profit or loss	1 450 330	1 450 330	-	-
Financial assets available for sale	-	-	28 415 812	28 415 812
Investment securities incl.:	39 179 100	39 179 100	-	-
- debt securities measured at fair value through other comprehensive income	38 221 051	38 221 051	-	-
- debt securities measured at fair value through profit and loss	136 511	136 511	-	-
- equity securities measured at fair value through other comprehensive income	821 538	821 538	-	-
LIABILITIES				
Deposits from banks	2 832 928	2 832 928	2 783 083	2 783 083
Hedging derivatives	912 482	912 482	578 798	578 798
Financial liabilities held for trading	1 233 713	1 233 713	1 237 704	1 237 704
Deposits from customers	149 616 658	149 607 250	111 481 135	111 496 805
Subordinated liabilities	2 644 341	2 653 397	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 Group has financial instruments which in accordance with the IFRS are not carried at fair value in the consolidated financial statements. The fair value of such instruments is measured using the following methods and assumptions.

Apart from assets that are not measured at fair value, all the other fair values fulfil conditions for classification to Level 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 Group 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 Group made the following classification of its financial instruments measured at fair value in the statement of financial position:

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

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

Level III (measurement methods using material non-market parameters): This level includes equity securities that are not quoted in the active market, measured using the expert valuation model; investment certificates measured at the balance sheet date at the price announced by the mutual fund and debt securities. 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 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	1 344,0	1 344,5	1 344,3	1 341,9	1 339,8

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 Group classified its financial instruments to the following fair value levels:

31.12.2018	Level I	Level II	Level III	Total
Financial assets				
Financial assets held for trading	8 688 624	1 081 227	-	9 769 851
Hedging derivatives	-	73 221	-	73 221
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	1 360 030	1 450 330
Debt securities measured at fair value through other comprehensive income	38 193 781	-	27 270	38 221 051
Debt securities measured at fair value through profit and loss	-	-	136 511	136 511
Equity securities measured at fair value through other comprehensive income	16 720	-	804 818	821 538
Total	46 899 125	1 244 748	2 695 380	50 839 253
Financial liabilities				
Financial liabilities held for trading	175 689	1 058 024	-	1 233 713
Hedging derivatives	-	912 482	-	912 482
Total	175 689	1 970 506	-	2 146 195

31.12.2017	Level I	Level II	Level III	Total
Financial assets				
Financial assets held for trading	2 189 110	1 226 551	447	3 416 108
Hedging derivatives	-	218 061	-	218 061
Financial investment assets - debt securities	27 462 401	-	32 532	27 494 933
Financial investment assets - equity securities	19 328	-	901 551	920 879
Total	29 670 839	1 444 612	934 530	32 049 981
Financial liabilities				
Financial liabilities held for trading	-	1 237 704	-	1 237 704
Hedging derivatives	-	578 798	-	578 798
Total	-	1 816 502	-	1 816 502

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

Level III	Financial assets					
	Financial assets held for trading	Loans and advances to customers measured at fair value through P/L	Loans and advances to customers measured at fair value through comprehensive income	Debt securities measured at fair value through profit and loss	Debt securities measured at fair value through other comprehensive income	Equity securities measured at fair value through other comprehensive income
31.12.2018						
As at the beginning of the period	447	-	-	-	32 532	901 551
Impact of the implementation of IFRS 9	-	1 530 800	-	93 165	-	(15 094)
Profit or losses						
<i>recognised in income statement</i>	(26)	33 539	-	12 573	-	-
<i>recognised in equity (OCI)</i>	-	-	-	-	-	45 472
Purchase	-	17 294	366 751	20 013	-	2 604
Sale	(421)	-	-	-	-	(316)
Matured	-	(169 229)	-	-	(5 262)	-
Transfer	-	(90 300)	-	1 770	-	(125 320)
Other	-	37 926	-	8 990	-	-
As at the end of the period	-	1 360 030	366 751	136 511	27 270	808 897

Level III	Financial assets			Financial liabilities
	Financial assets held for trading	Financial investment assets - debt securities	Financial investment assets - equity securities	Financial liabilities held for trading
31.12.2017				
As at the beginning of the period	251	38 240	849 578	-
Profit or losses				
<i>recognised in income statement</i>	(29)	-	-	-
<i>recognised in equity</i>	-	-	68 337	-
Purchase	1 057	-	2 036	-
Sale	(832)	-	(18 400)	-
Matured	-	-	-	-
Transfer	-	-	-	-
Other - bonds redemption	-	(5 708)	-	-
As at the end of the period	447	32 532	901 551	-

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

The value of all litigation amounts to PLN 1,328,055 k, which is 4.98% of the Group's equity. This amount includes PLN 730,097 k claimed by the Group, PLN 550,808 k in claims against the Group and PLN 47,150 k of the Group's receivables due to bankruptcy or arrangement cases.

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. 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.

As at 31.12.2018 the amount of significant court proceedings which had been completed amounted to PLN 565,324 k.

As at 31.12.2018, the value of provisions for legal claims was PLN 132,382 k. In 37 cases against Santander Bank Polska SA, 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.

Santander Bank Polska SA 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 36.

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

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

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

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

Off-balance sheet liabilities

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

Contingent liabilities - sanctioned	Stage 1	Stage 2	Stage 3	31.12.2018	31.12.2017
Liabilities sanctioned					
- financial	27 932 101	461 631	83 414	28 477 146	24 642 271
- credit lines	23 100 430	392 403	70 976	23 563 809	20 279 546
- credit cards debits	4 035 243	57 473	12 438	4 105 154	3 730 667
- import letters of credit	788 817	11 755	-	800 572	624 207
- term deposits with future commencement term	7 611	-	-	7 611	7 851
- guarantees	5 438 168	141 102	27 530	5 606 800	4 885 661
Provision for off-balance sheet liabilities	(33 235)	(12 343)	(35 470)	(81 048)	(50 652)
Total	33 337 034	590 390	75 474	34 002 898	29 477 280

46.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 and Santander Consumer Bank applied 0.50% (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 658,739 k compared with PLN 605,429 k a year before.

In 2018, deposits opened with financial institutions to secure the value of transactions totalled PLN 1,265,897 k (in 2017 – PLN 772,961 k).

In 2018, the Group accepted PLN 200,887 k worth of deposits securing transactions (vs. PLN 500,105 k in 2017).

Other assets pledged and liabilities accepted as collateral are disclosed in Notes 32 and 43.

47. Finance and operating leases

Finance leases

Lease agreements where the Group acts as a lessor

Santander Bank Polska Group conduct leasing activity through leasing companies which specialise in funding vehicles, means of transport, machines and equipment for businesses and personal customers and property.

The items "Loans and advances to customers" and "Loans and advances to banks" contain the following amounts relating to the finance lease obligations:

Finance leases gross receivables - maturity	31.12.2018	31.12.2017
less than 1 year	3 217 790	2 724 540
between 1 and 5 years	5 425 275	4 452 169
over 5 years	101 820	115 819
Total	8 744 885	7 292 528

Present value of minimum lease payments - maturity	31.12.2018	31.12.2017
less than 1 year	3 268 594	2 751 560
between 1 and 5 years	4 868 075	4 011 195
over 5 years	75 693	86 205
Total	8 212 362	6 848 960

Reconciliation between the finance lease receivables and the present value of minimum lease payments	31.12.2018	31.12.2017
Finance lease gross receivables	8 744 885	7 292 528
Unearned finance income	(532 523)	(443 568)
Impairment of finance lease receivables	(111 875)	(84 140)
Present value of minimum lease payments, net	8 100 487	6 764 820

Lease agreements where the Group acts as a lessee

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

Operating leases

Lease agreements where the Group acts as a lessee

Santander Bank Polska SA leases offices in compliance with operational leasing agreements. As a standard, agreements are concluded for a period over 5 years. An insignificant part of the offices is subleased outside the Group. In 2018 and 2017 rentals totalled PLN 222,959 k and PLN 234,684 k, respectively. These payments are presented in the profit and loss account under "Operating expenses".

The majority of lease agreements signed by Santander Consumer Bank SA were concluded for a definite period of time ranging from three to five years. As regards the premises for mobile units and offices of the hire purchase structure the lease agreements were entered for an indefinite period subject to two up to six months' notice.

PSA Finance Polska, acting together with its subsidiary PSA Consumer Finance Polska, leases mainly office space under the agreement renegotiated in 2016 and valid until 2021.

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

Lease payments - maturity	31.12.2018	31.12.2017
less than 1 year	212 026	208 032
between 1 and 5 years	539 677	474 185
over 5 years	152 639	384 471
Total	904 342	1 066 688

Lease agreements where the Group acts as a lessor

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

Future minimum lease fees due to irrecoverable operating lease	31.12.2018	31.12.2017
less than 1 year	11 025	9 301
between 1 and 5 years	8 929	9 160
over 5 years	-	-
Total	19 954	18 461

48.Consolidated 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 Group.

Cash and cash equivalents	31.12.2018	31.12.2017
Cash and balances with central banks	8 856 479	4 146 222
Receivables from interbank deposits*	3 105 091	2 136 307
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	18 012 307	7 662 368
The impact of changes in currency exchange rates during the financial year on cash and cash equivalents	39 420	(89 445)

* financial assets with initial maturity below three months

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

In the periods presented in the financial statement Santander Bank Polska Group 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:	7 054 874	6 542 339
- operating activities	6 307 596	5 875 868
- investing activities	747 278	666 471
Interests paid, including:	(1 552 820)	(1 231 416)
- operating activities	(1 271 805)	(993 307)
- financing activities	(281 015)	(238 109)

The table below shows acquisition of demerged 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

49. Related parties

The tables below present intercompany transactions. They are effected between associates and related entities. Most of the transactions are banking transactions made as part of ordinary business activities and mainly include loans, deposits, guarantees and leases. Intercompany transactions effected within the Group by the Bank and its subsidiaries have been eliminated from the consolidated financial statements. In the case of internal Group transactions, a documentation is prepared in accordance with requirements of tax regulations for transfer pricing.

Transactions with associates	31.12.2018	31.12.2017
Assets	85	93
Other assets	85	93
Liabilities	105 680	120 382
Deposits from customers	105 519	90 102
Sell-buy-back transactions	-	30 044
Other liabilities	161	236
Income	38 779	14 223
Fee and commission income	38 779	14 223
Expenses	5 532	6 654
Interest expense	1 512	1 806
Fee and commission expense	2 406	3 020
Operating expenses incl.:	1 614	1 828
<i>General and administrative expenses</i>	<i>1 614</i>	<i>1 828</i>

Transactions with Santander Group	with the parent company		with other entities	
	31.12.2018	31.12.2017	31.12.2018	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
<i>Loans and advances</i>	583 784	95 993	-	-
<i>Current accounts</i>	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	127 328	86 720
Deposits from banks incl.:	294 866	62 996	10 721	23 539
<i>Current accounts</i>	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	16 477	10 604
Income	120 921	14 914	16 324	411
Interest income	11 036	11 321	235	95
Fee and commission income	2 595	3 593	414	299
Other operating income	5	-	94	17
Net trading income and revaluation	107 285	-	15 581	-
Expenses	23 674	94 960	44 622	76 712
Interest expense	1 574	1 050	459	2 298
Fee and commission expense	1 222	1 171	148	205
Net trading income and revaluation	-	74 862	-	57 672
Operating expenses incl.:	20 878	17 877	44 015	16 537
<i>Staff, Operating expenses and management costs</i>	20 877	17 877	44 013	16 529
<i>Other operating expenses</i>	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	-	-

Transactions with Members of Management and Supervisory Boards

Remuneration of Santander Bank Polska Management Board Members, Supervisory Board Members and key management Santander Bank Polska Group's.

Loans and advances granted to the 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	45 666
Additional benefits (e.g among others, life insurance cover without pension option, medical cover, travel expenses and school fees)	1 066	1 136	1 107	1 062
The awards paid in 2018 and 2017 *	9 940	8 186	21 236	16 587
Equivalent paid for unused annual leave	146	125	136	130
Additional compensation for termination of the contract and the non-competition clause	1 105	-	208	-
Loans and advances made by the Bank to the Members of the Management Board/Key Management and to their relatives	10 103	11 054	25 188	22 693
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	4 873	2 651
The number of conditional rights to shares	27 220	34 670	42 652	41 194

* included part of the award for 2017, 2016, 2015, 2014 and 2013 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" and in the case of subsidiaries - by the principles outlined in their respective internal regulations.

Santander Bank Polska Group 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 (PLN 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).

50. 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 51.

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.

51. 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 (+95k clients), and also in the mass segment with new 226k clients. In addition, new 35k 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 Polska S.A. 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 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
Ordinary shares issued	1 031 839
Total purchase consideration	1 289 799

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, the Group of 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	DB Securities
ASSETS			
Cash and balances with central banks		51 073	-
Loans and advances to banks		405	159 690
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	-
Investment securities incl.:		83 090	271
- debt securities measured at fair value through other comprehensive income		63 077	-
- debt securities measured at fair value through profit and loss		20 013	-
- equity securities measured at fair value through other comprehensive income		-	271
Intangible assets		195 977	1 041
Property, plant and equipment		19 043	125
Net deferred tax assets		52 972	940
Other assets		37 017	17 896
Total assets		19 245 139	179 963
LIABILITIES			
Deposits from banks		4 430 226	74
Financial liabilities held for trading		12 122	-
Deposits from customers		13 041 354	130 095
Provisions for off balance sheet credit risk		7 945	-
Other provisions		5 230	-
Other liabilities		113 698	6 826
Total liabilities		17 610 575	136 995
Net assets acquired		1 634 564	42 968

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 result from by the fact that such relationships provide Santander Bank Polska with numerous benefits such as potentially reduced selling and marketing costs, 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

As regards fair value adjustment on performing loans, it was calculated also based on discounted cash flows (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 covered 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 portfolio 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 POI 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 602,584 k.

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.

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, the Group of Santander Bank Polska 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 in the 'Gain on acquisition of enterprise' in the consolidated 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	(1 677 532)
Total	(387 733)

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 assess 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.

Purchase consideration – impact 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 a functional break down of the above mentioned costs:

Salaries and bonuses	26 529
Consulting fees	30 061
IT costs	10 330
Administrative expenses	23 364
Marketing and communication	12 899
Other costs	5 687
Total	108 870

In addition, Santander Bank Polska S.A. recognized additional allowance for impairment receivables taken over in the purchase transaction for the amount of PLN 130,473 k.

52. Employee benefits

Staff benefits include the following categories:

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

Within these categories, the companies of the Santander Bank Polska Group create the following types of provisions:

Provisions for unused holidays

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

Provisions for employee bonuses

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

Provisions for retirement allowances

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

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

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

The amount of the retirement 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 probability of an individual get to the retirement age or die while working is determined using the multiple decrement model, taking into consideration the following risks: possibility of dismissal from service, risk of total disability to work and risk of death.

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

- interest rate risk – the decrease in market yields on government bonds would increase the defined benefit plans obligations,

- remuneration risk – the increase in remuneration of the Bank’s employees would increase the defined benefit plans obligations,
- mobility risk – changes in the staff rotation ratio,
- longevity risk – the increase in life expectancy of the Bank’s employees would increase the defined benefit plans obligations.

The principal actuarial assumptions as at 31 December 2018 are as follows:

- the discount rate at the level of 3.15% (3.3% as at 31 December 2017),
- the future salary growth rate at the level of 2.0% (2,0% as at 31 December 2017),
- the probable number of leaving employees calculated on the basis of historical data concerning personnel rotation in the Group,
- the mortality adopted in accordance with Life Expectancy Tables for men and women, published the Central Statistical Office, adequately adjusted on the basis of historical data of the Bank.

Reconciliation of the present value of defined benefit plans obligations

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

	31.12.2018	31.12.2017
As at the beginning of the period	72 726	60 397
Provision acquired in a business combination	5 407	-
Current service cost	2 163	308
Prior service cost	(28 357)	-
Interest expense	1 607	2 611
Actuarial (gains) and losses	(12 688)	9 410
Balance at the end of the period	40 858	72 726

Sensitivity analysis

The following table presents how the impact on the defined benefits obligations would have increased (decreased) as a result of a change in the respective actuarial assumptions by one percentage point as at 31 December 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 December 2017.

Defined benefit plan obligations	1 percent increase	1 percent decrease
Discount rate	9,00%	-9,78%
Future salary growth rate	-9,91%	7,04%

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	59 853	58 392
Provisions for employee bonuses	286 302	257 986
Provisions for retirement allowances	40 858	72 726
Other staff-related provisions	17 329	18 618
Total	404 342	407 722

Detailed information on employee provisions have been presented in Note 37

53. 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.

Share based payments granted in 2017:

	2017
Number of share based payments	131 262
Share price	350.00 PLN
Exercise price	10
Vesting period	3 years
Expected volatility of share prices	30.07%
Award life	3 years
Discounted risk free rate	2.12%
Fair value per award	323.36 PLN
Dividend yield	1.71%

The table below summarizes movement in the plan:

	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 years 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 12,446 k and PLN 7,173 k respectively.

The table below presents information about the number of conditional rights to shares vested in Santander Bank Polska SA Management Board members under the 5th Incentive Scheme and the 6th Incentive Scheme in 2017.

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

The table below presents information about the number of conditional rights to shares vested in Santander Bank Polska Group Key Management.

No. of awards	2018	2017
Outstanding at 1 January	41 194	31 415
Granted	-	44 134
Expired	-	(9 484)
Exercised	-	(19 616)
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	42 652	41 194

54. Dividend per share

As of the date of publication of this report, the Management Board of Santander Bank Polska 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.

55. 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.

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 Porrás 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 Strojowska	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	