INFORMATION ON CAPITAL ADEQUACY OF BANK ZACHODNI WBK GROUP

as at 31th December 2014

2014

Bank Zachodni WBK

Grupa Santander

TABLE OF CONTENTS


Zachodni WBK

1. Introduction

This document is issued under the Bank Zachodni WBK Group Disclosure Strategy formulated based on 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 which formed the legal basis of the reporting date i.e. 31 December 2014.

Starting from January 1st, 2014 by the decision of the European Parliament and of the Council the new regulations of the CRD IV/CRR package come into force. The CRD IV/CRR package consist of two parts, the CRD IV Regulation and CRR Directive. The Directive requires transposition to the specific country law while the Regulation is binding without any transposition in all the member countries of the EU.

Bank Zachodni WBK is the significant subsidiary of Banco Santander S.A. with its seat in Spain, which is the EU parent institution. Bank Zachodni WBK S.A. discloses information about the capital adequacy on a consolidated basis – at the highest local level of prudential consolidation – i.e. based on the data of Bank Zachodni WBK.

The purpose of the report is to present information about the capital adequacy of the Bank Zachodni WBK Group pursuant to the requirements laid down in Article 13 of CRR (i.e. disclosure of information laid down in Articles 437, 438, 440, 442, 450, 451 and 453 of CRR).

The data presented in the report were prepared as at 31 December 2014 and include:

- Risk management principles
- Own funds
- Value of Risk Weighted Assets
- Information on capital adequacy
- Remuneration policy for those categories of staff whose professional activities have a material impact on its risk profile.

Bank Zachodni WBK forms a Group with 16 subsidiaries which are consolidated in accordance with IAS 27 and one subsidiary which is not consolidated and associates which are accounted for using the equity method.

The subsidiaries are fully consolidated with Bank Zachodni WBK except for Lizar Sp. z o.o. which is excluded from consolidation due to the insignificant scale of its operations and reported financials.

The scope of consolidation used by Bank Zachodni WBK Group for the purpose of capital adequacy assessment in accordance with CRR is different than the scope of consolidation adopted for the published consolidated financial statements of the Group made in compliance with IAS/IFRS. The subsidiaries BZ WBK Aviva Towarzystwo Ubezpieczeń Ogólnych S.A., BZ WBK Aviva Towarzystwo Ubezpieczeń na Życie S.A. BZ WBK Nieruchomości S.A. and Giełdokracja Sp. z o.o. are excluded from prudential consolidation.

As at 31 December 2014, Bank Zachodni WBK formed a Group with the **following subsidiaries**:

- Santander Consumer Bank S.A. (SCB S.A.)
- Santander Consumer Finanse S.A. – subsidiary of SCB S.A.
- AKB Marketing Services Sp. z o.o. - subsidiary of SCB S.A.
- Santander Consumer Multirent Sp. z o.o.- subsidiary of SCB S.A.
- S.C. Poland 2014-1 Limited - subsidiary of SCB S.A.
- BZ WBK Asset Management S.A.
- BZ WBK Towarzystwo Funduszy Inwestycyjnych S.A. - subsidiary of BZ WBK Asset Management S.A.
- BZ WBK-Aviva Towarzystwo Ubezpieczeń Ogólnych S.A.*
- BZ WBK-Aviva Towarzystwo Ubezpieczeń na Życie S.A.*
- BZ WBK Finanse Sp. z o.o.
- BZ WBK Faktor Sp. z o.o. - subsidiary of BZ WBK Finanse Sp. z o.o.
- BZ WBK Leasing S.A. - subsidiary of BZ WBK Finanse Sp. z o.o.
- BZ WBK Lease S.A. - subsidiary of BZ WBK Finanse Sp. z o.o.
- Lizar Sp. z o.o. - subsidiary of BZ WBK Lease S.A.
- BZ WBK Inwestycje Sp. z o.o.
- BZ WBK Nieruchomości S.A.*
- Giełdokracja Sp. z o.o.*

*Company excluded from prudential consolidation in accordance with CRR

Compared with 31 December 2013, Bank Zachodni WBK Group was extended by four entities as a result of the following:

- Acquisition by Bank Zachodni WBK of 3,120,000 ordinary and preferred shares in SCB with its registered office in Wrocław with a nominal value of PLN 100 each, representing 60% of the share capital and approximately 67% of votes at the General Meeting of SCB pursuant to the Investment Agreement of 27 November 2013 between Bank Zachodni WBK, Santander Consumer Finance and Banco Santander on the acquisition of shares in Santander Consumer Bank by way of private placement and in-kind contribution. As a result of the abovementioned transaction, Bank Zachodni WBK gained control over SCB and its four subsidiaries.
- Removal of Dom Maklerski BZ WBK (Brokerage House) from the business register (KRS) without a liquidation procedure on 31 October 2014 and its division in accordance with the Division Plan of 24 July 2014 through:
  - Transfer to Bank Zachodni WBK of an organised part of the enterprise of the Brokerage House connected with the provision of brokerage services and other services which do not constitute the advertising business;
  - Set-up of Giełdokracja, a limited liability company, which took over a part of the enterprise connected with provision of educational services related to the capital market, advertising and communication services, and maintenance of internet portals (all shares were taken up by Bank Zachodni WBK as the sole shareholder of the former Brokerage House).
- Removal of BFI Serwis in liquidation from the business register (KRS) on 20 November 2014.

As a result of the above-mentioned changes, the Brokerage House is now a unit of the bank which meets the definition of a brokerage office and conducts brokerage activity in accordance with the clearance issued by the Polish Financial Supervision Authority (KNF) on 10 June 2014.

Currently, the largest subsidiary in Bank Zachodni WBK Group is Santander Consumer Bank, which forms SCB Group with four subsidiaries: Santander Consumer Finanse (investment of cash surpluses and cooperation with Bank Zachodni WBK and Warta in terms of financial advisory services), AKB Marketing Services (auxiliary banking services), Santander Consumer Multirent (leasing) and S.C. Poland 2014-1 Limited (SPV set up for the purpose of securitisation transaction).

Associated companies

In the consolidated financial statements of Bank Zachodni WBK for the 12-month period ended 31 December 2014, the following companies are accounted for using the equity method in accordance with IAS 28:

- Metrohouse Franchise S.A. - associated undertaking of BZ WBK Inwestycje Sp. z o.o.
- Metrohouse S.A. – subsidiary of Metrohouse Franchise S.A.
- POLFUND - Fundusz Poręczeń Kredytowych S.A.

As part of organisational changes in Metrohouse Group, in September 2014, BZ WBK Inwestycje contributed all shares of Metrohouse to Metrohouse Franchise (registered on 1 July 2014) in exchange for 41,630k shares in Metrohouse Franchise representing 20.58% stake in the share capital and voting power in the company. As a result of another increase in the share capital of Metrohouse Franchise, the share of BZ WBK Inwestycje in the above company was 20.13% as at 31 December 2014.

In December 2014, BZ WBK Inwestycje sold 320,000 shares in Krynicki Recycling, reducing its stake in the share capital to 19.96%. In consequence, the company was removed from the list of associates as at 31 December 2014.

Bank Zachodni WBK
Grupa Santander

2. Risk Management

Bank Zachodni WBK Group monitors and manages a number of risks, the key ones being credit risk, market risk, liquidity risk and operational risk. The purpose of risk management is to ensure that Bank Zachodni WBK Group takes risk in a conscious and controlled manner while increasing value for shareholders.

As part of the strategic risk management the Group creates policies that define the approach to the identification and measurement of risks and the optimal risk-to-reward ratio. The Group also determines and reviews its risk appetite. Bank Zachodni WBK Group regularly reviews and develops its risk management tools taking into account changes in the Group's risk profile, changes in the financial services sector, legislation and best market practices.

The Management Board and Supervisory Board of Bank Zachodni WBK set the tone for 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.

Detailed rules as well as roles and responsibilities of individual units of Bank Zachodni WBK Group are described in relevant internal risk management policies.

Bank Zachodni WBK Group places focus on the consistency of its risk management processes to ensure adequate control over risk exposure. Policies and procedures implemented by the subsidiaries reflect the standards applied by the Group.

In keeping with the applicable law, the bank exercises oversight over the risk management system in Santander Consumer Bank (SCB), in line with the rules applied by Bank Zachodni WBK Group to supervision of its subsidiaries. Management Board member in charge of the Risk Management Division and Management Board member in charge of the Financial Management Division sit on the Supervisory Board of SCB as representatives of the bank. In line with Bank Zachodni WBK strategy for equity investments, they are responsible for supervising the activity of SCB and ensuring that it operates in compliance with the adopted plans and procedures safeguarding security of its operations. The bank monitors risk level and profile of SCB by means of Bank Zachodni WBK risk management committees.

Details about managing different risk types, the structure of corporate governance and roles of selected units in risk management oversight are presented in **Note 4** of the Consolidated Financial Statements of Bank Zachodni WBK Group for 2014.

2.1. Credit risk

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

Credit risk is defined as the possibility of suffering a loss resulting from the borrower's failure to meet its credit obligations, 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 Bank Zachodni WBK Group arises mainly from **lending activities on the retail, corporate and interbank markets**. This risk is managed as part of the policy approved by the Management Board on the basis of the adopted credit procedures as well as on the basis of discretionary limits allocated to individual credit officers based on their knowledge and experience. The Group's internal system of credit grading and monitoring allows for an early identification of likely defaults that might impair the loan book. Additionally the Group uses multiple credit risk mitigation tools, both collateral (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 significant credit portfolios.

Pro-active credit risk management is recognised as key to Bank Zachodni WBK Group's performance in the volatile markets and deteriorating economic growth conditions. In 2014, the Group continued its conservative credit risk management policy with the focus on ensuring a balanced growth of the high quality credit portfolio. The observed dynamic growth of loan portfolio volumes was driven by favourable macroeconomic developments, optimisation of credit policies and processes, development of loan portfolio management tools (in particular, for the SME and corporate portfolios) as well as finalised standardisation of policies and tools after the merger with Kredyt Bank. Credit policies were optimised in response to macroeconomic developments, such as interest rate cuts.

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

The Group is closely looking at the macroeconomic environment and monitoring 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 Bank also introduced changes to its pricing policy in response to falling reference rates.

Forbearance Policy

In 2014, the Bank established a Restructuring Committee to further improve the quality of the loan portfolio through the early implementation of debt restructuring actions and arrangements to streamline the debt service for corporate borrowers. The Committee takes decisions concerning:

- the relationship management strategy for corporate borrowers in distress whose exposure does not exceed PLN 25m,
- debt cancellation,
- sale of receivables.

Decisions on distressed corporate borrowers with exposure in excess of PLN 25m are made by Credit Committee.

Debt restructuring solutions for corporate borrowers are provided only after an analysis of the borrower's financial standing, identification of the underlying causes for problems with debt service, assessment of repayment capacity under the new conditions and assessment of the collateral in place. The restructuring arrangements depend on the result of the assessment and may include in particular: a grace period, change of the repayment schedule (reduction of loan instalments), capitalisation of interest, extension of the maturity date etc. This applies both to retail and business customers.

From 2014 onwards, each debt restructuring arrangement is accompanied by respective entries to the Bank's IT systems, so that the restructured debt portfolio can be identified, i.e. by the time when the customer's standing is considered to have stabilised, terms of restructure have been met and the customer has regained their repayment capacity. The receivables/customer is treated as a restructured borrower throughout the restructuring period. The portfolio of restructured debt is monitored on a regular basis. The restructuring process is often a long-term one, therefore the bank assumes that the applied solutions will increase the restructured portfolio in consecutive periods. Classification of customers to respective restructuring categories is independent of the classification to performing/non-performing portfolio.

Under the adjustment process to new reporting requirements, solutions were developed to ensure the identification of debt restructuring cases including the project of changes in the ITS standard proposed by EBA. The identification is based on debt restructuring made both in the performing portfolio and the non-performing one, in line with the definition provided in Recommendation R. The basic information considered during the identification of forbearance cases includes: the borrower's current financial standing, observed and expected repayment capacity, willingness to make repayments as well as the nature and frequency of amendments to loan repayment terms for facilities held by a given borrower. Those rules apply both to retail and corporate customers.

Risk Management Forum

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

The oversight over the credit risk models is the responsibility of the **Models and Methodology Panel.**

Risk Management Division

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

Credit Policies

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

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.

Collateral

In the Group's security model, **the Securities and Credit Documentation Centre** is the central unit responsible for creation and maintenance of securities.

The role of the Centre 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 collatera**l as well as ensuring that establishment, monitoring and release of security covers is duly effected.

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

Retail customers

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

Business customers

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

Credit risk stress testing

Stress testing is a part of the credit risk management process used to evaluate potential effects of specific events or movements of a set of financial and macroeconomic variables or change in risk profile on Bank Zachodni WBK Group’s standing. 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 limits and internal capital allocation.

Calculation of impairment

In Bank Zachodni WBK Group, charges updating impairment are recognised in accordance with the International Accounting Standards/International Financial Reporting Standards (IAS/IFRS). The charges reflect credit impairment, which is recognised if the Group presents objective evidence that such amounts cannot be recovered in line with the signed loan agreement. Objective evidence of impairment was defined in accordance with recommendation of Basel Committee, with the International Accounting Standards (IAS 39) and Recommendation R.

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

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

Details about impairment charges are presented in **Note 4** of the Consolidated Financial Statements of Bank Zachodni WBK Group for 2014.

Leasing and factoring

Bank Zachodni WBK Group has **leasing operations** that specialise in leasing machines, computer hardware and office equipment for business customers. The Group's leasing companies also finance vehicles for both business and retail customers. The Group's **factoring operations** are conducted by BZ WBK Faktor Sp. z o.o. Factoring is a short-term finance for the companies that provide trade credit (i.e. supply goods or services on extended payment terms) to their counterparties.

2.2. Market risk

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

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

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

The key objective of the **market risk policy** pursued by the Group is to reduce the impact of interest and FX rate changes on the Group's profitability and market value as well as to grow income within the strictly defined risk limits while ensuring the Group's liquidity.

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

Interest rate risk and FX risk 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 from time to time by the Risk Management Forum, the bank's Management Board and the Supervisory Board.

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

The market risk on the trading portfolio is managed by the **Global Banking & Markets Division**, which is also responsible for the ownership supervision over Brokerage House. 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. This limits are approved by the Risk Management Forum, the bank's Management Board and the Supervisory Board.

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

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

Assessment methods

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

VaR is determined by means of a statistical modelling process as a difference between the mark-to-market value of positions and the market values based on the most severe movements in market rates from a determined observation window. VaR is calculated separately for interest rate risk, FX risk and the repricing risk of the equity instruments portfolio of Brokerage Office.

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

Interest rate position risk

Interest rate position risk in the banking book

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

The bank's subsidiaries also mitigate their exposure to the interest rate risk. If there is a mismatch between the repricing of assets and liabilities, the company enters into appropriate transactions via the standard bank accounts held with the bank or makes derivative transactions with the bank, which from the transaction date manages the risk as part of the global limit of Bank Zachodni WBK Group.

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

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

In 2014, the global NIM and MVE limits for the banking book were not exceeded.

Interest rate position risk in the trading book

The trading book contains securities and derivatives held by the Global Banking & Markets Division for trading purposes. The instruments are marked to market each day, and any changes in their value are reflected in the profit and loss.

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

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

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

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

The total regulatory capital requirement for the risk of debt instruments is calculated for the positions generated by transactions in the trading portfolio, using maturity ladders approach.

FX risk

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

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

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

In 2014, the FX VAR limit was exceeded. Positions for individual currencies were within established nominal limits, however, exceeded the VaR limit. The next day, open position (EUR) was limited and VAR was in the prescribed limit. In 2014, this was the only case of exceeding the VaR limit, reported to the appropriate committees appointed by the Management Board and the Supervisory Board.

FX Balance Sheet

In 2014, the share of assets in foreign currencies in the balance sheet remained at the level observed in 2013, alike the mismatch of assets and liabilities in particular currencies. Observed structural fx gap was funded mainly from FX swaps, FX interest rate swaps.

Capital requirement for FX risk is calculated using the basic approach as:

1) 8% of the total FX position - if the FX position exceeds 2% of own funds

2) zero – if the total FX position accounts for less than 2% of own funds.

As at 31 December 2014, the total FX position was not higher than 2% of own funds of Bank Zachodni WBK Group.

Equity instruments position risk

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

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

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

2.3. Liquidity risk

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

The Bank Zachodni WBK Group Liquidity Management Policy is designed to:

- ensure the ability to finance assets and satisfy claims, both current and future, in a timely manner and at an economic price
- manage the maturity mismatch between assets and liabilities
- set a scale of the liquidity risk in the form of various internal limits
- ensure proper organization of the liquidity management process within the Group
- prepare the organization for emergence of adverse factors, either external or internal

- ensure compliance with regulatory requirements, both qualitative and quantitative.

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

In addition, the policy's aim is to ensure an adequate structure of funding the growing scale of the Group's business by maintaining liquidity ratios at pre-defined levels. The Group uses a number of other limits and observation ratios (including the loans to deposits ratio, the ratio of dependence on funding in the wholesale market, and the ratios required by Basel 3: LCR and NSFR). In terms of the long-term liquidity, in addition to the internal measures, the Group uses a limit corresponding to the regulatory limit, which requires that the equity and the stable sources of funding should fully cover the credit portfolio and non-liquid assets (e.g. fixed assets).

Management Process

The responsibility for supervision over the liquidity risk management process rests on the Assets and Liabilities Committee (ALCO), which also provides advice to the Management Board. ALCO prepares management strategies and recommends to the Management Board appropriate actions with regard to strategic liquidity management.

Day-to-day management of liquidity is delegated to the Financial Management Division. The Assets and Liabilities Management Department, which is a part of the Division, is responsible for developing and updating the relevant liquidity management strategies.

The Group has a scenario-based contingency plan approved by the Management Board to cater for unexpected liquidity problems, whether caused by external or internal factors. The plan also contains stress test with systemic and idiosyncratic scenarios. ALCO supervises liquidity risk management process in subsidiaries.

Risk Measurement and Reporting

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

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

2.4. Operational risk

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

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

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

Bank Zachodni WBK Group has defined the **Operational Risk Management Strategy** and the **Operational Risk Management Policy and Framework**. In addition, detailed procedures and guidelines are used to define how risks are identified, estimated, monitored and mitigated.

The Operational **Risk Management Committee** (ORMCo) established by the Management Board is responsible for setting operational risk management standards for Bank Zachodni WBK Group. ORMCo is the main forum for discussions on operational risk. It sets out the strategic direction for operational risk management, determines and monitors objectives for managing operational risk, including business

[†] This definition includes legal risk but excludes strategic and reputation Risk.

continuity, information security, outsourcing / insourcing and money laundering risk in all business areas of Bank Zachodni WBK. The effects of this work are reported to the Risk Management Committee.

In 2014, special tasks relating to operational risk management and post-merger integration initiatives were being pursued, which included mass migration of data of the former Kredyt Banku to the IT systems of Bank Zachodni WBK. To maintain the highest standards of operational risk management, all the migration processes were subject to a comprehensive risk analysis. Thanks to the professional approach and effective operational risk management that included e.g. numerous pre-migration tests and problem-solving at source ensured that the process was smooth and that any unplanned stoppages in system operations.

In 2014, Bank Zachodni WBK also took steps to become compliant with Recommendation D. Changes were implemented in IT technology management and ITC environment security to reflect the best industry practice.

Bank Zachodni WBK Group uses the following **tools**:

- Identification and assessment of operational risk

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

- Reporting on operational incidents and lessons learned

Each organisational unit is required to report operational incidents on a monthly basis. The Group runs a database of operational incidents identified across Bank Zachodni WBK Group. The data are used to analyse the root cause and consequences of the incidents, capture lessons learned and take preventive and corrective measures.

Operational incidents in Bank Zachodni WBK Group in 2014
gross losses (PLN k)

Operational event class			
Event types	**Event category**	**PLN k**	**%**
1 Internal fraud	1.1. Unauthorised activity	443	0,75%
	1.2. Theft and fraud	2 123	3,59%
2 External fraud	2.1. Theft and fraud	29 547	49,91%
	2.2. Systems security	282	0,48%
3 Rules for employment and safety at work	3.1. Employee relations	779	1,32%
	3.2. Safe environment	2	0,00%
4 Customers, products and operating practices	4.1. Customer service, privacy breaches, obligations to customers	544	0,92%
	4.2. Improper trade / market practices	11 840	20,00%
	4.3. Product flaws	2 925	4,94%
5 Damage to tangible assets	5.1. Natural disasters and other incidents	2 904	4,90%
6. Business interruption and system errors	6.1. Systems	43	0,07%
7 Execution of transactions, delivery and management of operating processes	7.1. Transaction capture, execution and maintenance of transactions	6 235	10,53%
	7.2. Monitoring and reporting	7	0,01%
	7.3. Customer acquisition and preparation of documentation	2	0,00%
	7.4. Customer account management	642	1,08%
	7.5. Counterparties other that the Bank's clients (e.g. clearing chambers)	138	0,23%
	7.6. Vendors and suppliers	750	1,27%

In "External fraud – theft and fraud" (2.1), most losses are connected with the credit process. In 2014, credit-related losses accounted for 65% of all losses reported under this category. It should be noted, though, that Bank Zachodni WBK Group adopted a very restrictive definition of external fraud. For example, in this category the Group includes situations where the customer used false employment or salary certificate/statement, or cases of business activity being conducted without due registration. To reduce fraud, Bank Zachodni WBK is constantly improving its vetting, control and monitoring processes using advanced models and specialist IT systems. The increase in losses vs. previous year primarily results from credit growth at Bank Zachodni WBK (including the impact of acquisition of the credit portfolio of Santander Consumer Bank, affiliate that was incorporated in the Group on 01 07 2014).

The value of losses in 2014 in "Inappropriate business or market practices" (4.2.) was largely affected by one identified event. The case was thoroughly analysed to identify its causes and to prevent its future reoccurrence. As a result of the analysis, processes were improved as procedural and system solutions were put in place.

The increased value of losses under "Transaction capture, execution and maintenance of transactions" (7.1) results from materialisation of a single internal event resulting from non-compliance with the applicable procedures. To prevent the risk of similar incidents occurring in the future, awareness-raising initiatives were carried out and an IT solution was designed to optimise the process.

- Analysis of risk indicators

Bank Zachodni WBK Group monitors risk indicators, both financial and operational ones. Risk indicators provide early warning of emerging threats and operational losses and depict the risk level present in the Group.

- Business continuity management (BCM)

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

- Insurance

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

- Regular reporting to the Risk Management Committee and Supervisory Board

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

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

2.5. Legal & compliance risk

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

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

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

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

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

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

The Audit and Compliance Committee regularly reviews key compliance issues identified by the Compliance Area:

- as part of compliance monitoring
- as part of the monitoring of proprietary transactions effected by employees

- based on the information on regulators' activity
- as part of the review of upcoming legislative initiatives
- as part of the review of anti-money laundering initiatives
- as part of the review of ethical issues
- as part of the review of customers' complaints.

The Compliance Area's major responsibilities include (subject to the specific responsibility of Financial Accounting and Control Division, Risk Management Division and Business Partnership Division): prevention of legal and compliance risk, maintenance of appropriate relations with business units and market regulators, providing support to the Bank management and Bank Zachodni WBK Group companies in the strategic decision-making process regarding compliance, coordination (under the applicable laws) of the implementation of compliance management standards by compliance units operating in the Group companies.

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

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

2.6. Reputation risk

Reputation risk is defined as the risk arising from negative perception of the bank and other companies from Bank Zachodni WBK Group by customers, counterparties, shareholders or investors.

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

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

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

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

Key risk mitigation measures:

- Monitoring of local, nationwide and certain international mass media sources (Corporate Communication and Marketing Area)
- Daily monitoring of social media sources (in particular: Facebook, Twitter) in the context of references to Bank Zachodni WBK (Corporate Communication and Marketing Area)
- Collection and analysis of image-sensitive information by the Press Office (Corporate Communication and Marketing Area)
- Response to information which poses a threat to public perception of the Bank Zachodni WBK Group's image (Corporate Communication and Marketing Area)
- Keeping the representatives of nationwide and local media up to date about new products and changes to the regulations regarding the existing products
- Customer satisfaction index (Corporate Communication and Marketing Area)
- Preparation and control by relevant Bank Zachodni WBK units of all important communiqués and reports for the shareholders, the Polish Financial Supervision Authority (KNF) and the Warsaw Stock Exchange and timely publication of such communiqués and reports;

- Evaluation of new products or their modifications, procedures, commercial materials, processes and other bank initiatives (promotions, contests), training materials for sales staff - in respect of their compliance with the regulations and the regulatory guidelines (Compliance Area)
- Participation in the process of handling customer complaints, especially those addressed to the regulators (Compliance Area)
- Supervision of the after-sales control of investment products (Compliance Area)
- Mystery shopping surveys for investment products (Compliance Area)
- Regular monitoring of the reputation risk associated with the products offered by Bank Zachodni WBK Group through the analysis of customer complaints, sales volumes, number of customers and rate of return (Compliance Area).

Reputation risk is not and will not be quantified as this is a risk type that is hard to measure otherwise than in qualitative terms.

Bank Zachodni WBK
Grupa Santander

3. Own funds

The level of own funds of the Bank Zachodni WBK Group is adjusted to the Group's business.

Own funds are calculated in accordance with the Banking Law (Journal of Laws of 2015, item 128) and legislative package of the Capital Requirements Regulation and the Capital Requirements Directive IV (“CRDIV/CRR”):

According to CRR, own funds of the Group are a sum of:

- Tier I capital
- Tier II capital

Tier I capital consists of:

- Common Equity Tier I capital, which is a sum of items of Common Equity Tier I capital items after adjustments, deductions and inclusion
- Additional Tier capital

Tier II capital includes items of Tier II capital after deduction.

Common equity Tier I consists of:

1) Share capital, fully paid and registered at its nominal value

2) Emission premium

3) Supplementary capital

4) Profit or loss eligible– pursuant to Art. 26 of CRR, the non-audited profit for the current period or the annual profit may be included in Common Equity Tier I capital, as long as the Bank is granted approval from a relevant authority (KNF in this case). Relevant authority shall issue the approval on conditions that:

    1. Profits have been verified by institution-independent persons responsible for analysing financial statements of the institution

    2. The institution has satisfactorily proved that the profit amount has been reduced by all forseeable encumbrances and dividends

5) Accumulated other comprehensive income

6) Reserve capital

7) General risk fund

8) Minority interest recognised in Common Equity Tier I capital – calculated in line with the standards indicated in Art. 84 of CRR

9) Adjustment and deductions from Common Equity Tier I items:

    a) Additional value adjustments due to the requirements of prudent valuation – acc. to Article 34 and 105 CRR

    b) Goodwill arising on acquisition

    c) Other intangible assets

    d) Surplus of deferred tax assets or liabilities exceeding 10% of Tier I - according to EBA’s interpretation re. inclusion of assets and reserves under deferred tax, in line with the answer Q&A 2014_980 , the Bank nets deferred tax assets and deferred tax liabilities in order to determine the treshold value necessary to calculate the deductible amount

e) Surplus of material exposure in financial sector institutions exceeding 10% of Tier I

f) Portion of deferred income tax assets depending on future profitability and arising from temporary differences, as well as direct and indirect holdings in Common Equity Tier I instruments, where the institution has invested a considerable amount of funds, which shall be deducted

g) Unrealised gains and losses related to assets or liabilities measured at fair value and recognised in balance sheet – disclosure in interim period in accordance with Article 467 (1) and 468 (1) of CRR.

Tier II capital includes eligible subordinated loans of the bank and instruments issued by subsidiaries that are given recognition in Tier II Capital.

Reconciliation between balance sheet items used to calculate own funds and regulatory own funds, according to methodology described in Annex I to Commission Implementing Regulation (EU) No 1423/2013 and according to article 437 (1)(a) of CRR, is presented in the table below.

Differences in own funds items of Bank Zachodni WBK Group
due to different scope of accounting and prudential consolidation
(Disclosure according to Article 2 of Commission Implementing Regulation (EU) No 1423/2013) – in PLN k

ITEMS OF CONSOLIDATED STATEMENT OF FINANCIAL POSITION USED FOR CALCULATION OF OWN FUNDS	as at 31.12.2014	Adjustments for companies that are not covered by prudential consolidation	filters	Part of year-end profit, not eligible	Deferred tax provision	BALANCE SHEET ITEMS IMPACTING REGULATORY OWN FUNDS	item no. in the table 2
Assets							
Investments in subsidiaries, associates and joint ventures, and investment financial assets :	27 099 885	-	-	-	-		
-including significant investments into financial sector entities – amount not exceeding the threshold set in Article 48(1)(b)	*49 400*	-	-	-	-	*49 400*	73
Intangible fixed assets	505 385	-69 279	-	-	0	436 106	8
Goodwill	2 542 325	-853 809	-	-	-32 398	*1 656 118*	8
Deferred tax assets (net)	1 181 610			-			
-including assets that do not exceed the threshold set in Article 48(1)(a)	*1 181 610*	*76 111*	-	-	*32 398*	*1 290 119*	75
Liabilities							
Subordinated obligations	1 539 967	-	-	-	-		
- including loans eligible as instruments under Tier II	*421 968*	-	-	-	-	*421 968*	46
Equity attributable to shareholders of BZ WBK S.A. including:							
Share capital	992 345	-	-	-	-	992 345	1
Pozostałe kapitały, w tym:	12 309 424		-	-	-		
- share premium	*7 035 424*	-	-	-	-	*7 035 424*	1
- general banking risk fund	*649 810*	-	-	-	-	*649 810*	3a
- reserve capital	*4 954 693*	*-27 929*	-	-	-	*4 926 764*	3
- supplementary capital	*353 785*	*27 702*			-	*381 487*	2
Revaluation reserve:	951 546	-4 478	-	-	-	947 068	3
- including unrealised gains on debt instruments		-	*623 204*	-	-	*623 204*	26a
- including unrealised gains on equity instruments		-	*708 585*	-	-	*708 585*	26a
Current year profit	1 914 711	17 464	-	-1 561 228	-	370 947	5a

Table 1

As at 31 December 2014, the total own funds of the Bank Zachodni WBK Group amounted to **PLN 13,044,924k.**

The amounts and nature of their specific items is presented in Table 2. The disclosure uses the template presented in Annex 6 to article 5 of Commission Implementing Regulation (EU) No 1423/2013, which states the disclosure requirement of own funds items during the transitional period. The table is limited to lines relevant for Bank Zachodni WBK Group.

References in the last column of Table 1 allow the mapping between individual elements of own funds with balance sheet items used for their calculation.

The nature and amounts of specific items on own funds of Bank Zachodni WBK Group during the interim period - as at 31.12.2014(Disclosure according to Article 5 of Commission Implementing Regulation (EU) No 1423/2013) – in PLN k

		(A) AMOUNT AT DISCLOSURE DATE	(B) REGULATION (EU) No 575/2013 ARTICLE REFERENCE	(C) AMOUNTS SUBJECT TO PRE-REGULATION (EU) No 575/2013 TREATMENT OR PRESCRIBED RESIDUAL AMOUNT OF REGULATION (EU) 575/2013
Common Equity Tier 1 capital: instruments and reserves				
1	Capital instruments and the related share premium accounts	8 027 769	26 (1), 27, 28, 29, EBA list 26 (3)	-
	of which: shares	8 027 769	EBA list 26 (3)	-
2	Retained earnings	381 486	26 (1) (c)	-
3	Accumulated other comprehensive income (and any other reserves)	5 873 832	26 (1)	-
3a	Funds for general banking risk	649 810	26 (1) (f)	-
5	Minority interests (amount allowed in consolidated CET1)	728 472	84, 479, 480	-
5a	Independently reviewed interim profits net of any foreseeable charge or dividend	370 947	26 (2)	-
6	**Common Equity Tier 1 (CET1) capital before regulatory**	**16 032 316**		-
Common Equity Tier 1 (CET1) capital: regulatory adjustments				
7	Additional value adjustments (negative amount)	-13 649	34, 105	-
8	Intangible assets (net of related tax liability) (negative amount)	-2 092 223	36 (1) (b), 37, 472 (4)	-
26a	Regulatory adjustments relating to unrealised gains and losses pursuant to Articles 467 and 468	-1 331 789		-
	of which: filter for unrealised gains on debt instruments	*-623 204*	*468*	-
	of which: filter for unrealised gains on equity instruments	*-708 585*	*468*	-
28	**Total regulatory adjustments to Common Equity Tier 1 (CET1)**	**-3 437 661**		-
29	**Common Equity Tier 1 (CET1) capital**	**12 594 655**		-
Additional Tier 1 (AT1) capital: instruments				
36	**Additional Tier 1 (AT1) capital before regulatory adjustments**	**-**		-
Additional Tier 1 (AT1) capital: regulatory adjustments				
43	**Total regulatory adjustments to Additional Tier 1 (AT1) capital**			-
44	**Additional Tier 1 (AT1) capital**			-
45	**Tier 1 capital (T1 = CET1 + AT1)**	**12 594 655**		-
Tier 2 (T2) capital: instruments and provisions				
46	Capital instruments and the related share premium accounts	421 968	62, 63	-
48	Qualifying own funds instruments included in consolidated T2 capital (including minority interest and AT1 instruments not included in rows 5 or 34) issued by subsidiaries and held by third party	28 301	87, 88, 480	-
51	**Tier 2 (T2) capital before regulatory adjustment**	**450 269**		-
Tier 2 (T2) capital: regulatory adjustments				
57	**Total regulatory adjustments to Tier 2 (T2) capital**	**-**		-
58	**Tier 2 (T2) capital**	**450 269**		-
59	**Total capital (TC = T1 + T2)**	**13 044 923**		-
59a	Risk weighted assets in respect of amounts subject to pre-CRR treatment and transitional treatments subject to phase out as prescribed in Regulation (EU) No 575/2013 (i.e. CRR residual amount)	3 348 797		-
60	**Total risk-weighted assets**	**101 016 091**		-
Capital ratios and buffers				-
61	Common Equity Tier 1 (as a percentage of total risk exposure amount	12,5%	92 (2) (a), 465	-
62	Tier 1 (as a percentage of total risk exposure amount	12,5%	92 (2) (b), 465	-
63	Total capital (as a percentage of total risk exposure amount	12,9%	92 (2) (c)	-
64	Institution specific buffer requirement (CET1 requirement in accordance with article 92 (1) (a) plus capital conservation and countercyclical buffer requirements plus a systemic risk buffer, plus systemically important institution buffer expressed as a percentage of total risk exposure amount)	9,00%	CRD 128, 129, 140	-
Amounts below the thresholds for deduction (before risk-weighting)				-
73	Direct and indirect holdings of the CET1 instruments of financial sector entities where the institution has a significant investment in those entities (amount below 10% threshold and net of eligible short positions	49 400	36 (1) (i), 45, 48, 470, 472 (11)	-
75	Deferred tax assets arising from temporary difference (amount below 10 % threshold , net of related tax liability where the conditions in Article 38 (3) are met)	1 290 119	36 (1) (c), 38, 48, 470, 472 (5)	-

Table 2

3.1. Tier I

Common Eqiuty Tier I

Share capital is stated in the nominal amount as shown in the Statutes and in the entry to the Court Register. The nominal value of a share is PLN 10. All the issued shares are fully paid-up. As at 31 December 2014, the share capital was **PLN 992,345k**. Details of the instruments are presented in Table 3.

Supplementary capital is created from profit allocations and from share premium. By the Bank's Statutes, the supplementary capital is created from net profit allocations. Its purpose is to cover any balance sheet losses. The value of the allocations is determined by the General Meeting of Shareholders. As at 31 December 2014, the supplementary capital in own funds was **PLN 7,416,911k**. incl. share premium of PLN 7,035,424k.

Reserve capital is created from net profit allocations in an amount approved by the General Meeting of Shareholders. Reserve capital is used to cover balance sheet losses if they are greater than the supplementary capital. The decision to resort to the reserve capital is taken by the General Meeting of Shareholders. As at 31 December 2014, after including prudential consolidation adjustments, the reserve capital in own funds was **PLN 4,926,764k.**

General risk fund for unidentified banking business risk is created from net profit allocations in an amount approved by the General Meeting of Shareholders. The general risk fund is used to cover costs and losses connected with unidentified banking risks that were not separately provided for. As at 31 December 2014, the general risk fund earmarked for unidentified risks of the banking business was **PLN 649,810k.**

Net profit of Bank Zachodni WBK Group for year 2014 totaled PLN 2,047,292k, including PLN 132,581k of profit attributable to shareholders who do not exercise control. As at 31.12.2014, according to article 26 CRR and based on the consent received from Polish Financial Supervision Authority, Bank Zachodni WBK included the amount of **PLN 370,947k** of current year profit on own funds elements.

Minority interests

Consolidated own funds reflects minority interests in Tier I capital in the amount of **PLN 728,472k.**

Compared to 2013, minority interest are no longer included in own funds based on the balance sheet value, but are calculated according to article 86-87 of CRR. CRR provisions also define new requirements in relation to a subsidiary that can be taken into account in the calculation of minority interests. On that basis, insurance subsidiaries BZ WBK-Aviva TUO and BZ WBK-Aviva TU are excluded from regulatory minority interest calculation.

Adjustment and deductions from Common Equity Tier I

Bank Zachodni WBK Group has calculated the additional value adjustments due to the requirements for prudent valuation according to articles 14 and 105 of CRR. It amounted to PLN **(13 649)k**.

Adjustment due to goodwill amounted to **PLN (1,688,516)k**, and after including the associated deferred tax liabilities, the net adjustment was **PLN (1,656,117)k**. The goodwill arising on the merger with Kredyt Bank, represents a control premium, and arises from the possibility to generate additional benefits from the expected synergies, increase in revenues, achieved market share, combination of staff competencies and an increase in the effectiveness of processes, all of which is an excess over the fair value of the acquired assets.

As at 31 December 2014, deduction from Tier I regarding other intangible assets amounted to **PLN (436,106)k.**

Unrealised gains related to assets or liabilities measured at fair value and recognised in balance sheet are excluded from own funds in the transitional period. In 2014, the Group deducted 100% of gains in the amount of **PLN (1,331,789)k**. Breakdown between debt and equity instruments is presented in Table 2.

Unrealised losses related to assets or liabilities measured at fair value and recognised in balance in sheet were fully excluded from Tier I capital according to Article 467(3).

3.2. Tier II

Subordinated liabilities

Until 31 December 2013, liabilities arising from registered bonds bearing a floating interest rate (fully taken up and paid for by the EBRD), were recognised in own funds under the Banking Law Act and KNF approval dd. 13 October 2010 in the amount of EUR 99m.

These items meet CRR requirements regarding eligible elements of Tier II capital and continue to be taken into account in the calculations of Bank Zachodni WBK Group's capital ratio. They will be depreciated using a straight-line method during the final 5 years of maturity according to art. 64 CRR.

As at 31.12.2014, under Art. 490(5) of CRR, the bank excluded from own funds subordinated liabilities to KBC NV.

Hence, as at 31 December 2014, own funds include subordinated liabilities of **PLN 421,968k.**

Subordinated liabilities of the Bank Zachodni WBK Group eligible as Tier II capital as at 31 December 2014 (PLN k)

Entity	Nominal value [k]	Currency	Amount included in own funds [k]	Redemption date	Start date of amortization	Subordinated liabilities included in own funds [PLN k]
European Bank for Reconstruction and Development	100 000	EUR	99 000 EUR	05.08.2020	05.08.2015	421 968
						421 968

Instruments issued by subsidiaries that recognised in Tier II capital

As in 2014 the bank took over control over Santander Consumer Bank S.A., the entity's eligible own funds were recognised in the Group's Tier 2 capital in accordance with Article 87- 88 of CRR.

More details about the subordinated liabilities are presented in **Note 33** to the Consolidated Financial Statements of the Bank Zachodni WBK Group for 2014.

Detailed description of capital instruments' main features is presented in Table 3.

Description of main features of Common Equity Tier I and Tier II instruments of Bank Zachodni WBK S.A. (Disclosure according to Article 3 Commission Implementing Regulation (EU) No 1423/2013)

	Capital instruments' main features		
1	Issuer	Bank Zachodni WBK S.A.	Bank Zachodni WBK S.A.
2	Unique identifier (eg CUSIP, ISIN or Bloomberg identifier for private placement	PLBZ00000044	XS0531310182
3	Governing law(s) of the instrument	polish	english/polish
	Regulatory treatment		
4	Transitional CRR rules	Common Equity Tier I	Tier II
5	Post-transitional CRR rules	Common Equity Tier I	Tier II
6	Eligible at solo/(sub-)consolidated/solo & (sub-)consolidated	solo and consolidated	solo and consolidated
7	Instrument type (types to be specified by each jurisdiction)	shares - Common Eqiuty Tier I as published in Regulation (EU) No 575/2013 article 28	Tier II as published in Regulation (EU) No 575/2013 article 63
8	Amount recognised in regulatory capital (currency in million, as of most recent reporting date)	PLN 992,345 m	PLN 421,97 m
9	Nominal amount of instrument	10 PLN	50 000 EUR
9a	Issue price	Series A: 10 PLN Series B: 10 PLN Series C: 10 PLN Series D: 102 PLN Series E: 102 PLN Series F: 40 PLN Series G: 10 PLN Series H: 10 PLN Series I: 212.60 PLN Series J: "Share Exchange Ratio" re. the merger of BZ WBK with Kredyt Bank, pursuant to Resoliution no. 2 of the Extraordinary Meeting of BZ WBK Shareholders, dd. 30.07.2012 r. Series K: 10 PLN Series L: 400.53 PLN	100% of nominal value
9b	Redemption price	N/A	100% of nominal value
10	Accounting classification	Shareholders' equity	Liability - amortised cost
11	Original date of issuance	Series A: 08.11.1991 Series B: 21.12.1996 Series C: 31.12.1996 Series D: 25.10.1999 Series E: 17.05.2000 Series F: 30.11.2000 Series G: 13.06.2001 Series H: 10.07.2009 Series I: 09.08.2012 Series J: 04.01.2013 Series K: 11.07.2014 Series L: 18.07.2014	05.08.2010
12	Perpetual or dated	N/A	Dated
13	Original maturity date	No maturity	05-08-2020
14	Issuer call subjet to prior supervisory approval	N/A	Yes
15	Optional call date, contingent call dates, and redemption amount	N/A	N/A
16	Subsequent call dates, if applicable	N/A	N/A
	Coupons / dividends		
17	Fixed or floating dividend/coupon	Floating	Floating
18	Coupon rate and any related index	N/A	rate 3.8% per annum above three-month EURIBOR for each interest period
19	Existence of a dividend stopper	No	Yes
20a	Fully discretionary, partially discretionary or mandatory (in terms of timing	Fully discretionary	Mandatory
20b	Fully discretionary, partially discretionary or mandatory (in terms of amount)	Fully discretionary	Mandatory
21	Existence of step up or other incentive to redeem	N/A	No
22	Noncumulative or cumulative	Noncumulative	Cumulative
23	Convertible or non-convertible	Nonconvertible	Nonconvertible
24	If convertible, conversion trigger (s)	N/A	N/A
25	If convertible, fully or partially	N/A	N/A
26	If convertible, conversion rate	N/A	N/A
27	If convertible, mandatory or optional conversion	N/A	N/A
28	If convertible, specifiy instrument type convertible into	N/A	N/A
29	If convertible, specifiy issuer of instrument it converts into	N/A	N/A
30	Write-down features	No	No
31	If write-down, write-down trigger (s)	N/A	N/A
32	If write-down, full or partial	N/A	N/A
33	If write-down, permanent or temporary	N/A	N/A
34	If temporary write-down, description of write-up mechanism	N/A	N/A
35	Position in subordination hierachy in liquidation (specify instrument type immediately senior to instrument)	N/A	the lowest priority of satisfaction and will rank only to the extent permitted by applicable laws raelating to creditors' right
36	Non-compliant transitioned features	No	No
37	If yes, specifiy non-compliant features	N/A	N/A

Table 3

*'N/A' not applicable

Bank Zachodni WBK
Grupa Santander

4. Capital requirements

The capital requirements of Bank Zachodni WBK Group are set in accordance with part III 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 was the official legal basis as at 31 December 2014.

In 2014, Bank Zachodni WBK applied the standardised approach to the calculation of capital requirement for credit, market and operational risk. Under this approach the total capital requirement for credit risk is calculated as a sum of risk-weighted assets multiplied by 8%. To calculate risk-weighted exposures, risk weights are allocated to all exposures in accordance with the CRR. The Group measures its balance sheet assets and liabilities in accordance with International Accounting Standards and International Financial Reporting Standards.

The Bank calculates and monitors capital requirements for all key risks, including:

- capital requirement for credit risk
- capital requirement for market risk, including:
  - capital requirement for positions risk, including:
    - specific and general risk of debt instruments
    - specific and general risk of equity instruments
  - capital requirement for FX risk
- capital requirement for the settlement, supplier and counterparty risk
- capital requirement for credit valuation adjustments
- capital requirement for the excess of large exposures limit
- capital requirement for the excess of capital concentration limit
- capital requirement for operational risk.

Bank Zachodni WBK Group calculates capital requirement separately for the exposures classified into the banking and trading book.

4.1. Capital requirements for individual risk types

As at 31 December 2014, the total capital requirements of Bank Zachodni WBK Group calculated in line with the CRR was **PLN 8 082 444k**, including:

- for credit risk and counterparty credit risk: **PLN 6 956 272k**
- for market risk: **PLN 84 493k**
- for credit valuation adjustment risk: **PLN 101 862k**
- for operational risk: **PLN 939 817k.**

The increase in capital requirements as at 31 December 2014 compared with the previous year was driven by the incorporation of Santander Consumer Bank (with its subsidiaries) into Bank Zachodni WBK Group in Q3 2014.

The table below presents a specification of capital requirements for different risks.

Capital requirements of the Bank Zachodni WBK Group
as at 31 December 2014 (PLN k)

No.	CAPITAL REQUIREMENTS FOR INDIVIDUAL RISK TYPES	as at 31.12.2014
1.	Credit risk and Counterparty risk	6 956 272
2.	Risk of exceeding the exposure concentration limit and the large exposure limit	-
3.	Market risk including:	84 493
3.1	FX risk	-
3.2	commodity prices risk	-
3.3	risk of positions of equity instruments, including: :	6 828
3.3.1	specific risk	6 033
3.3.2	general risk	110
3.3.3	Specific approach to the risk of positions in collective investment undertakings (CIUs)	685
3.4	risk of debt instrument positions, including:	77 665
3.4.1	specific risk	129
3.4.2	general risk	77 536
4.	Supply settlement risk	-
5.	Credit valuation adjustment risk	101 862
6.	Operational risk	939 817
	TOTAL CAPITAL REQUIREMENT (items 1+2+3+4+5+6+7)	**8 082 444**

The biggest item is the total capital requirement of Bank Zachodni WBK Group is the capital requirement for credit risk, including counterparty credit risk, which on 31 December 2014 accounted for **86.07%** of the total capital requirement. Bank Zachodni WBK Group manages credit risk on a priority basis, using its internal rating systems, credit concentration limits and sectoral exposure limits, seeking to maintain the possible highest quality of the credit portfolio.

The table below present a specification of the capital requirement for credit risk and counterparty credit risk by exposure classes, in accordance with the CRR.

Capital requirement of Bank Zachodni WBK Group for credit risk and counterparty credit risk
as at 31.12.2014 (PLN k)

No.	Exposure Class	Capital requirement for credit risk and counterparty risk
1.	Exposures to central governments or central banks	7 797
2.	Exposures to regional governments or local authorities	2 795
3.	Exposures to public sector entities	8 009
4.	Exposures to multilateral development banks	0
5.	Exposures to institutions bank	186 723
6.	Exposures to corporates	1 653 967
7.	Retail exposures	1 731 249
8.	Exposures secured by mortgages on immovable property	2 596 369
9.	Exposures in default	314 103
10.	Exposures associated with particularly high risk	5 121
11.	Exposures in the form of units or shares in collective investment undertakings	51
12.	Equity exposures	78 029
13.	Other items	372 059
	Total exposures covered by the standardised approach	**6 956 272**

4.2. Exposure structure

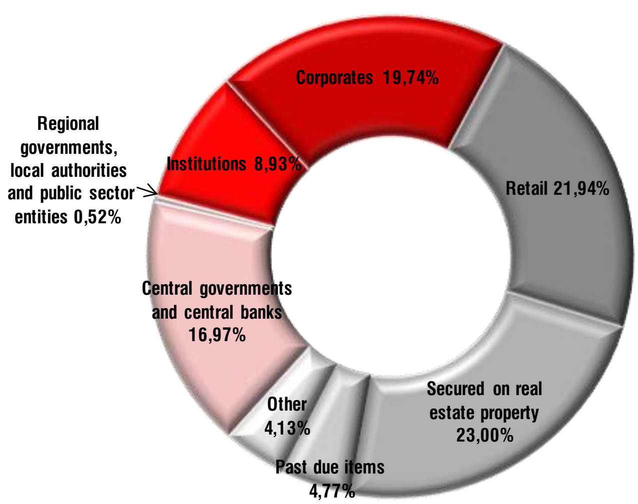
In the process of capital adequacy assessment, each type of exposure was classified in accordance with Article 112 of the CRR.

The original exposure before conversion factors represents the value of the exposure exclusive of value and provisioning adjustments, conversion factors and credit risk mitigation techniques.

Credit risk and counterparty credit risk exposures as at 31.12.2014 (PLN k)

No.	Exposure Class	Exposure Value	Average value of the exposure
1.	Exposures to central governments or central banks	28 031 090	24 761 871
2.	Exposures to regional governments or local authorities	241 712	284 693
3.	Exposures to public sector entities	611 870	490 916
4.	Exposures to multilateral development banks	-	-
5.	Exposures to institutions bank	14 753 430	15 813 796
6.	Exposures to corporates	32 608 794	31 733 405
7.	Retail exposures	36 244 008	33 677 426
8.	Exposures secured by mortgages on immovable property	37 992 676	38 131 099
9.	Exposures in default	7 880 085	7 486 772
10.	Exposures associated with particularly high risk	42 671	29 670
11.	Exposures in the form of units or shares in collective investment undertakings	640	15 388
12.	Equity exposures	901 257	891 111
13.	Other items	5 877 314	5 972 164
	Total exposures covered by the standardised approach	**165 185 547**	**159 288 311**

Percentage structure of exposures by different asset classes in 2014



The structure of balance sheet and off-balance sheet exposures of the Bank Zachodni WBK Group by maturity is presented below. Exposures with residual maturity between 1-5 years represent the bulk of the exposures.

Credit risk and counterparty credit risk exposures by maturities as at 31.12.2014 (PLN k)

No.	Exposure Class	Residual Term to Maturity				
		<1 year	1-5 years	>5 years	without residual term to maturity	Total
1.	Exposures to central governments or central banks	23,26%	45,90%	31,84%	-	28 031 090
2.	Exposures to regional governments or local authorities	9,56%	62,36%	28,08%	-	241 712
3.	Exposures to public sector entities	91,82%	7,69%	0,49%	-	611 870
4.	Exposures to multilateral development banks	0,00%	0,00%	0,00%		-
5.	Exposures to institutions bank	53,67%	29,76%	16,57%	-	14 753 430
6.	Exposures to corporates	22,82%	65,07%	12,11%	-	32 608 794
7.	Retail exposures	18,22%	52,28%	29,50%	-	36 244 008
8.	Exposures secured by mortgages on immovable property	7,04%	23,58%	69,38%	-	37 992 676
9.	Exposures in default	71,67%	21,96%	6,37%	-	7 880 085
10.	Other exposure classes	-	-	-	100,00%	6 821 882
	Total exposures covered by the standardised approach	**22,47%**	**41,35%**	**32,05%**	**4,13%**	**165 185 547**

Credit risk concentration

Bank Zachodni WBK complies with the Banking Law requirements with regard to the limits of risk-bearing exposures to a single entity or to a group of connected entities. As at 31.12.2014, the maximum limit for the bank, pursuant to Article 71 of the Banking Law was:

- PLN 3 261 237k (25% of the Group's own funds).

The Group's policy is designed to minimise the exposure concentration risk bthrough its large exposures policy whose provisions are more stringent than the statutory requirements. This ensures that diversification of exposures to individual borrowers is maintained.

The analysis of concentration of exposures performed as at 31.12.2014, showed that the bank did not have any exposures that would exceed the statutory limits.

In line with its credit policy, Bank Zachodni WBK Group issues credit to enterprises from different sectors. Through diversification of its credit portfolio, Bank Zachodni WBK Group reduces the risk arising from excessive credit concentration. As at the end of December 2014, the highest concentration levels were recorded in the production and distribution sectors (excluding the public and retail sectors).

Credit risk and counterparty credit risk exposures by sectors as at 31.12.2014 (PLN k)

No.	Exposure Class	Industry Analysis											
		Public Sector	Detail (including mortgages)	Property	Manuafacturing	Distribution	Construction	Agriculture	Transport	Financial	Energy	Other Secotrs	Total
1.	Exposures to central governments or central banks	25 603 586	-	-	-	-	-	-	-	-	-	2 427 504	28 031 090
2.	Exposures to regional governments or local authorities	241 712	-	-	-	-	-	-	-	-	-	-	241 712
3.	Exposures to public sector entities	611 870	-	-	-	-	-	-	-	-	-	-	611 870
4.	Exposures to multilateral development banks	-	-	-	-	-	-	-	-	-	-	-	-
5.	Exposures to institutions bank	-	-	-	-	-	-	-	-	14 753 430	-	-	14 753 430
6.	Exposures to corporates	-	-	1 773 825	10 062 541	8 767 204	2 069 904	121 840	620 641	1 521 345	3 845 717	3 825 777	32 608 794
6.1.	of witch SME	-	-	46 620	859 939	1 088 361	235 258	32 935	163 362	14 538	48 777	340 141	2 829 931
7.	Retail exposures	-	26 310 452	128 434	1 831 735	3 029 002	845 814	1 286 456	1 025 896	141 540	64 449	1 580 230	36 244 008
7.1.	of witch SME	-	-	127 617	1 827 642	3 026 375	845 521	1 286 375	1 025 894	141 259	64 415	1 559 935	9 905 033
8.	Exposures secured by mortgages on immovable property	-	23 029 925	6 913 943	2 404 090	3 577 088	187 574	683 646	327 460	135 982	151 731	581 237	37 992 676
8.1.	of witch SME	-	-	107 513	560 897	1 015 633	91 455	356 870	81 230	24 218	43 551	312 821	2 594 188
9.	Exposures in default	24	2 432 485	1 753 512	873 084	912 677	424 612	71 898	140 366	26 380	762 615	482 432	7 880 085
10.	Exposures associated with particularly high risk	-	-	-	-	-	-	-	-	-	-	42 671	42 671
11.	Exposures in the form of units or shares in collective investment undertakings	-	-	-	-	-	-	-	-	-	-	640	640
12.	Equity exposures	-	-	-	-	-	-	-	-	1 602	-	899 655	901 257
13.	Other items	-	-	-	-	-	-	-	-	-	-	5 877 314	5 877 314
	Total exposures covered by the standardised approach	**26 457 192**	**51 772 862**	**10 569 714**	**15 171 450**	**16 285 971**	**3 527 904**	**2 163 840**	**2 114 363**	**16 580 279**	**4 824 512**	**15 717 460**	**165 185 547**

Credit risk and counterparty credit risk exposures by countries as at 31.12.2014 (PLN k)

No.	Exposure Class	Geographic distribution*												
		Poland	Belgium	United Kingdom	Luxembourg	Spain	France	Germany	Austria	Finland	Norway	Netherlands	Other countries	Total
1.	Exposures to central governments or central banks	28 009 439	-	-	-	-	-	21 651	-	-	-	-	-	28 031 090
2.	Exposures to regional governments or local authorities	241 712	-	-	-	-	-	-	-	-	-	-	-	241 712
3.	Exposures to public sector entities	611 870	-	-	-	-	-	-	-	-	-	-	-	611 870
4.	Exposures to multilateral development banks	-	-	-	-	-	-	-	-	-	-	-	-	-
5.	Exposures to institutions bank	7 395 587	3 542 752	1 358 350	-	637 813	702 659	170 869	226 002	182 011	168 698	29 043	339 646	14 753 430
6.	Exposures to corporates	31 488 287	1	260 410	428 570	35 292	1	95 517	-	-	-	130 821	169 895	32 608 794
7.	Retail exposures	36 226 053	60	4 622	-	1 608	346	998	94	-	1	105	10 121	36 244 008
8.	Exposures secured by mortgages on immovable property	37 540 399	747	36 624	290 376	5 527	1 640	4 980	1 749	-	-	1 669	108 965	37 992 676
9.	Exposures in default	7 840 847	8	4 557	2	8	73	592	264	-	1	7	33 726	7 880 085
10.	Exposures associated with particularly high risk	42 671	-	-	-	-	-	-	-	-	-	-	-	42 671
11.	Exposures in the form of units or shares in collective investment undertakings	640	-	-	-	-	-	-	-	-	-	-	-	640
12.	Equity exposures	901 257	-	-	-	-	-	-	-	-	-	-	-	901 257
13.	Other items	5 877 314	-	-	-	-	-	-	-	-	-	-	-	5 877 314
	Total exposures covered by the standardised approach	**156 176 076**	**3 543 568**	**1 664 563**	**718 948**	**680 248**	**704 719**	**294 607**	**228 109**	**182 011**	**168 700**	**161 645**	**662 353**	**165 185 547**

* Distribution by the country of the borrower

Delinquent and impaired positions

An exposure is considered as delinquent if the obligor is in arrears with capital and/or interest payments. In such circumstances, the entire exposure is considered as delinquent, regardless of whether or not the payment delay relates to the whole exposure or a part thereof.

An exposure is considered as impaired, if the Group has objective evidence that it will not be able to recover the exposure in accordance with the underlying credit agreement. Objective indications of impairment were defined in accordance with recommendations of the Basel Committee and the International Accounting Standards(IAS 39) and Recommendation R.

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

Twice a year, to facilitate proper calculation of impairment, the Group compares the assumptions and parameters used for impairment calculations with the actual situation, taking into account changes of economic conditions, modifications in the Group's credit policies and recovery strategies to ensure adequacy of provisions. The responsibility for ensuring adequacy of the impairment charges rests with the Provisions Committee.

Pursuant to Commission Delegated Regulation (EU) No 183/2014 (supplementing Regulation (EU) No 575/2013 of the European Parliament and of the Council on prudential requirements for credit institutions and investment firms, with regard to regulatory technical standards for specifying the calculation of specific and general credit risk adjustments), in calculation of its capital adequacy the bank takes into account specific and general credit risk adjustments by which the bank's Common Equity Tier 1 capital has been reduced in order to reflect losses exclusively related to credit risk according to the applicable accounting framework and recognised as such in the profit or loss account, irrespective of whether they result from impairments, value adjustments or provisions for off-balance sheet items. After an independent overview of the financial statements as at 30 June 2014. and obtaining the necessary approval of the Bank included part of the profit of the current period in the amount of PLN 947,370k own funds. Accordingly, included in this report adjustments for specific and general credit risk are consistent with the date indicated above.

Impaired and delinquent exposures by industries as at 31.12.2014 (PLN k)

Industry structure	Impaired Original Exposures	Overdue original exposures	Adjustment for specific and general credit risk	including: for impaired exposures
Public sector	24	166	1 280	18
Retail (including mortgages)	2 432 485	5 691 076	2 519 944	1 823 218
Facilities management	1 753 512	1 567 128	678 457	633 364
Production sector	873 084	781 988	455 845	422 973
Distribution	912 677	822 565	480 806	426 790
Construction	424 612	398 577	295 736	286 048
Farming sector	71 898	242 597	59 307	46 479
Transport	140 366	256 959	104 210	93 168
Financial sector	26 380	53 236	18 147	15 513
Energy sector	762 615	349 746	300 493	295 230
Other sectors	482 432	744 755	973 505	600 911
Total	**7 880 085**	**10 908 793**	**5 887 730**	**4 643 712**

Impaired and delinquent exposures by countries as at 31.12.2014 (PLN k)

Country	Impaired Original Exposures	Overdue original exposures	Adjustment for specific and general credit risk	including: for impaired exposures
Poland	7 840 846	10 761 593	5 862 986	4 621 724
Italy	99	50 104	72	71
Ireland	15 015	37 937	12 062	10 944
China	13	17 679	3	2
Liechtenstein	16 269	16 269	8 077	8 077
UK	4 557	11 160	1 627	1 393
Spain	8	4 142	188	1
Austria	264	2 013	293	178
Germany	592	2 025	345	315
Sweden	1 472	1 476	609	608
Other	950	4 395	1 468	399
Total	**7 880 085**	**10 908 793**	**5 887 730**	**4 643 712**

Reconciliation of changes to adjustments for impaired exposures as at 31.12.2014 (PLN k)

As at 31.12.2013	Provision charge	Claw-backs and adjustments	As at 31.12.2014
3 103 444	897 035	643 233*	4 643 712

* significantly influenced by the acquisition of SCB in H2 2014

**when calculating the exposure, the Bank takes into account only the amount of adjustments for general and specific credit risk, which were used to reduce Tier I capital in order to reflect losses exclusively related to credit risk according to the applicable accounting framework and recognised as such in the profit or loss account, irrespective of whether they result from impairment, value adjustments or provisions for off-balance sheet items.

4.3. Allocating risk weights to the credit portfolio

The risk weights used in the calculation of capital requirement for credit risk in the standardised approach are based on the provision of Chapter 2, Title II, Part III of the CRR. Risk weights are allocated in line with the category of the exposure and the credit quality of the exposure/entity.

The Group uses credit risk mitigation techniques both for funded credit protection and for unfunded credit protection. In the latter case, borrowers protected by guarantees are allocated a risk grade that corresponds to the risk grade of the guarantor. Most providers of unfunded credit protection are banks, including Bank Gospodarstwa Krajowego (with its “de minimis” guarantee programme) and the Ministry of Finance as a State unit.

Defaulted exposures have their risk weight allocated in accordance with the rules laid down in Article 127(1)of the CRR.

The Group has identified retail exposures that are fully secured on residential properties, applying a preferential risk weight of 35% to them (in accordance with Article 125(1) of the CRR). Bank Zachodni WBK has not identified exposures effectively secured by mortgage on a commercial property, to which preferential risk weights are applied in accordance with Article 126.

As at 31 December 2014, the Group’s debt instruments portfolio included **PLN 2 216 850k** worth of bonds of Bank Gospodarstwa Krajowego, which were fully guaranteed by the State Treasury. They were allocated a preferential risk weight of 0%.

A part of the portfolio of loans issued to SMEs under the “de minimis” guarantee programme, in an amount not exceeding 60% of the loan sanctioned, was allocated a preferential risk weight used for Bank Gospodarstwa Krajowego.

Credit risk and counterparty credit risk exposures
by type of collateral
as at 31.12.2014 (PLN k)

No.	Exposure Class	Exposures secured by guarantees
1.	Exposures to central governments or central banks	-
2.	Exposures to regional governments or local authorities	-
3.	Exposures to public sector entities	-
4.	Exposures to multilateral development banks	-
5.	Exposures to institutions bank	2 216 850
6.	Exposures to corporates	172 326
7.	Retail exposures	854 162
8.	Exposures secured by mortgages on immovable property	-
9.	Exposures in default	8 778
10.	Exposures associated with particularly high risk	-
11.	Exposures in the form of units or shares in collective investment undertakings	-
12.	Equity exposures	-
13.	Other items	-
	Total exposures covered by the standardised approach	**3 252 116**

In each asset class, appropriate risk weight is allocated depending on the available credit rating of external rating institutions or export credit agencies. The Bank accepts ratings of the following agencies:

- Fitch Ratings;
- Moody's Investors Service;
- Standard and Poor's Ratings Services.

If two credit ratings are available for an exposure and the ratings are linked to different risk weight of the particular exposure, the Bank uses the higher risk weight. If for an exposure 3 or more credit ratings are available, the Bank uses two ratings with the lowest risk weights and if the two are different, the higher risk weight is applied.

Credit risk and counterparty credit risk exposures
by risk weights
as at 31.12.2014 (PLN k)

No.	Exposure Class	Risk Weightings								
		0%	20%	35%	50%	75%	100%	150%	250%	Total
1.	Exposures to central governments or central banks	27 543 770	487 320	-	-	-	-	-	-	28 031 090
2.	Exposures to regional governments or local authorities	-	241 453	-	259	-	-	-	-	241 712
3.	Exposures to public sector entities	-	546 079	-	65 791	-	-	-	-	611 870
4.	Exposures to multilateral development banks	-	-	-	-	-	-	-	-	-
5.	Exposures to institutions bank	8 384 257	2 730 675	-	3 606 589	-	28 996	2 913	-	14 753 430
6.	Exposures to corporates	326 053	-	-	-	-	32 150 117	132 624	-	32 608 794
7.	Retail exposures	854 162	-	-	-	35 389 846	-	-	-	36 244 008
8.	Exposures secured by mortgages on immovable property	-	-	6 628 108	-	-	31 364 568	-	-	37 992 676
9.	Exposures in default	8 636	142	-	-	-	5 902 226	1 969 081	-	7 880 085
10.	Exposures associated with particularly high risk	-	-	-	-	-	-	42 671	-	42 671
11.	Exposures in the form of units or shares in collective investment undertakings	-	-	-	-	-	640	-	-	640
12.	Equity exposures	-	-	-	-	-	851 857	-	49 400	901 257
13.	Other items	2 677 470	456 910	-	-	-	1 452 815	-	1 290 119	5 877 314
	Total exposures covered by the standardised approach	**39 794 348**	**4 462 579**	**6 628 108**	**3 672 639**	**35 389 846**	**71 751 219**	**2 147 289**	**1 339 519**	**165 185 547**

There are not many companies on the Polish market which have a credit rating from the agencies listed above. As a result, 77.02% of the exposures presented below do not have a credit quality rating.

Credit risk and counterparty credit risk exposures by credit rating as at 31.12.2014 in PLN thousand

No.	Exposure Class	Credit quality step							
		1	2	3	4	5	6	Lack	Total
1.	Exposures to central governments or central banks	-	25 603 586	-	-	-	-	2 427 504	28 031 090
2.	Exposures to regional governments or local authorities	-	241 712	-	-	-	-	-	241 712
3.	Exposures to public sector entities	-	611 870	-	-	-	-	-	611 870
4.	Exposures to multilateral development banks								
5.	Exposures to institutions bank	775 643	11 591 386	2 152 079	189 744	1 405	2 913	40 260	14 753 430
6.	Exposures to corporates	-	172 326	3 080 157	-	332 623	1	29 023 687	32 608 794
7.	Retail exposures	-	854 162	-	-	-	-	35 389 846	36 244 008
8.	Exposures secured by mortgages on immovable property	-	-	-	189 024	-	-	37 803 652	37 992 676
9.	Exposures in default	142	8 660	-	250 297	-	-	7 620 986	7 880 085
10.	Exposures associated with particularly high risk	-	-	-	-	-	-	42 671	42 671
11.	Exposures in the form of units or shares in collective investment undertakings	-	-	-	-	-	-	640	640
12.	Equity exposures	-	-	-	-	-	-	901 257	901 257
13.	Other items	-	-	-	-	-	-	5 877 314	5 877 314
	Total exposures covered by the standardised approach	**775 785**	**39 083 702**	**5 232 236**	**629 065**	**334 028**	**2 914**	**119 127 817**	**165 185 547**

Bank Zachodni WBK
Grupa Santander

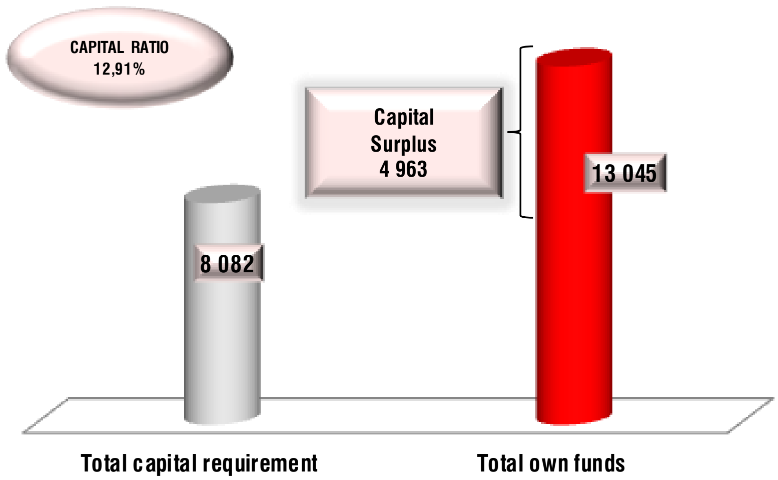
5. Capital adequacy

5.1 Regulatory capital adequacy

Pursuant of Article 92 of CRR, total capital ratio is determined on the basis of own funds and total capital requirements multiplied by 12.5.

Taking into account total capital requirements of **PLN 8 082 444k** as at 31 December 2014 and own funds of **PLN 13 044 924k**, the capital ratio of Bank Zachodni WBK Group is **12.91%.**

Capital adequacy of Bank Zachodni WBK Group as at 31.12 2014 in PLNm



5.2 Internal capital adequacy

Introduction

It is the policy of the Bank Zachodni WBK Group to maintain the level of capital adequate to the type and scale of operations and the level of risk. The level of own funds required to ensure safe operations of Bank Zachodni WBK Group and capital requirements estimated for the unexpected loss is determined in accordance with the CRD IV / CRR package plus KNF recommendations regarding stricter criteria for mortgage-backed exposures.

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

The Management Board delegated on-going capital management to Capital Committee. Capital Committee conducts regular assessment of capital adequacy of the Bank and the Group, also in extreme conditions, monitors the actual and required capital levels and initiates transactions affecting these levels (e.g. by recommending the value of dividends to be paid).

The Credit Committee is the first body in the bank to define capital policy and rules for assessment of capital adequacy both for the Bank and the Group. It also approves capital plans and sets out rules underpinning allocation of capital into individual segments when estimating profitability of the same. However, any ultimate decisions regarding increase or decrease of capital are taken by relevant authorities of the bank and subsidiaries in accordance with the applicable law and the Bank's Statutes.

Capital Policy

The Group's capital management policy envisages the minimum level of solvency ratio at 12% both for the bank and the Group(calculated according to applicable regulations and directives of the European Parliament and European Council).

At the same time Tier 1 capital ratio (CET1 capital to Risk Weighted Assets for credit, market and operational risk) should be maintained at a minimum level of 9% both for the Bank and the Group.

The regulatory solvency ratio is 8%.

Regulatory Capital

The capital requirement for **Bank Zachodni** WBK Group as at 31.12.2014 was determined in accordance with Regulation no. 575/2013 of the European Parliament and the Council of 26 June 2013 on prudential requirements for credit institutions and investment firms as well as KNF recommendation on stricter criteria for mortgage-backed exposures.

The credit risk requirement is the most important among capital requirements.

The value of asset exposure is the carrying value of the asset after adjustments for specific credit risk, additional value adjustments and other own fund deductions related to a particular asset. The off-balance sheet exposure is the percentage of the nominal value less adjustments for specific credit risk.

Internal Capital

Independent from the regulatory methods for measuring capital requirements, Bank Zachodni WBK Group assesses both current and future capital adequacy based on internal methods and models of risk measurement - process (ICAAP).

Under the ICAAP process, the Group estimates the required level of internal capital to ensure secure conduct of its banking business in accordance with the Group’s risk profile defined in the “Risk Appetite Statement”.

For the purpose of the ICAAP process, the Group uses statistical loss estimation models for measurable risks, such as credit risk, market risk or operational risk, and carries out qualitative assessment for other material risks not covered by the model, e.g. reputation risk or compliance risk.

The internal capital is estimated on the basis of risk parameters including the probability of default of Bank Zachodni WBK Group customers (PD - probability of default) and loss given default (LGD: Loss Given Default).

Results of the ICAAP process are an element of assessment of the current and future capital requirements, and are the basis for assessment of risk appetite and the Group’s strategy.

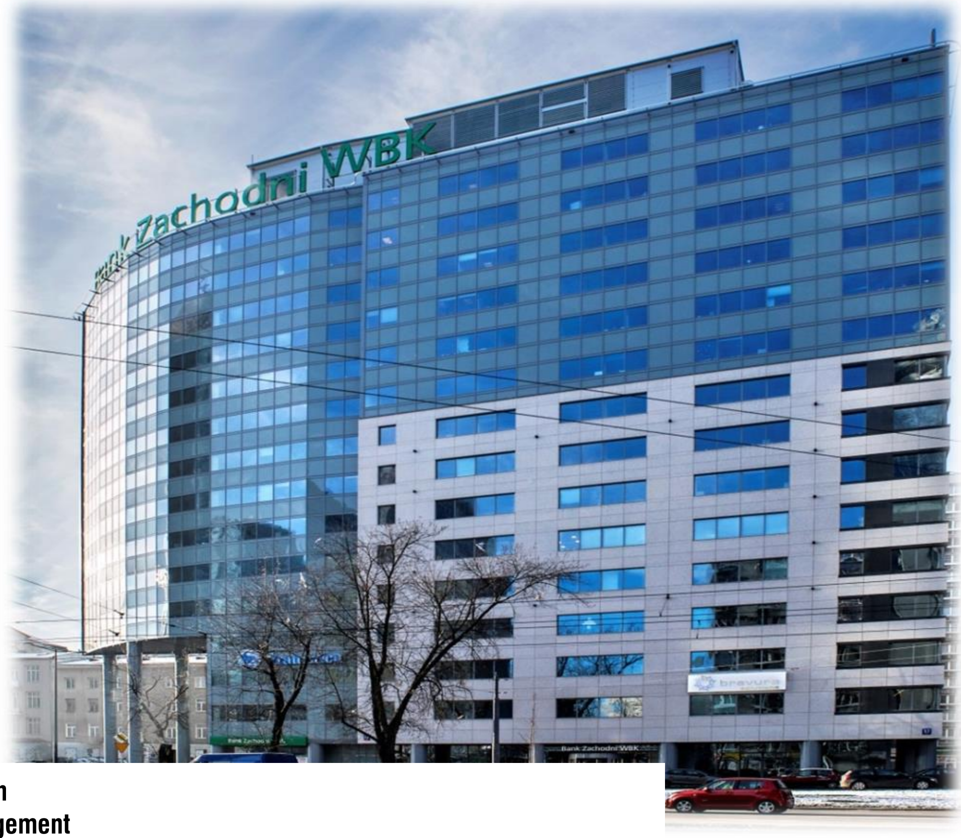
Bank Zachodni WBK Group performs an internal assessment of capital requirements also in stressed conditions, taking into account different macroeconomic scenarios.

The internal capital estimation models are assessed and reviewed annually to adjust them to the scale and profile of the Group's business and to take account of any new risks and the management judgment.

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

Return on assets

As at 31.12.2014, the ROA was 1.6%, calculated as profit attributable to shareholders of the parent for four consecutive quarters to the average value of assets (at the beginning and at the end of the current reporting period).



Bank Zachodni WBK
Grupa Santander

6. Policy of variable components of remuneration

Bank Zachodni WBK Group operates the following policies:

- Policy on variable components of remuneration paid to individuals holding managerial positions in Bank Zachodni WBK Group
- Policy on remuneration for the Management Board Members of Bank Zachodni WBK

The above policies reflect all the statutory requirements relating to the calculation of fixed and variable components of remuneration, criteria for payment of variable remuneration and all components of remuneration in general (fixed and variable components, long-term incentive schemes, etc.)

Bank Zachodni WBK Group has general regulations applicable to all its employees, including those who have a significant influence on the bank's risk profile as well as regulations pertaining specifically to the foregoing individuals.

In addition, the Group operates the **Policy on variable components of remuneration paid to individuals holding managerial positions in Bank Zachodni WBK Group**, which applies to material risk takers, and corresponding regulations in subsidiaries. The policy is reviewed annually or more frequently in the event of major organisational changes.

Decision-making process in determining remuneration policy

Any regulations pertaining to the allocation of variable components of remuneration and applicable to all employees of Bank Zachodni WBK Group are issued by way of an ordinance of the Management Board Member in charge of the Business Partnership Division. The Policy on variable components of remuneration paid to individuals holding managerial positions in Bank Zachodni WBK Group is passed by the Management Board and approved by the Supervisory Board. Resolutions of the Supervisory Board pertain only to fixed and variable remuneration of Management Board members. With regard to other employees, the Remuneration and Nominations Committee reviews the bonus schemes while responsibility for approving the same rests with the Management Board member in chargé of the Business Partnership Division.

The bank has a Remuneration and Nominations Committee of the Supervisory Board, whose role is to i.a. express its opinion on proposed remuneration regulations to be introduced in the bank.

The Remuneration and Nominations Committee supports the Supervisory Board with respect to:

- succession planning for Management Board positions
- preparation of recommendations to the Supervisory Board on matters relating to the membership of the Management Board
- overall monitoring of the market practices and remuneration levels
- preparing recommendations to the Supervisory Board to ensure that the bank's remuneration practices are fair and competitive and provide sufficient motivation for the Management Board members and senior executives.

In 2014, the Remuneration and Nominations Committee met 5 times and took 1 decision by circulation.

From 1 January to 16 April, the members of the Committee were:

- Gerry Byrne – Committee Chairman
- Jose Antonio Alvarez, Jose Luis de Mora - Committee Members.

On 16 April 2014, due to the new term of office of the Supervisory Board, the following individuals were appointed to the Committee:

- Gerry Byrne – Committee Chairman
- Danuta Dąbrowska, Witold Jurcewicz, Jose Luis de Mora, Jerzy Surma - Committee Members.

The three Committee members: Danuta Dąbrowska, Witold Jurcewicz and Jerzy Surma have the status of independent members.

In its remuneration policy, Bank Zachodni WBK Group uses the criteria of identification of the persons that have a significant influence on the bank's risk profile within the meaning of the Commission Delegated Regulation No. 604/2014 of 4 March 2014 supplementing Directive 2013/06/EU of the European Parliament and of the Council with regard to regulatory technical standards with respect to qualitative and appropriate quantitative criteria to identify those categories of staff whose professional activities have a material impact on an institution's risk profile.

Performance-linked remuneration

All Bank employees are included in bonus schemes based on which variable components of remuneration are granted. Every bonus scheme specifies that the launch of the bonus pool as well as its amount depend on meeting particular business targets.

Business targets are linked to the performance of a given area, or the entire Bank in the case of support units. In the case of sales units the performance of individual employees is also taken into account when determining variable remuneration.

Characteristic features of the remuneration system and performance criteria that are the basis of allocation of shares, share options or variable remuneration components

The remuneration system consists of two basic elements – fixed and variable remuneration.

The fixed remuneration depends on the grade of the employee's job role. A pay band is defined for every job grade. The values within the pay band are determined based on the findings of the salary report produced annually by the HAY Group.

Variable remuneration depends on the bonus scheme that applies to a particular employee. Whether the bonus pool is launched in individual bonus schemes depends on meeting certain business targets (PBT or PAT value or dynamics). One of the targets for business units is meeting a defined level of RoRWA (return on risk-weighted assets).

Granting variable remuneration components (including shares and phantom stock) is based on the provisions of regulations to bonus schemes which apply to individual employees.

In the case of job roles characterised by a significant impact on the Bank's risk profile, pursuant to the guidelines of the Polish Financial Supervision Authority (KNF), a policy is applied under which part (not less than 50%) of the variable remuneration is paid out in the form of capital market instruments. In the case of the Bank these are phantom shares. Additionally, not less than 40% of the variable remuneration is deferred for a period of 3 years, while the payment of every deferred part is contingent upon the absence of negative circumstances that would make payment impossible or reduce the amount to be paid out.

Another form of variable remuneration are also the Bank's long-term incentive plans (3-year plans) addressed to key employees. The award in the programme is granted in the form of Bank Zachodni WBK shares (new issue) provided that business requirements defined in the Regulations have been met.

Fixed remuneration components to variable components

The ratio of fixed remuneration components to variable remuneration components depends on the bonus scheme that applies to a given employee, the degree of business targets execution and thus on the amount of the bonus granted, as well as on whether the given employee has been included in the long-term incentive plan. If business targets are not met at the minimum required level, the variable component of remuneration may not be paid at all.

In line with AGM resolution of 16 April 2014, total variable remuneration for a given calendar year for persons whose professional activities have a material impact on the risk profile must not exceed 200% of the fixed remuneration for that calendar year.

Main parameters of the variable remuneration components

When developing the remuneration system, the Bank aimed at making it possible to recruit and retain adequately trained and qualified staff members who would be capable of delivering on all of the Bank's strategic processes.

The result of the above is implementing differentiated bonus schemes addressed to different employee groups, in particular differentiating between sales and support staff. Individual schemes differ in terms of the bonus triggering criteria and bonus amount. The bonus schemes differ also in terms of target levels of bonuses which an employee included in such schemes may receive as well as the frequency of payments.

Summary information on the remuneration of the Bank Zachodni WBK employees covered by the variable remuneration policy, presented by areas of activity and executives concerned

			BONUS PAID IN 2014*				BONUS DEFERRED (2012/2013) remuneration not payable yet		
Area	Headcount	Fixed remuneration for 2014 (PLN)**	Deferred bonus for 2012 (PLN)	Bonus for 2013 (PLN)***	Non-redeemed phantom shares (number of phantom shares)	Long-term performance share programme completed in 2014 (number of BZ WBK shares)	In cash (PLN)	In phantom shares (number of phantom shares)	Long-term performance share programme launched in 2014 (number of BZ WBK shares)****
Management Board	10	11 956 676	1 646 581	6 933 057	-	38 570	3 871 475	11 695	24 073
Retail Banking	7	3 016 499	79 368	1 916 797	-	6 985	188 000	558	3 800
Business and Corporate Banking	4	1 857 000	-	822 874	-	2 492	110 557	-	4 353
Global Banking and Markets	8	5 102 764	570 801	3 404 508	-	10 027	1 227 679	590	4 440
Business Support	22	8 169 697	153 274	4 769 143	-	19 468	443 639	1 243	13 073
TOTAL	**51**	**30 102 636**	**2 450 024**	**17 846 379**	**-**	**77 542**	**5 841 350**	**14 086**	**49 739**

* at the report preparation date, no data on variable components of remuneration for the financial year

** exclusinve of additional remuneration for members of the Management Board for the completed integration with Kredyt Bank S.A.,

*** the portion paid in 2014 for 2013, not deferred. Contains phantom shares cashed in the financial year.,

**** maximum amount, subject to meeting business criteria during the programme.

Summary information on remuneration of employees of the Bank Zachodni WBK Group subsidiaries covered by the variable remuneration policy

			BONUS PAID IN 2014*			BONUS DEFERRED (2012/2013) remuneration not payable yet	
Subsidiares	Headcount	Fixed remuneration for 2014 (PLN)	Deferred bonus for 2012 (PLN)	Bonus for 2013 (PLN)**	Non-redeemed phantom shares (number of phantom shares)	In cash (PLN)	In phantom shares (number of phantom shares)
BZ WBK Faktor	1	456 000	-	173 629	-	60 000	151
BZ WBK Leasing	2	885 360	67 793	327 562	-	167 239	494
Santander Consumer Bank***	10	5 798 271	194 595	641 323	5 601	740 298	6 688
TOTAL	**13**	**7 139 631**	**262 388**	**1 142 514**	**5 601**	**967 537**	**7 333**

* at the report preparation date, no data on variable components of remuneration for the financial year,

** the portion paid in 2014 for 2013, not deferred. Contains phantom shares cashed in the financial year,

*** Including Management Board members who resigned from the Management Board in 2013 - Ramon Billordo and Jose Luis Sanchez Diaz, and in 2014 - Artur Wawrzyniak.

In the financial year, one person working for Bank Zachodni WBK Group received remuneration falling within the range of EUR 1.5m – EUR 2m.

In 2014, there were no new sign-on and severance payments or severance payments for members of staff whose actions have a material impact on the risk profile of the institution.

5th Incentive Scheme

On 30 June 2014, the Extraordinary General Meeting of Bank Zachodni WBK introduced a three-year long 5th Incentive Scheme beginning in 2014 and addressed to the bank and subsidiary employees that have a key contribution to the value of the organisation. The main objective of the programme is to retain and motivate the top-performing executives.

The Incentive Scheme covers all Management Board members of the bank and 484 key employees of Bank Zachodni WBK (as at 31 December 2014) indicated by the Management Board and approved by the Supervisory Board. Having executed an agreement with the bank, the participants are eligible to subscribe for and acquire a defined number of shares at the nominal value of PLN 10 per share provided that certain economic criteria are met. For the award to be granted, the bank must achieve a stated net profit growth rate in 2014-2016. Persons who are covered by the EU regulations on variable remuneration components and have a significant impact on the risk profile of the Group are additionally required to achieve a stated RoRWA ratio in the respective years of the programme. For the purpose of the scheme, the bank will issue up to 250,000 performance shares.

The three-year long 5th Incentive Scheme is monitored to check if any of the employees might have lost their participant status. The main reason for losing the status is the termination of the employment relationship, either with the bank or another entity of Bank Zachodni WBK Group. As at 31 December 2014, no participant of the 5th Incentive Scheme lost their participant status.