



# Financial statements of Alior Bank Spółka Akcyjna

for the financial year ended 31 December 2016

*This version of our report is a translation from the original, which was prepared in Polish language. All possible care has been taken to ensure that the translation is an accurate representation of the original. However, in all matters of interpretation of information, views or opinions, the original language version of our report takes precedence over this translation.*

## Selected financial data relating to the financial statements

	In PLN '000		
	1.01.2016 - 31.12.2016	1.01.2015- 31.12.2015	% (A-B)/B
	A	B	C
Net interest income	1 941 874	1 496 696	29,7%
Net fee and commission income	334 357	331 629	0,8%
Trading result & other	392 060	330 850	18,5%
Net impairment allowance and write-downs	-794 733	-671 772	18,3%
General administrative expenses	-1 543 456	-1 098 821	40,5%
Profit before tax	707 265	388 582	82,0%
Net profit	632 075	311 415	103,0%
Total net cash flow	-495 059	745 939	-166,4%
Loans and advances to customers	46 279 849	30 913 990	49,7%
Amounts due to customers	51 404 848	33 674 676	52,7%
Total equity	6 222 863	3 519 267	76,8%
Total assets	61 211 849	40 009 419	53,0%
<b>Selected ratios</b>			
Basic earnings per share (PLN)	6,18	4,32	43,1%
Capital adequacy ratio	13,67%	12,54%	9,0%
Tier 1	11,32%	9,68%	16,9%

	In EUR '000		
	1.01.2016 - 31.12.2016	1.01.2015- 31.12.2015	% (A-B)/B
	A	B	C
Net interest income	443 786	357 651	24,1%
Net fee and commission income	76 412	79 246	-3,6%
Trading result & other	89 599	79 060	13,3%
Net impairment allowance and write-downs	-181 624	-160 527	13,1%
General administrative expenses	-352 734	-262 574	34,3%
Profit before tax	161 635	92 856	74,1%
Net profit	144 451	74 416	94,1%
Total net cash flow	-113 138	178 250	-163,5%
Loans and advances to customers	10 461 087	7 254 251	44,2%
Amounts due to customers	11 619 541	7 902 071	47,0%
Total equity	1 406 615	825 828	70,3%
Total assets	13 836 313	9 388 577	47,4%
<b>Selected ratios</b>			
Basic earnings per share (EUR)	1,41	1,03	36,9%
Capital adequacy ratio	13,67%	12,54%	9,0%
Tier 1	11,32%	9,68%	16,9%

The following exchange rates were applied in order to translate the selected items of the consolidated financial statements into EUR:

a) as at 31.12.2016

- balance sheet items - at the average EUR exchange rate expressed in PLN, announced by the NBP as at 31.12.2016 - 4.4240;  
- income statement and cash flow statement items - at the average EUR exchange rate expressed in PLN, constituting the arithmetic mean of the average exchange rates announced by the NBP as at the end of each month - 4.3757;

b) as at 31.12.2015

- balance sheet items - at the average EUR exchange rate expressed in PLN, announced by the NBP as at 31.12.2015 - 4.2615;  
- income statement and cash flow statement items - at the average EUR exchange rate expressed in PLN, constituting the arithmetic mean of the average exchange rates announced by the NBP as at the end of each month - 4.1848;

## Table of contents

Income statement .....	5
Statement of comprehensive income .....	5
Statement of financial position .....	6
Statement of changes in equity .....	7
Statement of cash flows .....	8
Additional information to the financial statements .....	9
1. Information about the Bank .....	9
2. Summary of significant accounting policies .....	13
3. Operating segments .....	49
Notes to the income statement .....	51
4. Net interest income .....	51
5. Net fee and commission income .....	52
6. Trading result .....	53
7. Net result realized on other financial instruments .....	54
8. Net other operating income and expenses .....	54
9. General administrative expenses .....	54
10. Net impairment allowance and write-downs .....	55
11. Income tax .....	56
12. Earnings per share .....	58
Notes to the statement of financial position .....	58
13. Cash and balances with the central bank .....	59
14. Available-for-sale financial assets and investment securities held to maturity .....	59
15. Loans and advances to customers .....	61
16. Amounts due from banks .....	64
17. Property, plant and equipment .....	65
18. Intangible assets .....	66
19. Other assets .....	67
20. Amounts due to customers .....	67
21. Amounts due to banks .....	69
22. Provisions .....	70
23. Other liabilities .....	70
24. Financial assets and financial liabilities held for trading .....	72
25. Hedge accounting .....	75
26. Subordinated liabilities .....	76
27. Equity .....	78
28. Fair value .....	79
29. Off-balance sheet items .....	82
30. Acquisition of the demerged business of Bank BPH SA .....	83
31. Acquisitions of Spółdzielcze Kasły Oszczędnościowo-Kredytowe .....	93
32. Cash flow statement – additional information .....	95
33. Assets pledged as collateral .....	96
34. Transactions with related entities .....	96

35. Offsetting of financial assets and liabilities.....	99
36. Transactions, remuneration and shares held by members of the management and supervisory bodies .....	100
37. Incentive program for senior executives .....	102
38. Legal claims.....	108
39. Significant events after the balance sheet date .....	108
40. Establishment of the Bond Issue Schemes.....	109
41. Rating .....	110
Explanatory notes on risk .....	110
42. Market risk .....	110
43. Foreign exchange risk .....	113
44. Interest rate risk .....	115
45. Liquidity risk.....	117
46. Credit risk .....	121
47. Operational risk .....	141
48. Capital management.....	143
49. Registered audit company .....	146

## Income statement

	Note	1.01.2016- 31.12.2016	1.01.2015- 31.12.2015
Interest income		2 933 858	2 395 168
Interest expense		-991 984	-898 472
<b>Net interest income</b>	<b>4</b>	<b>1 941 874</b>	<b>1 496 696</b>
<b>Dividend income</b>		<b>68</b>	<b>74</b>
Fee and commission income		592 337	545 655
Fee and commission expense		-257 980	-214 026
<b>Net fee and commission income</b>	<b>5</b>	<b>334 357</b>	<b>331 629</b>
<b>Trading result</b>	<b>6</b>	<b>319 779</b>	<b>268 576</b>
<b>Net result on other financial instruments</b>	<b>7</b>	<b>21 919</b>	<b>12 923</b>
Other operating income		102 014	79 492
Other operating expenses		-51 720	-30 215
<b>Net other operating income</b>	<b>8</b>	<b>50 294</b>	<b>49 277</b>
<b>Profit from acquisition the demerged business of Bank BPH</b>	<b>30</b>	<b>508 056</b>	<b>0</b>
<b>General administrative expenses</b>	<b>9</b>	<b>-1 543 456</b>	<b>-1 098 821</b>
<b>Net impairment allowance and write-downs</b>	<b>10</b>	<b>-794 733</b>	<b>-671 772</b>
<b>Banking tax</b>		<b>-130 893</b>	<b>0</b>
<b>Profit before tax</b>		<b>707 265</b>	<b>388 582</b>
Income tax expense	<b>11</b>	-75 190	-77 167
<b>Net profit</b>		<b>632 075</b>	<b>311 415</b>
<b>Net profit</b>		<b>632 075</b>	<b>311 415</b>
<b>Weighted average number of ordinary shares</b>		<b>102 218 667</b>	<b>72 088 316</b>
<b>Net profit per share (in PLN)</b>	<b>12</b>	<b>6,18</b>	<b>4,32</b>
<b>Diluted earnings per share (in PLN)</b>	<b>12</b>	<b>6,03</b>	<b>4,15</b>

## Statement of comprehensive income

	Note	1.01.2016- 31.12.2016	1.01.2015- 31.12.2015
<b>Net profit</b>		<b>632 075</b>	<b>311 415</b>
<b>Taxable other comprehensive income to be credited to the net profit / (loss) after the required conditions have been satisfied</b>		<b>-86 852</b>	<b>-6 211</b>
Foreign currency translation differences		-22	0
Results of the measurement of financial assets available for sale (net)		-56 068	-626
Profit/loss on valuation of financial assets available for sale	14	-69 220	-773
Deferred tax	11	13 152	147
Results of the measurement of hedging instruments (net)		-30 762	-5 585
Profit/loss on valuation of hedging instruments	25	-37 978	-6 895
Deferred tax	11	7 216	1 310
<b>Total net comprehensive income</b>		<b>545 223</b>	<b>305 204</b>

## Statement of financial position

<b>ASSETS</b>	<b>Note</b>	<b>As at 31.12.2016</b>	<b>As at 31.12.2015</b>
Cash and balances with the Central Bank	13	1 082 991	1 750 135
Financial assets held for trading	24	419 551	390 569
Available-for-sale financial assets	14	9 357 734	4 253 119
Investment securities held to maturity	14	1 954	0
Hedging derivatives	25	71 684	139 578
Amounts due from banks	16	1 364 226	642 540
Loans and advances to customers	15	46 279 849	30 913 990
Assets pledged as collateral	33	366 984	628 332
pledged assets		29 783	576 534
Property, plant and equipment	17	483 520	227 633
Intangible assets	18	480 913	379 820
Investments in subsidiaries		72 359	21 975
Non-current assets held for sale		679	888
Income tax asset	11	523 371	274 015
Deferred		523 371	274 015
Other assets	19	706 034	386 825
<b>TOTAL ASSETS</b>		<b>61 211 849</b>	<b>40 009 419</b>
<b>LIABILITIES AND EQUITY</b>	<b>Note</b>	<b>As at 31.12.2016</b>	<b>As at 31.12.2015</b>
Financial liabilities held for trading	24	298 314	310 180
Amounts due from banks	21	381 235	1 051 028
Amounts due from customers	20	51 404 848	33 674 676
Derivative hedging instruments	25	6 119	0
Provisions	22	286 791	9 801
Other liabilities	23	1 433 760	526 393
Income tax liabilities		13 125	21 776
Current		13 125	21 776
Subordinated loans	26	1 164 794	896 298
<b>Total liabilities</b>		<b>54 988 986</b>	<b>36 490 152</b>
<b>Equity</b>	<b>27</b>	<b>6 222 863</b>	<b>3 519 267</b>
Share capital		1 292 578	727 075
Supplementary capital		4 184 953	2 280 668
Revaluation reserve		-71 615	15 215
Other reserves		184 894	184 894
Foreign currency translation differences		-22	0
Profit for the year		632 075	311 415
<b>TOTAL LIABILITIES AND EQUITY</b>		<b>61 211 849</b>	<b>40 009 419</b>

## Statement of changes in equity

1.01.2016 - 31.12.2016	Share capital	Supplementary capital	Other reserves	Revaluation reserve	Foreign currency translation differences	Net profit	Total equity
<b>As at 1 January 2016</b>	<b>727 075</b>	<b>2 280 668</b>	<b>184 894</b>	<b>15 215</b>	<b>0</b>	<b>311 415</b>	<b>3 519 267</b>
<b>Transfer of the previous year result</b>	-	<b>311 415</b>	-	-	-	<b>-311 415</b>	<b>0</b>
<b>Comprehensive income</b>	-	-	-	<b>-86 830</b>	-22	<b>632 075</b>	<b>545 223</b>
Net profit	-	-	-	-	-	632 075	<b>632 075</b>
Other comprehensive income	-	-	-	-86 830	-22	-	<b>-86 852</b>
<b>Share issue</b>	<b>565 503</b>	<b>1 592 870</b>	-	-	-	-	<b>2 158 373</b>
<b>As at 31 December 2016</b>	<b>1 292 578</b>	<b>4 184 953</b>	<b>184 894</b>	<b>-71 615</b>	-22	<b>632 075</b>	<b>6 222 863</b>

1.01.2015 - 31.12.2015	Share capital	Supplementary capital	Other reserves	Revaluation reserve	Net profit	Total equity
<b>As at 1 January 2015</b>	<b>699 784</b>	<b>1 775 397</b>	<b>184 167</b>	<b>21 426</b>	<b>337 030</b>	<b>3 017 804</b>
<b>Transfer of the previous year result</b>	-	<b>337 030</b>	-	-	<b>-337 030</b>	<b>0</b>
<b>Comprehensive income</b>	-	-	-	<b>-6 211</b>	<b>311 415</b>	<b>305 204</b>
Net profit	-	-	-	-	311 415	311 415
Other comprehensive income	-	-	-	-6 211	-	-6 211
<b>Share-based payments</b>	-	-	<b>727</b>	-	-	<b>727</b>
<b>Share issue</b>	<b>27 291</b>	<b>168 241</b>	-	-	-	<b>195 532</b>
<b>As at 31 December 2015</b>	<b>727 075</b>	<b>2 280 668</b>	<b>184 894</b>	<b>15 215</b>	<b>311 415</b>	<b>3 519 267</b>

## Statement of cash flows

	Note	1.01.2016- 31.12.2016	1.01.2015- 31.12.2015
<b>Operating activities</b>			
<b>Profit before tax for the year</b>		<b>707 265</b>	<b>388 582</b>
<b>Adjustments:</b>		<b>397 899</b>	<b>93 407</b>
Unrealized foreign exchange gains/losses		-7 404	-597
Dividends		68	74
Amortization/depreciation of tangible and intangible assets		101 832	85 223
Change in tangible and intangible assets impairment write-down		26 413	7 249
Change in provisions		276 990	731
Share-based payments		0	727
Gross profit after adjustments and before changing balances		<b>1 105 164</b>	<b>481 989</b>
Change in loans and receivables	32.2	-15 915 576	-4 355 141
Change in financial assets available for sale		-5 104 615	-1 283 273
Change in investment securities held to maturity		-1 954	0
Change in financial assets held for trading		-28 982	86 252
Change in assets pledged as collateral		261 348	298 859
Change in hedging asset derivatives		67 894	-59 373
Change in non-current assets held for sale		209	20
Change in other assets	32.4	-394 399	-16 378
Change in deposits		16 890 060	5 667 299
Change in issued debt		509 442	617 274
Change in financial liabilities held for trading		-11 866	-39 113
Change in hedging liabilities derivatives		6 119	-4 777
Change in other liabilities and other comprehensive income	32.3	696 172	-334 063
<b>Net cash flow from operating activities before income tax</b>		<b>-1 920 984</b>	<b>1 059 575</b>
Income tax paid		-258 007	-166 548
<b>Net cash flow from operating activities</b>		<b>-2 178 991</b>	<b>893 027</b>
<b>Investing activities</b>			
<b>Outflows:</b>		<b>-697 182</b>	<b>-518 014</b>
Purchase of property, plant and equipment	32.5	-317 754	-98 797
Purchase of intangible assets	32.6	-154 349	-72 281
Investments in subsidiaries		-50 384	-346 936
The acquisition of demerged BPH business, net of cash acquired	32.7	-174 695	0
<b>Inflows:</b>		<b>5 102</b>	<b>310</b>
Disposal of property, plant and equipment		5 102	310
<b>Net cash flow from investing activities</b>		<b>-692 080</b>	<b>-517 704</b>
<b>Financing activities</b>			
<b>Outflows:</b>		<b>-59 189</b>	<b>-201 216</b>
Repayment of long-term liabilities		0	-167 029
Interest expense – subordinated loan		-59 189	-34 187
<b>Inflows:</b>		<b>2 435 201</b>	<b>571 832</b>
Inflows from share issue		2 158 373	195 532
Inflows from the issuance of subordinated liabilities		276 828	376 300
<b>Net cash flow from financing activities</b>		<b>2 376 012</b>	<b>370 616</b>
<b>Total net cash flow</b>		<b>-495 059</b>	<b>745 939</b>
<b>incl. exchange gains/(losses)</b>		<b>22 147</b>	<b>10 859</b>
<b>Balance sheet change in cash and cash equivalents</b>		<b>-495 059</b>	<b>745 939</b>
Cash and cash equivalents, opening balance		<b>2 202 212</b>	<b>1 456 273</b>
Cash and cash equivalents, closing balance	32.1	<b>1 707 153</b>	<b>2 202 212</b>
<b>Additional disclosures on operating cash flows</b>			
Interest income received		2 844 313	2 077 930
Interest expense paid		-984 454	-549 248

## Additional information to the financial statements

### 1. Information about the Bank

#### 1.1 General information

Alior Bank Spółka Akcyjna (the Bank), with its registered office in Warsaw, ul. Łopuszańska 38D, was entered in the register of businesses maintained by the District Court for the Capital City of Warsaw, 13th Business Department of the National Court Register under the number KRS 0000305178. The Bank was assigned a tax identification number NIP: 107-001-07-31 and statistical number REGON: 141387142.

Since 14 December 2012, the Bank has been listed on the Warsaw Stock Exchange (ISIN: PLALIOR00045).

#### 1.2 Duration and scope of business activities

On 18 April 2008, the Polish Financial Supervision Authority (the "PFSA") granted permission for the incorporation of a bank under the name Alior Bank S.A. On 1 September 2008, the PFSA issued a licence for the Bank to commence its business activities. On 5 September 2008, the PFSA granted the Bank permission to conduct brokerage activities. The duration of the Bank's operations is indefinite.

On 4 November 2016, the District Court for the Capital City of Warsaw in Warsaw, 13th Business Department of the National Court Register entered an increase in the share capital of Alior Bank in the Register of Business from PLN 1,292,577,120.00 to PLN 1,292,577,630.00 effected by issuing 51 ordinary bearer J-series shares with a par value of PLN 10.00 each, in connection with the demerger of Bank BPH based on art. 529 §1.4 of the Commercial Companies Code. In accordance with art. 530 § 2 of the Commercial Companies Code, on registration of the capital increase, the said District Court registered a business combination between Alior Bank S.A. and the demerged part of Bank BPH S.A. comprising all the assets and liabilities specified in the Demerger Plan constituting the core business activities of Bank BPH. Thus, the Demerger became effective and the Core Business Activities of Bank BPH became officially a part of Alior Bank.

The transaction is discussed in Note 30.

The Bank offers services to business, institutional and retail (individual) customers (including private banking) on the territory of Poland and conducts trading and investment activities as well as brokerage activities. The Bank's core activities include maintaining bank accounts, granting loans and advances, issuing banking securities and the purchase and sale of foreign currency. As stated in the Articles of Association, Alior Bank operates on the territory of the Republic of Poland and the European Economic Area.

The Bank provides services principally to customers from Poland. The share of foreign customers in the total number of the Bank's customers is insignificant.

In 2016, as part of its retail banking activities, Alior Bank opened a foreign branch in Romania.

### 1.3 Shareholders of Alior Bank Spółka Akcyjna

As at 31 December 2016, the Bank's share capital amounts to PLN 1 292 577 630 (in words: one billion two hundred and ninety-two million five hundred and seventy-seven thousand six hundred and thirty zlotys) and is divided into 129 257 763 (in words: one hundred and twenty-nine million two hundred and fifty-seven thousand seven hundred and sixty-three) ordinary shares with a par value of PLN 10.00 (in words: ten zlotys) each, including:

- 50 000 000 A-series ordinary shares;
- 1 250 000 B-series ordinary shares;
- 12 332 965 C-series ordinary shares;
- 6 358 296 G-series ordinary shares;
- 410 704 D-series ordinary shares;
- 2 355 498 H-series ordinary shares;
- 56 550 249 I-series ordinary shares;
- 51 J-series ordinary shares.

Due to Alior Bank's status as a public company, as defined in the Act on Public Offering and the fact that the Bank's shares are listed on a regulated market (the primary market) run by the WSE, the Bank does not have detailed information on all its shareholders. Alior Bank has information on some of its shareholders who hold shares constituting at least 5% of the total number of votes at the General Shareholders' Meeting and of Alior Bank's share capital, according to the notifications received by Alior Bank pursuant to art. 69 of the Act on Public Offering.

The table below shows information on significant shareholders as at 31 December 2016 holding shares directly representing at least 5% of the total number of votes at the General Shareholders' Meeting and of Alior Bank's share capital, in accordance with the notifications received by Alior Bank pursuant to art. 69 of the Act on Public Offering.

Shareholder	Number of shares	Par value of shares [PLN]	% share in share capital	Number of votes	% share in total number of votes
<b>PZU S.A.<sup>1</sup></b>	37 773 265	377 732 650	29.22%	37 773 265	29.22%
<b>Aviva OFE Aviva BZ WBK<sup>2</sup></b>	9 262 138	92 621 380	7.17%	9 262 138	7.17%
<b>Other shares</b>	82 222 360	822 223 600	63.61%	82 222 360	63.61%
<b>Total</b>	<b>129 257 763</b>	<b>1 292 577 630</b>	<b>100%</b>	<b>129 257 763</b>	<b>100%</b>

<sup>(1)</sup> Together with the parties to the agreement dated 27 April 2016, i.e. PZU Życie, PZU Specjalistyczny Fundusz Inwestycyjny Otwarty Universum, and PZU Fundusz Inwestycyjny Zamknięty Aktywów Niepublicznych BIS 2, based on the number of shares registered at the Extraordinary General Meeting held on 29 July 2016.

<sup>(2)</sup> Based on the number of shares registered at the Extraordinary General Meeting held on 29 July 2016.

On 11 and 14 March 2016, the Management Board received notifications pursuant to art. 69 of the Act on Public Offering concerning a change in the share of the total number of votes at the General Meeting held by PZU S.A. and Alior Lux S.à.r.l. & Co. S.C.A. In accordance with the notifications received, as a result of the transaction dated 9 March 2016 (settled on 11 March 2016), PZU S.A. together with its subsidiary PZU Życie S.A. held 18 345 820 shares in the Bank constituting 25.232% of the votes at the General Shareholders' Meeting. As a result of the sale, Alior Lux S.à.r.l. & Co. S.C.A. does not hold any shares in the Bank.

In accordance with the notification received pursuant to art. 69 of the Act on Public Offering, as a result of a written agreement concluded on 27 April 2016 between Powszechny Zakład Ubezpieczeń S.A., Powszechny Zakład Ubezpieczeń Na Życie S.A., PZU Specjalistyczny Fundusz Inwestycyjny Otwarty UNIVERSUM and PZU Fundusz Inwestycyjny Zamknięty

Aktywów Niepublicznych BIS 2, concerning unanimous voting at the Bank's General Shareholders' Meetings and the change in the currently held total share in the general number of votes, the above-mentioned entities held in aggregate as at that date 21 247 464 shares in the Bank, representing 29.22% of the votes at the General Shareholders' Meeting.

Pursuant to resolution no. 3 of the Extraordinary General Shareholders' Meeting of the Bank of 5 May 2016 on increasing the share capital by issuing I-series shares as part of a closed subscription conducted through a public offering, establishing 23 May 2016 as the date of exercising the pre-emptive rights to I-series shares, granting the Supervisory Board the competence to approve the conclusion of the subissue contract, dematerialization and to apply for the admission of pre-emptive rights, rights to shares and I-series shares to trading on the regulated market run by the WSE and changing the Articles of Association, as well as authorizing the Supervisory Board to agree upon the text of the consolidated Articles of Association — in the audited period, the share capital of the Bank was increased by 56 550 249 ordinary bearer I-series shares with a par value of PLN 10.00 each. On 24 June 2016, the shares were registered in the National Court Register. The registration was the fulfilment of one of the conditions of the share sale and demerger agreement related to acquiring the demerged business of Bank BPH SA of 31 March 2016 concluded between the Bank and GE Investments Poland sp. z o.o., DRB Holdings B.V and Selective American Financial Enterprises, LLC. On 27 June 2016, the shares were registered by the National Deposit of Securities.

In connection with the share issue discussed above and based on the number of shares registered at the Extraordinary General Shareholders' Meeting of 29 July 2016, Powszechny Zakład Ubezpieczeń S.A., Powszechny Zakład Ubezpieczeń na Życie S.A., PZU Fundusz Inwestycyjny Zamknięty Aktywów Niepublicznych BIS 2 and PZU Specjalistyczny Fundusz Inwestycyjny Otwarty UNIVERSUM hold a total of 37 773 265 shares in the Bank constituting 29.22% of the votes at the General Meeting.

In accordance with resolution no. 3 of the Extraordinary General Shareholders' Meeting of the Bank of 29 July 2016 on: the demerger of Bank BPH Spółka Akcyjna pursuant to art. 529 § 1.4 of the Commercial Companies Code, on 4 November 2016, the District Court for the Capital City of Warsaw in Warsaw, 13th Business Department of the National Court Register entered the share capital increase of Alior Bank by issuing 51 ordinary bearer J-series shares with a par value of PLN 10.0 each in the register of businesses.

To the best knowledge of the Bank's Management Board, in the period from the publication of the last interim report, there were no changes in the structure of the shareholders holding at least 5% of the general number of votes, apart from those discussed above.

## 1.4 Information on the composition of the Bank's Management and Supervisory Boards

As at 31 December 2016 and 31 December 2015, the composition of the Bank's Management Board was as follows:

<b>Wojciech Sobieraj</b>	President of the Management Board
Małgorzata Bartler	Vice-President of the Management Board
Krzysztof Czuba	Vice-President of the Management Board
Joanna Krzyżanowska	Vice-President of the Management Board

Witold Skrok	Vice-President of the Management Board
Barbara Smalska	Vice-President of the Management Board
Katarzyna Sułkowska	Vice-President of the Management Board

In the reporting period, there were no changes in the composition of the Bank's Management Board.

### **Members of the Bank's Management Board who held shares in the Bank as at 31 December 2016**

Shareholder	Number of shares/ votes	Par value of shares [PLN]	% share in share capital	% share in total number of votes
<b>Wojciech Sobieraj</b>	435 296	4 352 960	0.34%	0.34%
<b>Witold Skrok</b>	178 421	1 784 210	0.14%	0.14%
<b>Katarzyna Sułkowska</b>	28 612	286 120	0.02%	0.02%
<b>Krzysztof Czuba</b>	298	2 980	0.00%	0.00%

According to the notifications dated 2 June 2016 concerning the placement of subscriptions for new issue shares as part of executing the pre-emptive rights, there was a change in the percentage holding of the Bank's shares by Mr Witold Skrok – the Vice-President of the Bank's Management Board and Mr Krzysztof Czuba – the Vice-President of the Bank's Management Board. Moreover, in connection with the registration of the Bank's share capital increase on 24 June 2016, there was a change in the percentage share in the Bank's share capital of the shares held by other Management Board Members as indicated in the above table.

On 22 December 2016, the Management Board of Alior Bank S.A informed about receiving a notification dated 22 December 2016, pursuant to art. 19 clause 1 of the MAR Regulation from Ms Katarzyna Sułkowska – Vice-President of the Bank's Management Board concerning the sale of the Bank's shares on 21 December 2016.

The composition of the Bank's Supervisory Board as at 31 December 2016 was as follows:

<b>Michał Krupiński</b>	<b>- Chair of the Supervisory Board</b>
Małgorzata Iwanicz-Drozdowska	- Deputy Chair of the Supervisory Board
Dariusz Gątarek	- Member of the Supervisory Board
Stanisław Ryszard Kaczoruk	- Member of the Supervisory Board
Marek Michalski	- Member of the Supervisory Board
Sławomir Niemierka	- Member of the Supervisory Board
Maciej Rapkiewicz	- Member of the Supervisory Board
Paweł Szymański	- Member of the Supervisory Board

The composition of the Bank's Supervisory Board as at 31 December 2015 was as follows:

<b>Helene Zaleski</b>	<b>- Chair of the Supervisory Board</b>
Przemysław Dąbrowski	- Deputy Chair of the Supervisory Board
Małgorzata Iwanicz-Drozdowska	- Member of the Supervisory Board
Sławomir Dudzik	- Member of the Supervisory Board
Niels Lundorff	- Member of the Supervisory Board
Marek Michalski	- Member of the Supervisory Board
Sławomir Niemierka	- Member of the Supervisory Board
Krzysztof Obłój	- Member of the Supervisory Board

In the reporting period, there were changes to the composition of the Bank's Supervisory Board caused by the expiry of the second four-year term of office to which the Supervisory Board Members had been appointed. As a result, on 30 March 2016, the Annual General Shareholders' Meeting of the Bank appointed the Bank's Supervisory Board for a third term of office, with the composition as follows:

- Mr Dariusz Gątarek;
- Ms Małgorzata Iwanicz – Drozdowska;
- Mr Stanisław Ryszard Kaczoruk;
- Mr Michał Krupiński;
- Mr Marek Michalski;
- Mr Sławomir Niemierka;
- Mr Maciej Rapkiewicz;
- Mr Paweł Szymański.

The appointed members of the Bank's Supervisory Board do not perform any activities that are competitive to the Bank's operations, neither do they appear in competitive companies as shareholders of partnerships or private partnerships, or members of the management or supervisory bodies of share-holding companies or other competitive legal persons.

On 17 June 2016, the Bank's Management Board was notified pursuant to art. 160.1 of the Act on Trading in Financial Instruments of 29 July 2005 by Professor Małgorzata Iwanicz-Drozdowska – a Member of the Bank's Supervisory Board about the sale of 1 465 shares in the Bank.

Therefore, to the best knowledge of the Bank's Management Board, as at 31 December 2016, the Supervisory Board Members of Alior Bank S.A. do not hold any shares in the Bank.

## 1.5 Approval of the financial statements

The financial statements of Alior Bank Spółka Akcyjna for the financial year ended 31 December 2015 were approved for publication by the Bank's Management Board on 2 March 2016.

These financial statements of Alior Bank Spółka Akcyjna were approved for publication by the Bank's Management Board on 28 February 2017.

## 2. Summary of significant accounting policies

### 2.1 Basis of preparation

#### **Scope and comparatives**

These financial statements cover the year ended 31 December 2016 and comprise the comparatives for the year ended 31 December 2015. The financial statements have been prepared in Polish zloty (PLN) and all amounts are presented in PLN thousands, unless otherwise stated.

In the financial statements of Alior Bank S.A. the fair value concept has been adopted for financial assets and liabilities designated at fair value through profit or loss, including derivatives and financial assets classified as available for sale, with the exception of those items whose fair value cannot be reliably estimated. The remaining financial assets (including

loans and advances) are carried at amortized cost less impairment losses or at cost less impairment losses. Non-current assets held for sale are stated at the lower of their carrying amount and fair value less costs to sell. Other assets and liabilities and non-current assets are shown using the model based on the cost of purchase or manufacture, i.e. after initial recognition, they are shown at historical cost less amortization/depreciation and impairment allowances.

### **Statement of compliance**

These financial statements of the Alior Bank S.A. have been prepared in accordance with the International Financial Reporting Standards (IFRS) as adopted by the European Union as at 31 December 2016, and, with respect to aspects not regulated by these standards, in accordance with the Accounting Act of 29 September 1994 (consolidated text, Journal of Laws of 30 January 2013, item 330 as amended), as well as the secondary legislation based thereon and the requirements applicable to issuers of securities admitted to or seeking admission to trading on a stock exchange.

### **Going concern**

The separate financial statements of Alior Bank S.A. have been prepared on the assumption that the Bank will continue as a going concern for a period of at least 12 months after the balance sheet date, i.e. after 31 December 2016.

As of the date of approval of these financial statements, the Bank's Management Board is not aware of any circumstances that would have a negative effect on the Bank's operations for any reasons.

### **Presentation of the financial statements**

In the statement of financial position, the Bank presents assets and liabilities in line with the liquidity criterion. The Bank does not offset income and expenses, unless it is required or permitted by standards or interpretations.

## **2.2 Significant judgements in the application of accounting policies, estimates and assumptions**

The preparation of the Bank's financial statements in accordance with the IFRS requires that the Bank's Management Board apply professional judgement and use estimates and assumptions that affect the amounts of revenues, costs, assets and liabilities, as well as disclosures concerning contingent liabilities as at the reporting date. However, due to the uncertainty associated with the professional judgement and estimates adopted, the amounts of assets and liabilities may change in the future in line with the ultimate effects of transactions.

### **Estimates and assumptions**

The areas in which estimates adopted as at the reporting date are exposed to the risk of adjustment to the carrying value of recognized assets and liabilities in the following financial year are presented below. The assumptions and estimates made by the Bank were based on data available as at the date of preparing the financial statements. However, the current circumstances and the assumptions relating to the future may change due to changes on the market or circumstances that are beyond the Bank's control. Such changes are reflected in the estimates upon their occurrence.

### Fair value of financial instruments

If it is impossible to determine the fair value of financial assets or liabilities recognized in the financial statements on the basis of active markets, it is determined using other measurement techniques, which include: using recent market transactions, an analysis of discounted cash flows, option valuation models and other techniques which are commonly used by market participants. Wherever possible, input data is obtained from observable markets. If this is not possible, professional judgement must be used to assess liquidity risk, credit risk and volatility risk. Changes in the assumptions relating to such risks can affect the recognized fair value of financial instruments. The valuation of financial instruments is discussed in detail in section 2.3.5.

For the purposes of disclosures under IFRS 7, the Bank estimates the value of changes in the valuation of derivatives with a linear risk profile assuming a parallel shift in yield curves of 50 b.p. For this purpose, the Bank constructs yield curves based on market data. The Bank analyses the effect of a change in yield curves on the transaction valuation for the following scenarios:

For a portfolio of derivatives with a linear risk profile not covered by hedge accounting

Estimated valuation change [in PLN '000]	31.12.2016		31.12.2015	
	scenario +50bp	scenario -50bp	scenario +50pb	scenario +50bp
IRS	41 063	-41 063	-5 888	5 888
CIRS	-511	511	-432	432
other instruments	-198	198	-1 260	1 260
Total	40 354	-40 354	-7 580	7 580

Instruments covered by hedge accounting

Estimated valuation change [in PLN '000]	31.12.2016		31.12.2015	
	scenario +50bp	scenario -50bp	scenario +50pb	scenario +50bp
IRS	-66 108	66 108	-44 255	44 255
Total	-66 108	66 108	-44 255	44 255

### Impairment of loans and advances to customers

The Bank assesses all loan exposures in the balance sheet (groups of loan exposures in the balance sheet) in order to identify objective indications of impairment, based on the most up-to-date information possessed by the Bank as at the revaluation date. When determining the amount of impairment loss, an assessment is made of the estimated amounts and due dates of future cash flows. The estimates are based on assumptions concerning a number of factors, therefore the actual results may differ from the estimates. As a result, the amount of impairment loss may change in the future.

The exposures in respect of which indications of impairment have been identified are divided into those that are measured individually and those that are measured in groups. The exposures in respect of which no indications of impairment have been identified are grouped in accordance with the principle of maintaining a homogeneous risk profile and IBNR provisions are created for such groups of exposures. The amount of IBNR is determined based on PD, LGD and hedging parameters (taking into account the expected recovery rates).

The effect of increases/decreases in cash flows (including cash flows from the execution of hedges) on impairment of the portfolio of loans and advances measured individually by the Bank is presented in the following table (in PLN million):

	31.12.2016		31.12.2015	
	scenario +10%	scenario -10%	scenario +10%	scenario -10%
The estimated change in impairment of loans and advances resulting from a change in the present value of estimated cash flows for loans and advances measured individually by the Bank	-78.52	141.79	-40.24	102.43

The effect of increases/decreases in cash flows (including cash flows from the execution of hedges) on impairment of the portfolio of loans and advances measured by the Bank on a group basis is presented in the following table (in PLN million):

	31.12.2016		31.12.2015	
	scenario +10%	scenario -10%	scenario +10%	scenario -10%
The estimated change in impairment of loans and advances resulting from a change in the present value of estimated cash flows for loans and advances measured by the Bank using group method	-72.79	84.15	-62.01	73.83

The effect of increases/decreases in the PD parameter on the change in the IBNR provision is presented in the following table (in PLN million):

	31.12.2016		31.12.2015	
	scenario +10%	scenario -10%	scenario +10%	scenario -10%
The estimated change in impairment allowances for losses incurred but not reported (IBNR) of loans and advances resulting from a change in the value of PD LIP	17.18	-17.19	16.46	-16.47

A detailed description of the estimates of impairment losses is presented in Note 46.

### Impairment of assets available for sale

For the purposes of disclosures under IFRS 7, the Bank estimates the value of changes in the valuation of debt instruments available for sale assuming a parallel shift in yield curves of 50 b.p. For this purpose, the Bank constructs yield curves based on market data. The Bank analyses the effect of a change in yield curves on the transaction valuation for the following scenarios:

Estimated change in evaluation [in PLN '000]	31.12.2016		31.12.2015	
	scenario +10%	scenario -10%	scenario +10%	scenario -10%
Available-for-sale financial assets	-46 452	46 452	-14 387	14 387
Total	-46 452	46 452	-14 387	14 387

Impairment of available-for-sale assets is discussed in detail in section 2.3.7.

### Recognition of income from bancassurance

In 2016 and 2015, the Bank applied a method whereby bancassurance (insurance offered in association with cash and mortgage loans) fees are deferred, based on the "relative fair value" model which best reflects the economic substance of such transactions. Bancassurance is described in detail in the description of accounting policies in Note 2.3.2.

Estimated sensitivity analysis of the change in the revenues recognized by the Bank in 2016 with reference to income from bancassurance is as follows:

- Scenario of a 5 p.p. increase in the provision for withdrawals: -PLN 15.19 million (a decrease in net interest income);
- Scenario of a 5 p.p. decrease in the provision for withdrawals: +PLN 15.19 million (an increase in net interest income);
- Scenario of a 1 p.p. increase in revenue recognized upfront: +PLN 661 thousand (an increase in net commission income);
- Scenario of a 1 p.p. decrease in revenue recognized upfront: -PLN 661 thousand (a decrease in net commission income).

Estimated sensitivity analysis of the change in the revenues recognized by the Bank in 2015 with reference to income from bancassurance is as follows:

- Scenario of a 5 p.p. increase in the provision for withdrawals: -PLN 20.48 million (a decrease in net interest income);
- Scenario of a 5 p.p. decrease in the provision for withdrawals: +PLN 20.10 million (an increase in net interest income);
- Scenario of a 1 p.p. increase in revenue recognized upfront: +PLN 2.64 million (an increase in net commission income);
- Scenario of a 1 p.p. decrease in revenue recognized upfront: -PLN 2.64 million (a decrease in net commission income).

### **The impairment of goodwill on acquisition and merger with Meritum Bank ICB S.A.**

As at 31 December 2016, the Bank conducted obligatory impairment tests of goodwill on the acquisition of Meritum Bank Polska SA in line with the models developed based on the guidance contained in IAS 36.

Impairment tests are carried out by comparing the carrying amounts of cash generating units ("CGU") with their recoverable amounts.

Two CGUs – retail and corporate – were identified to which goodwill on the acquisition of Meritum Bank Polska SA was allocated.

The recoverable amount is estimated based on the value in use of the CGU. The value in use is the present estimated value of future cash flows for a period of 5 years, taking into account the residual value of the CGU. The residual value of the CGU has been calculated using the theoretical dividend model (Gordon growth model) by extrapolating cash flow projections beyond the forecast period, using the growth rate adopted at a level of 3%. Cash flow forecasts are based on the assumptions contained in the Bank's financial plan for 2017 and the Bank's strategy for subsequent years. The Bank applied a discount rate of 10.1%, taking account of the risk-free rate and risk premium, to discount future cash flows.

The impairment test conducted as at 31 December 2016 showed that the recoverable amounts exceeded the carrying amounts of the individual CGUs and therefore, no impairment was identified for the CGUs.

### **Determining the fair value of the acquired assets and liabilities (a separate part of the acquisition of BPH S.A.)**

The results of fair valuation of loan portfolio of the demerged part of BPH SA were subject to sensitivity analysis. Range of possible outcomes of the fair valuation was estimated under 50 basis points increase/decrease in discount rate scenarios. Shift of 50 bp. includes possible compound sensitivity of the key parameters used in the model, ie. the cost of credit risk, cost of capital, the cost of financing and the cost of servicing loans. Applying the above sensitivity

analysis results in obtaining the following results of the fair valuation of the loan portfolio: 277 million PLN in the case of reducing the discount rate by 50 p.p and 455 million PLN in the case of an increase of 50 p.p.

A detailed description of the valuation model is presented in note 30.

## 2.3 Major accounting policies

### 2.3.1 Transactions in foreign currencies

#### **Functional currency and presentation currency**

Items included in the Bank's financial statements are measured using the currency of the primary economic environment in which the entity operates ("the functional currency"). The financial statements have been prepared in Polish zloty and the amounts are given in thousands, unless otherwise stated. The Polish zloty is the functional and reporting currency of the Bank (the Polish zloty is also the functional currency of the Bank and other entities included in the financial statements).

#### **Transactions and balances in foreign currencies**

Foreign currency transactions are initially recorded using the exchange rate of the functional currency prevailing at the date of the transaction. At the end of each reporting period, the Bank translates:

- monetary assets and liabilities expressed in foreign currencies using the mid exchange rate set by the National Bank of Poland prevailing as at the end of the reporting period;
- foreign currency non-monetary items measured at historical cost using the exchange rate prevailing at the date of initially recording the transaction;
- foreign currency non-monetary items measured at fair value using the exchange rate prevailing at the date of determining the fair value.

Foreign exchange gains and losses resulting from the settlement of transactions and from the year-end translation of monetary assets and liabilities denominated in foreign currencies are recognized in the income statement. Foreign exchange gains and losses on items such as equity instruments classified as available for sale are included in the revaluation reserve of available-for-sale financial assets.

Income, expenses, assets and liabilities of foreign business entities (including branches), which have a functional currency other than PLN, valued at PLN according to the following schedule :

- assets and liabilities at the balance sheet date are valued at the average exchange rate published by National Bank of Poland for that date
- income and expenses are valued by the arithmetic average of exchange rates published by National Bank of Poland at the end of each day
- the foreign exchange rate differences from the valuation of foreign entities are accounted for as a separate component of equity. It is amortized to income statement on disposal of a foreign entity.

EUR	2016	2015
Exchange rate as at the last day of the period	4.4240	4.2615
Arithmetic mean of the exchange rates as at the last day of each in the period	4.3757	4.1848

RON	2016
Exchange rate as at the last day of the period	0,9749
Arithmetic mean of the exchange rates as at each day in the period	0,9714

### 2.3.2 Financial assets and liabilities - initial recognition and classification

The Bank records a financial asset or liability in the statement of financial position when it becomes a party to this instrument contract. Standardized purchase and sale transactions in respect of financial assets are recorded as at the settlement date.

Upon initial recognition all financial instruments are measured at fair value.

The Bank initially classifies financial assets and liabilities depending on their purpose, characteristics and intentions towards a purchased financial instrument.

The Bank classifies financial assets in the following categories: financial assets designated at fair value through profit or loss; available-for-sale financial assets; loans and receivables and held-to-maturity investments. Financial liabilities are classified in the following categories: financial liabilities measured at fair value through profit or loss and other financial liabilities.

#### **Financial assets and liabilities designated at fair value through profit or loss**

Financial assets and liabilities designated at fair value through profit or loss comprise:

- financial instruments held for trading – financial assets and liabilities are classified as held for trading if they have been acquired for the purpose of selling them in the near future. This category contains derivative instruments concluded by the Bank, which were not designated as effective hedging instruments in accordance with IAS 39 as at the date of establishing the hedging relationship;
- financial instruments classified initially to financial assets designated at fair value through profit or loss – financial assets and liabilities can be classified in this category when:
  - a designated financial asset or liability is a combined instrument containing one or more embedded derivatives qualifying for separate recognition, while the embedded derivative cannot significantly change the cash flows arising from the host contract or separating the derivative is not allowed;
  - such classification of an asset or liability eliminates or significantly reduces inconsistency with respect to measurement or recognition (known as accounting mismatch resulting from a different method of measurement of assets or liabilities or a different method of recognition of the related profits or losses);
  - a group of financial assets or liabilities, or both, is properly managed and its results are evaluated based on fair value, in line with the documented risk management principles or the Bank's investment strategy.

As at 31 December 2015 and 31 December 2014, the Bank did not hold financial assets classified in category of financial instruments classified upon initial recognition as valued at the fair value through profit or loss.

#### **Available-for-sale financial assets**

Available-for-sale financial assets are non-derivative financial assets which have been designated as available for sale, or other than loans and receivables, investments held to maturity, financial assets measured at fair value through profit or loss.

### **Investment securities held to maturity**

The Bank classifies here financial assets with determined or determinable payments and with determined maturity, which the Bank definitely intends and is able to hold to maturity.

### **Loans and receivables**

The Bank classifies within this category non-derivative financial assets with fixed or determinable payments that are not quoted in an active market, other than:

- financial assets which the Bank intends to sell immediately or in the near term, which shall be classified as held for trading, and those that the entity upon initial recognition designates as at fair value through profit or loss;
- financial assets that the entity upon initial recognition designated as available-for-sale;
- financial assets for which the holder may not recover all of its initial investments, other than because of credit deterioration, which are classified as available-for-sale.

As at 31 December 2016 and 31 December 2015, the Bank held in this category amounts due from other banks (inter-bank deposits, guarantee deposits, security deposits and cash on a current account) and loans and advances, purchased receivables and other amounts due from customers. As at 31 December 2016, the Bank also held repo transactions in this category.

### **Other financial liabilities**

Other financial liabilities are financial liabilities other than designated as at fair value through profit or loss that are deposits, loans or advances received.

As at 31 December 2016 and 31 December 2015, this category included amounts due to banks, including loans received, a subordinated loan received and amounts due to customers, including amounts due in respect of deposits and issued bank securities and repo transactions. Liabilities designated at amortized cost using the effective interest rate method.

## 2.3.3 Financial assets and liabilities – subsequent measurement

### **Financial assets and liabilities designated at fair value through profit or loss**

Financial assets and liabilities designated at fair value through profit or loss are measured at fair value with the measurement result taken to the income statement.

### **Available-for-sale financial assets**

Instruments classified as available for sale are measured to fair value with the measurement result taken to equity (other comprehensive income). On selling an instrument, the cumulative gain/loss is recognized in the income statement. Interest accrued using the effective interest rate on available-for-sale assets is recognized in the income statement.

In the event of objective evidence of impairment of debt financial assets available for sale, the cumulative revaluation write-down is eliminated from the revaluation reserve and recognized in the income statement.

### **Investment securities held to maturity**

Investments held to maturity are measured at amortized cost using the effective interest rate method. If there are indications of impairment, the Bank recognizes impairment losses.

## **Loans and receivables**

The Bank states loans and receivables at amortized cost using the effective interest rate method, taking account of impairment losses.

## **Renegotiated contracts**

The renegotiation of the contractual terms of loans and advances constitutes an indication of impairment, unless the renegotiation was not forced by the debtor's situation but was carried out on normal business terms. Subsequently, the Bank assesses whether impairment of such loans and advances should be recognized on a case-by-case or a group basis. In the case of renegotiation unforced financial situation of the debtor, if a change in the contractual cash flow is calculated new effective interest rate.

## **Other financial liabilities**

Other financial liabilities, including liabilities in respect of bank securities issued, are measured at amortized cost using the effective interest rate method.

## **Financial guarantee contracts/ unused commitments to provide financing**

Financial guarantee contracts are contracts that impose on the issuer an obligation to make certain payments to compensate the holder for a loss incurred due to a debtor's failure to make payment when due in accordance with the original or amended terms and conditions of the debt instrument.

Upon initial recognition, financial guarantee contracts and commitments of the Bank to provide financing unused by customers are measured at fair value. After initial recognition, they are measured at the higher of:

- the amount determined in accordance with IAS 37, Provisions, Contingent Liabilities and Contingent Assets; or
- initial cost less, as appropriate, accumulated amortization recognized in accordance with IAS 18, Revenue.

### **2.3.4 Derecognition of financial assets and liabilities from the balance sheet**

#### **Financial assets**

The Bank derecognizes a financial asset when:

- the contractual rights to cash flows from that financial asset have expired; or
- the Bank has transferred the contractual rights to obtain cash flows from that financial asset to another entity.

Upon transfer of a financial asset, the Bank assesses to what extent it retains the risks and benefits of ownership of a financial asset. In such cases:

- if the Bank transfers substantially all risks and benefits of ownership of a financial asset, it derecognizes the financial asset from the statement of financial position;
- if the Bank retains substantially all risks and benefits of ownership of a financial asset, it continues to recognize the financial asset in the statement of financial position;
- if the Bank neither transfers nor retains substantially all risks and benefits of ownership of a financial asset, it determines whether it has retained control over this financial asset. If control has been retained, the financial asset continues to be recognized in the balance sheet, and if there is no control it is derecognized up to the amount arising from the continuing involvement.

The Bank derecognizes loans and receivables or their portion, and if the rights related to a loan agreement expire the Bank waives such rights or performs an unconditional sale of the loan. If financial assets have been deemed irrecoverable, impairment write-downs are usually recognized. Receivables that were previously written off and subsequently recovered decrease the impairment write-downs in the income statement.

### **Financial liabilities**

The Bank derecognizes a financial liability or a portion thereof when the obligation specified in the contract has been fulfilled, forgiven or has expired.

#### **2.3.5 Fair value measurement**

##### **Fair value of financial instruments**

The individual items of financial assets/liabilities are classified to the following categories using the adopted fair value measurement approaches:

- level I - financial assets/liabilities measured directly based on prices quoted on the principal (or the most advantageous) market;
- level II - financial assets/liabilities measured using valuation techniques based on the assumptions developed with the use of information from the principal (or the most advantageous market);
- level III - financial assets/liabilities measured using valuation techniques commonly used by market participants, whose assumptions are not based on information from the principal and the most advantageous market.

Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction on the principal (or the most advantageous) market as at the measurement date under the current market conditions (i.e. the exit price), irrespective of whether such price is directly observable or estimated with the use of another measurement technique.

The fair value of financial instruments is based on prices quoted on the principal (or the most advantageous) active market, without deducting the transaction costs. If the market price is unavailable, the fair value of an instrument is estimated using the measurement models or techniques for discounting future cash flows.

The measurement techniques are based on:

- recent market transactions concluded directly between informed interested parties, provided that such information is available;
- a reference to the present fair value of another instrument with almost identical characteristics;
- the discounted cash flow method.

If there is a technique that is commonly used by market participants to measure a financial instrument and it has been demonstrated to provide reliable estimates of prices paid in actual market transactions, the Bank uses such a method. The selected measurement techniques are primarily based on market data. Which to a limited extent use data specific to the Bank. The measurement technique comprises all factors that the market participants would take into account when determining the price and it is consistent with the accepted methods of measurement of financial instruments. The Bank verifies the correctness of measurement using the available prices paid for the same instrument in recent market transactions or other available market data.

### Balance-sheet items measured at fair value

Financial instrument	Frequency	Recognition/presentation
Available-for-sale financial assets	Daily	other comprehensive income
Fx forward, fx swap, fx options	Daily	income statement
CIRS, FRA, IRS	Daily	income statement
Other derivatives	Daily	income statement
Shares listed on the Warsaw Stock Exchange	Daily	income statement

The Bank has adjusted the measurement of derivatives for counterparty credit risk. Consequently, the measurement of derivatives changes in the event of insolvency of either party to the transaction (Bilateral Credit Value Adjustment). The amount of such adjustment is calculated based on the estimates of the following parameters: PD (Probability of Default), LGD (Loss Given Default), Expected Exposure (EE) and Expected Negative Exposure (ENE). The effect of such adjustment on the financial result is presented in Note 28.

PD and LGD are estimated by the Bank using internal models based on market quotations of credit risk. Counterparty exposures are calculated taking into account the current valuation and its projection calculated based on the expected changes in market conditions. Additionally, the estimations of credit risk adjustments take into account mutual liabilities of the parties to the transaction resulting from hedging agreements.

### Derivatives

The Bank uses the following financial derivatives to manage market risk: FX-Forward, FX-Swap, IRS, CIRS, FRA, security forwards and futures. The Bank initially (on the date of signing the contract) recognizes such transactions at the fair value (without taking into account the transaction costs), and subsequently performs revaluations. Derivatives are recognized as financial assets if their fair value is positive, or as financial liabilities if it is negative.

Any gains or losses on the fair value changes of derivatives are taken directly to the trading result in the income statement, except for the effective portion of cash flow hedges, which are recorded in other comprehensive income.

The Bank uses cash flow hedge accounting. A detailed description of hedge accounting is presented in Note 25.

The Bank separates embedded derivatives from the host contract and recognizes them in the same manner as other derivatives, provided that:

- the business characteristics and risks associated with embedded derivatives are not closely related to the business characteristics and risks associated with the host contract;
- an independent instrument with the same contractual terms and conditions as the separated embedded derivative would meet the definition of a derivative;
- the host contract is not measured at fair value through profit or loss.

### 2.3.6 Reverse repo and repo transactions

In the statement of financial position, the Bank presents repo transactions on securities in accordance with the business purpose of such transactions.

The Bank verifies whether a purchase/sale of securities is associated with transferring the risks and benefits arising from such securities.

In the case of transactions concluded by the Bank to date, substantially all risks and benefits are retained by the seller of the securities, since the risk of changes in the net present value of an asset does not change significantly as a result of its transfer.

Therefore, both reverse repo (buy-sell-back) and repo (sell-buy-back) transactions in securities are presented in the Bank's balance sheet as deposits placed with the buyer of the securities or deposits received from the buyer of the securities, respectively. The difference between the sales price and the buy-back price is treated accordingly as interest expense/income.

Securities subject to repo transactions are not excluded from the statement of financial position and are measured in line with the principles specified for the individual security portfolios.

### 2.3.7 Impairment of financial assets

At the end of each reporting period, the Bank verifies whether there is any objective evidence of impairment of a financial asset or a group of financial assets. The Bank determines that a financial asset or a group of financial assets has been impaired and recognizes an impairment loss if and only if there is objective evidence of impairment resulting from one or more events that occurred after the initial recognition of the asset (loss event), and the loss event (or events) affect the expected future cash flows from that financial asset or a group of financial assets that can be measured reliably.

Evidence of impairment includes:

- significant financial difficulties of an issuer or debtor;
- contract default, e.g. failure to pay or being overdue with the payment of interest or principal;
- granting a loan for economic or legal considerations arising from the borrower's financial difficulties, a convenience which would not otherwise be granted by the lender;
- the high probability of bankruptcy or other financial reorganization of the borrower;
- disappearance of an active market for a given financial asset due to the borrower's financial difficulties;
- observing data indicating a measurable decline in estimated future cash flows related to a group of financial assets from the moment of their initial recognition, although a decline in an individual asset from the group of financial assets cannot yet be identified;
- information on significant adverse changes in the technological, market, economic, legal or other environment in which the issuer operates, indicating that the cost of investment in the equity instrument may not be recoverable.

A detailed description of impairment of financial assets is provided in Note 46.

#### **Financial assets measured at amortized cost**

In the case of financial assets measured at amortized cost, the Bank determines whether there is objective evidence of impairment of individual financial assets that are individually significant or, in the case of financial assets that individually are not significant, individually or collectively significant.

If the Bank determines that there is no objective evidence of impairment of a financial asset which is assessed on a case-by-case basis, irrespective of whether it is significant or not, the asset is included in a group of financial assets with similar credit risk characteristics which are collectively assessed for impairment. Assets assessed for impairment case-by-case for which the entity records impairment allowances or decides to continue to record the allowances are not recognized in the collective assessment of impairment.

If there is objective evidence that an impairment loss has been incurred, the amount of the impairment loss is the difference between the asset's carrying amount and the present value of estimated future cash flows (excluding future credit losses, which have not been incurred), discounted at the initial effective interest rate of the financial instrument (i.e. the effective interest rate fixed on initial recognition). Interest income is accrued using the interest rate applied for discounting future cash flows for the purpose of estimating impairment loss. Exposures with identified indications of impairment are classified into those measured on a case-by-case and on a group (collective) basis.

The individual assessment applies to exposures carrying the risk of impairment (calculated at customer level) which exceed the established thresholds set depending on the customer segment. Individual assessment is also applied to exposures threatened with impairment in respect of which the Bank is unable to identify the groups of assets with similar credit risk characteristics or does not have a sufficient sample for estimating group parameters.

For the purpose of collective valuation, groups with similar credit risk characteristics are identified and assessed collectively for impairment. The group valuation is based on the time of a given exposure being impaired and takes into account the specific nature of a given group in terms of the expected recoveries.

Future cash flows in a group of financial assets for which impairment is assessed collectively are estimated on the basis of the history of losses for assets with similar credit risk characteristics. The adjustment of the historical data takes into account the current circumstances and disappearance of conditions which are currently absent. The estimates of changes in future cash flows reflect changes in the related available data in the individual periods (such as unemployment rate, real estate prices, prices of goods, status of payments and other factors which indicate losses incurred in the group and their extent), and in principle are consistent with them. The method and assumptions adopted for estimating future cash flows are regularly reviewed in order to minimize the discrepancy between the estimated and actual losses.

If in the subsequent period the amount of impairment loss is reduced as a result of an event which took place after the impairment, then the previously recorded impairment loss is reversed by adjusting the balance of impairment allowances. The amount of the reversal is recognized in the income statement.

### **Available-for-sale financial assets**

At the end of each reporting period, the Bank assesses whether there is objective evidence of impairment for financial assets available for sale based on the same criteria as those adopted for financial assets measured at amortized cost. If such indications exist, the Bank establishes the amounts of impairment losses.

The amount of an impairment loss recorded is the amount of cumulative loss which is removed from equity and recorded in the income statement as a difference between the cost of purchase (less any repayment of principal and amortization) and the current fair value less any impairment losses related to a given asset previously recognized in the income statement.

Interest income for available-for-sale financial assets for which an impairment loss has been recorded is accrued on the reduced present value using the effective interest applied for discounting future cash flows for the purpose of estimating impairment loss.

If in a subsequent period the fair value of a debt instrument available for sale increases and the increase could be objectively linked to an event subsequent to the recognition of the loss in the income statement, the amount of the reversed impairment loss is recognized in the income statement.

Impairment losses in respect of investments in equity investments classified as available for sale may not be reversed through the income statement.

### 2.3.8 Offsetting of financial instruments

The Bank offsets financial assets with financial liabilities by recording a net amount in the statement of financial position when and only when:

- there is a valid legal title to offset the recorded amounts; and
- the Bank intends to settle the assets and liabilities on a net basis or realize the asset at the same time as it is settling the liabilities.

### 2.3.9 Subsidiaries

Subsidiaries are measured by Bank according to cost of acquisition, including write-downs.

### 2.3.10 Hedge accounting

Hedge accounting is applied in order to match in the income statement changes in the fair value of hedging instruments which are offset against the hedged item.

The Bank designates hedging instruments for hedge accounting purposes, so that the change in their fair value or cash flows covers in full or in part the change in fair value or future cash flows of the hedged item.

The Bank applies hedge accounting if all of the following conditions specified in IAS 39 have been satisfied:

- at the moment of establishing the hedge, formal documentation of the hedging relationship has been prepared, which specifies the goal and strategy of the hedge, type and identification of both the hedged and the hedging instrument, type of risk being hedged and the method of assessing the hedge effectiveness;
- the effectiveness of the hedge is expected to be high, i.e. high effectiveness in offsetting the fair value or cash flow changes, in line with the documented risk management strategy related to the specific hedging relationship;
- it is possible to reliably evaluate the hedge effectiveness, i.e. to reliably measure the fair value or cash flows related to both the hedged and the hedging item;
- in the case of cash flows, it is highly probable that a hedged transaction may occur which is exposed to cash flow risk affecting the income statement;

- the hedge is regularly assessed and its high effectiveness is evaluated in all the reporting periods for which the hedge had been designated.

As part of hedge accounting, the Bank applies cash flow hedge accounting.

A cash flow hedge means a hedge against changes in future cash flows which can be attributed to a specific type of risk related to a recorded asset or liability, or a highly probable projected transaction, affecting the income statement.

A cash flow hedge is recorded as follows in the books of account:

- a) the portion of gains or losses related to a hedging instrument constituting an effective hedge is recorded in other comprehensive income.

The effective portion of the hedge is recorded in the revaluation reserve at the lower of (in absolute amounts):

- gains or losses on the hedging instrument accumulated from the moment of establishing the hedge;
- a change in fair value (present value) of expected future cash flows arising from the hedged item, accumulated from the moment of establishing the hedge;

and

- b) the ineffective portion of gains or losses related to a hedging instrument is recorded in the income statement.

The effective portion of the hedge is transferred to profit or loss in the same period or periods in which the planned hedged transaction affects the income statement.

The Bank ceases to apply hedge accounting when at least one of the following events occurs:

- the hedging instrument is sold, expires, is terminated or exercised;
- the hedge accounting conditions referred to above have not been satisfied;
- the Bank annuls the hedging relationship;
- future cash flows are no longer considered to be probable.

If any of the above events occurs, the result on a hedging instrument when the hedge was effective is still recorded in the revaluation reserve, until the projected transaction is concluded and recognized in the income statement.

### 2.3.11 Leases

The Bank decides whether an agreement is a lease agreement or an agreement containing a lease, based on significant agreements, and assesses whether fulfilling the agreement depends on using a specific asset or assets, and the agreement transfers the right to use the asset.

The Bank is only a party to such lease agreements on the basis of which it accepts third party fixed assets for use at a charge or for drawing benefits from them over a specified period whereby all risks and benefits from the leased assets remain with the lessor. The lease charges over the lease period are recorded as costs in the income statement using the straight-line method.

### 2.3.12 Cash and cash equivalents

For the purpose of the cash flow statement, the balance of cash and cash equivalents comprises cash (cash in hand and at central bank) and its equivalents (highly liquid short-term investments, easily exchangeable to specified amounts of cash and exposed to insignificant risk of value changes).

### 2.3.13 Investment properties

#### **Recognition and measurement**

Investment properties comprise properties which the Bank treats as a source of economic benefits from rental income or an increase in their fair value (or both). Investment properties are initially measured at the cost of purchase or manufacture including transaction costs. Following initial recognition of investment properties, the Bank measures them at the cost of purchase or manufacture less accumulated depreciation and impairment.

### 2.3.14 Property, plant and equipment

#### **Recognition and measurement**

Property, plant and equipment comprise assets with an estimated useful life of more than one year, which are complete and used for the purpose of rendering services. Property, plant and equipment are initially recognized at acquisition cost or cost of development. After initial recognition property, plant and equipment are measured at acquisition cost or cost of development less accumulated depreciation and impairment losses.

#### **Depreciation and impairment**

Depreciation charges on property, plant and equipment are calculated using the straight-line method, in accordance with specified depreciation rates over their estimated useful life. Depreciation charges are taken to profit or loss. The amount subject to depreciation is the cost of purchase or development of a given asset, less any residual value of the asset. The economic useful life, depreciation rates, and residual value of depreciable fixed assets are reviewed each year. Depreciation charges are presented in general administrative expenses.

#### **Estimated useful lives of property, plant and equipment**

Specification	Useful life in years
Leasehold improvements (buildings and structures)	5-10
Plant and machinery	1-5
Fixtures and fittings	2-10
Vehicles	2.5-5

At each balance sheet date, the Bank evaluates its assets for indications of impairment. Where impairment indicators are identified, the Bank formally estimates the recoverable amount. Where the carrying amount of a given asset exceeds its recoverable amount, an impairment loss is recognized and the asset's carrying amount is written-down to its recoverable amount. The recognition or reversal of impairment losses are taken to profit or loss.

#### **Subsequent expenditure**

Expenditure incurred after initial recognition of a given item of property, plant and equipment is capitalized when it increases the future economic benefits from the asset. Otherwise, the expenditure is charged directly to the income statement when incurred.

### 2.3.15 Intangible assets

#### Recognition and measurement

Intangible assets are identifiable non-monetary assets without physical substance. They are initially measured at acquisition cost or cost of development. The Bank capitalizes:

- expenses incurred in relation to the purchase of a software licence and development of a licence or module to the acquired licence;
- the costs of development of an intangible asset, comprising all expenditure (including the costs of employee benefits) that can be directly attributed to the operations associated with the development of the intangible asset and preparing it for its intended use.

The cost of intangible assets purchased as part of separate transaction covers:

- purchase price, inclusive of import duties and non-refundable purchase taxes after deducting trade discounts and rebates;
- any directly attributable costs of preparing the asset for its intended use.

Goodwill comprises the excess of the cost of acquisition over the fair value of acquired assets, equity & liabilities and contingent liabilities of a subsidiary, associate or jointly controlled entity. After initial recognition goodwill is stated at cost, less accumulated impairment. In the case of disposal of a subsidiary, goodwill recognized on acquisition is calculated on the profit or loss representing the settlement of the sale.

#### Amortization and impairment

After initial recognition intangible assets with a finite economic useful life, including those internally generated, are recognized at acquisition cost or cost of development less accumulated amortization and impairment losses. At each balance sheet date, the Bank evaluates its assets for indications of impairment. Where impairment indicators are identified, the Bank formally estimates the recoverable amount. Where the carrying amount of a given asset exceeds its recoverable amount, an impairment loss is recognized and the asset's carrying amount is written down to its recoverable amount.

Goodwill impairment is determined by estimating the recoverable amount of the cash-generating unit concerned. If the recoverable amount of a cash-generating unit is lower than its carrying amount, an impairment loss is recognized. Impairment identified as a result of tests performed cannot be subsequently adjusted. Goodwill is analysed for impairment as at each balance sheet date (31 December) or earlier, if any indications of impairment have been identified.

Amortization charges on intangible assets are calculated using the straight-line method, in accordance with specified amortization rates over their estimated useful life. The economic useful life, amortization rates, and residual value of amortized intangible assets are reviewed each year. Depreciation charges are presented in general administrative expenses.

Specification	Useful life in years
Licences	2-12,5
System software	2-10
Development costs	2-12,5

### **Subsequent expenditure**

Expenditure incurred after initial recognition of a given intangible asset is capitalized when it increases the future economic benefits from the asset. The cost of developing a licence or an additional module to an acquired licence by the entity internally includes all outlays which can be directly attributed to the tasks of creating, manufacturing and adapting an asset for use in the manner intended by management.

Otherwise, such expenditure is taken to the profit or loss.

#### **2.3.16 Non-current assets held for sale**

Non-current assets held for sale are assets the carrying amount of which is to be recovered by their resale rather than continued use. The Bank classifies as held for sale only those assets which are available for immediate sale in their present condition and whose sale is highly probable, i.e. a decision has been made to execute the sales plan of a given asset, and an active programme for finding a buyer and completing the sales plan has been initiated. Moreover, such asset is offered for sale at a price which is rational taking into account the asset's current fair value, and it is expected that the sale will be recorded as closed within one year from the date of classifying a given asset to this category. This category also includes non-current assets repossessed as repayment of debt, which the Bank does not intend to use for its own purposes.

Non-current assets held for sale are stated at the lower of their carrying amount and fair value less costs to sell. Revaluation write-downs of non-current assets held for sale are recognized in the income statement for the period in which the write-downs were made. Amortization is not charged on assets classified to this category.

Non-current assets which no longer meet the classification criteria for inclusion in non-current assets held for sale are reclassified to an appropriate category of assets. Non-current assets withdrawn from assets held for sale are measured at the lower of:

- the carrying amount from before the moment of its classification to non-current asset held for sale, less amortization/depreciation that would have been recorded had the asset (the disposal group) not been classified as held for sale;
- and the recoverable amount as of the date of making a decision not to sell.

#### **2.3.17 Impairment of non-financial assets**

As at the balance sheet date, the Bank's assets, with the exception of deferred tax assets, are reviewed for indicators of impairment. If such indicators are identified, the Bank estimates the recoverable amount of the asset.

Impairment occurs when the carrying amount of an asset exceeds its recoverable amount. The impairment loss thus identified is recognized in the income statement.

The recoverable amount corresponds to the higher of: fair value less costs to sell and value in use of an asset.

Value in use is established by discounting the estimated future cash flows for a given asset, using the discount rate before taxation. For assets which do not generate independent cash flows, the Bank determines the recoverable amount on the level of a cash generating unit to

which a given asset belongs. An impairment loss can be reversed only to the level at which the carrying amount of the assets does not exceed the carrying amount which (less amortization/depreciation) would be established had no impairment loss been recorded.

The recoverable amount corresponds to the higher of the asset's value in use and net realizable value at the moment of performing the review.

When determining the value in use, the estimated future cash flows are discounted to the present value using the gross discount rate reflecting the current market expectations as to the time value of money and the risk typical to a given asset.

Impairment losses relating to goodwill are not reversed. With respect to other assets, the loss can be reversed provided that there has been no change in estimates based on which the recoverable amount is determined.

### 2.3.18 Provisions for employee benefits

Calculation of the provisions is based on a number of assumptions relating to both macroeconomic conditions, the employee turnover ratio and risk of death and other. The basis for the calculation of the said provisions is the estimated amount of pension or retirement benefits which the Bank will be required to pay out based on the Remuneration Regulations.

The estimated amount of benefits is calculated as the product of the following::

- estimated amount of the base for the calculation of retirement or pension benefits, in accordance with the provisions of Remuneration Regulations;
- estimated increase in the base for benefits calculations until the employee reaches retirement age;
- percentage ratio depending on the employee's number of years in service (in accordance with the provisions of Remuneration Regulations).

The calculated amount is discounted at year-end based on actuarial calculations. The financial discounting rate to be used in the calculation of the present value of employee benefits payable has been established based on the market rates of return on T-bonds, whose currency and maturity are the same as the currency and estimated realization date of employee benefits payable. The discounted amount is decreased by the amount of mid-year/annual valuation allowance recognized to increase employee-related provisions.

The actuarial discount is calculated as the product of financial discount and the probability of a given person reaching retirement age as a Bank employee. The amount of annual allowance and the probability are calculated based on models, which take into account the following three types of risk:

- the possibility of an employee resigning from work;
- the risk of an employee's total incapacity to work;
- the risk of an employee's death.

The probability of an employee resigning from work is estimated using the probability distribution, whilst taking into account the Bank's statistical data. The probability of an employee resigning from work depends on his/her age and is constant during each year of service.

The risk of an employee's death was expressed in the form of the most recent statistical data from Polish Life Expectancy Tables for men and women, published by the Central Statistical Office, as at the date of valuation. The provision resulting from actuarial valuation is updated on a half-yearly basis.

The effect of changes in actuarial assumptions on the valuation of employee benefits is presented in other comprehensive income.

### 2.3.19 Provisions

Provisions represent liabilities with an uncertain settlement date or amount. The Bank records provisions, which are measured in accordance with IAS 37, Provisions, Contingent Liabilities and Contingent Assets, when an entity has a current (legal or constructive) obligation resulting from past events and it is probable that settling the obligation will result in the need of an outflow of resources embodying economic benefits and the amount of the obligation can be reliably estimated. A provision is not recorded when these conditions are not met.

### 2.3.20 Equity

Equity comprises share capital, supplementary capital, revaluation reserve, other capital (including share-based employee benefits reserve), net profit/loss for the year and retained earnings/accumulated losses.

#### **Share capital**

Share capital is shown at the nominal value in accordance with the Articles of Association and entry in the National Court Register.

#### **Supplementary capital**

Supplementary capital is created out of profit appropriations on the basis of resolutions of the General Meeting. Supplementary capital also includes share premium, less issue costs. Supplementary capital is earmarked for offsetting balance sheet losses that may arise in connection with the Bank's operations.

#### **Revaluation reserve**

The revaluation reserve is created on the valuation of:

- financial instruments classified as available for sale;
- the effective portion of cash flow hedges.

The revaluation reserve includes charges related to deferred tax on the valuation of financial instruments classified as available for sale and valuation of the effective portion of cash flow hedges. The revaluation reserve is not subject to distribution.

#### **Other reserves**

Other reserves are created out of profit appropriations. They are earmarked for the purposes specified in the Bank's Articles of Association and in the provisions of the law.

#### **Net profit/loss for the year and retained earnings/accumulated losses**

The net profit/loss attributable to the parent company is the profit/loss before tax per the income statement for the year adjusted for income tax expense and profit/loss attributable to non-controlling interests.

#### **Non-controlling interests**

Non-controlling interests represent the portion of capital and reserves in a subsidiary which cannot be directly or indirectly attributed to the parent company.

## Dividends

Dividend for a given financial year which had been approved by the General Shareholders' Meeting but not yet paid up to the balance sheet date is disclosed as Dividend payable in other liabilities.

### 2.3.21 Net profit/loss

The Bank records all significant cost and income items on an accruals basis, in line with the principles of matching income and expenses, recognition and measurement of assets and liabilities and recording impairment losses.

## Net interest income

Interest income and expense comprise interest on financial instruments measured at amortized cost and instruments measured at fair value, including hedging derivatives, except for derivatives classified as held for trading, other than IRS/CIRS. Included in net interest income are also fees and commissions relating directly to origination of financial instruments (both income, inclusive of part of the insurance commission, and expense, including internal incremental costs) which are an integral part of the effective interest rate.

The effective interest rate method is a method of calculating the amortized cost of a financial asset or a financial liability and of allocating the interest income and interest expense. The effective interest rate is the rate that discounts the estimated future cash flows to the net carrying amount of the component of asset or financial liability. For financial assets or a group of similar financial assets for which an impairment loss has been recorded, interest income is accrued on the present value of the amounts due (less impairment losses), using the current interest rate applied for discounting future cash flows for the purpose of estimating impairment loss.

## Fee and commission income and expenses

Fee and commission income is generally recognized on an accruals basis when the service has been provided. It arises as a result of rendering financial services offered by the Bank. Fees and commission relating directly to origination of financial assets or liabilities (both income and expense) which are not an integral part of the effective interest rate are taken to the income statement on a straight-line basis and presented as commission income or expense. Other fees and commission (which are not an integral part of the effective interest rate and which are not amortized on a straight-line basis), relating to financial services offered by the Bank, such as cash management, brokerage services, investment advisory services, financial planning, investment banking and asset management services, are recognized in the income statement at the time the given service has been rendered (provided that they are rendered regularly).

## Bancassurance

The Bank allocates income obtained from the distribution of insurance products offered together with loan products in accordance with the economic substance of the transaction as:

1. an integral part of the income from offered financial instruments;
2. a fee for agency services;
3. a fee for the provision of additional services performed in the course of an insurance contract (deferred by the Bank over the period in which the services are provided).

The economic substance of income determines the method of its recognition in the Bank's books of account.

The "relative fair value" model is used to determine the method of allocation of the income on insurance offered together with cash and mortgage loans and insurance sold without association with financial instruments.

The "relative fair value" model is used to determine the method of allocation of the income on insurance offered together with cash and mortgage loans.

The "relative fair value model" adopted by the Bank consists of estimating fair values of the individual components of the aggregate loan sale service, including insurance, in order to determine the proportion of both services' fair values and then allocating the fair value of fee income from the entire loan and insurance transaction to the individual components. Additionally, in order to determine the correct amount of income to be deferred into interest income, the model provides for recording and updating a provision for returns of insurance mediation in the event of the Customer resigning from the insurance. The provision will be periodically verified for each of the loan product groups due to uncertainty related to the possibility of the Customer resigning from the insurance cover at any time during the contract. The Bank's insurance commission is reduced by the amount of uncertain income related to estimated returns due to a Customer's resignation from insurance.

The insurance commission in respect of insurance products offered to the Bank's Customers in association with loan products in accordance with the "relative fair value model" (which is periodically updated) is recognized after deducting a part of the commission for covering expected returns of commission due to customer resignation or termination of insurance.

The Bank also recognizes in the income statement income from sales of insurance distributed together with car loans and loans with legal cover insurance, which is deferred in the full amount at the effective interest rate.

Additionally, the Bank enables Customers to avail themselves of insurance cover for products other than those related to the sale of loan products, including accident, health and investment (insured equity funds) insurance. Income from the above is recognized as follows:

- insurance products based on monthly settlements both with the insurer and the Customers are recognized in the income statement on a monthly basis;
- from the sale of insurance not related to the sale of banking products, including: Unit Linked and Insurance with Equity Fund, is recognized on a one-off basis in the income statement at the moment of concluding the transaction in the part relating to the sale intermediation service provided, and deferred on the straight-line basis. As in the case of insurance products linked to loans, the model for insurance that is not linked also takes into account creating and updating of provisions for returns of commission due to customers resigning from insurance.

### **Net gain realized on other financial instruments**

The realized result on other financial instruments includes gains and losses on disposal of financial instruments classified as available for sale, and gains and losses on the redemption of own issue.

### **Trading result**

The trading result includes results on: foreign currency transactions, interest rate transactions, over hedge and other instruments. The result on foreign exchange transactions includes the

results on: Forex, swap (FX swap and CIRS with equity conversion), FX forward, currency options and the revaluation of assets and liabilities expressed in foreign currencies. The result on interest rate transactions includes interest rate swaps, FRA and result on interest rate options (cap/floor). It does not comprise interest income and expense on IRS and CIRS transactions. The result on other financial instruments is the result on commodity derivatives (including forwards and futures), the result on options for exchange indices, index baskets and commodities and the result on trading in equity securities.

### **Other operating income and expenses**

Other operating income and expenses are costs and income not directly related to the Bank's core activities. Other operating income comprises mainly income from third party asset management, compensation, penalties and fines received, fees from contracts with sundry business partners and reimbursement of the costs of making claims. Other operating expenses comprise mainly costs of operating risk, making claims, and managing third party assets. Other operating income also includes gains from bargain purchases arising on the settlement of an acquisition of a business in accordance with IFRS 3.

Income received is recognized in the income statement on a one-off basis. In the case of income from managing third party assets, one-off recognition in the income statement depends on the monthly settlement.

### **2.3.22 Taxation**

Corporate income tax comprises current and deferred tax. Income tax is recognized in the income statement, apart from those situations in which it is recorded in equity.

#### **Current income tax**

Liabilities (receivables) in respect of current corporate income tax for the current and prior periods are measured at the amounts of the expected payment to the tax authorities (subject to reimbursement from the tax authorities) in accordance with the tax rates and tax regulations which were legally and actually binding as at the end of the reporting period.

#### **Deferred tax**

Deferred tax is calculated in accordance with the liabilities method based on the identification of timing differences between the tax and balance sheet values of assets and liabilities. The Bank records deferred tax provisions in respect of all taxable temporary differences, except for:

- situations in which a deferred tax provision arises as a result of initial recognition of goodwill or initial recognition of an asset or a liability in a transaction not being a business combination, which at the moment of its conclusion does not affect either profit (loss) before tax or taxable income or tax loss;
- when the parent company, investor or partner in a joint venture are able to control the dates of reversal of the temporary differences, and it is probable that the temporary differences will not reverse in the foreseeable future.

A deferred tax asset is recorded in respect of all deductible temporary differences in the amount to which it is probable that sufficient taxable income will be earned in the future to enable the realization of the deductible differences, except for:

- situations in which a deferred tax asset arises as a result of initial recognition of an asset or a liability in a transaction not being a business combination, which at the moment of its conclusion does not affect either profit (loss) before tax or taxable income or tax loss;
- when the deductible temporary differences arise from investments in subsidiaries, branches, associates and interests in joint ventures outside where it is improbable that they will reverse in the foreseeable future and taxable income will be generated against which the temporary differences can be deducted.

The carrying amount of the deferred tax asset is verified as at the end of each reporting period. The Bank reduces its carrying amount up to the amount to which it is probable that sufficient taxable income will be generated to enable its partial or complete realization. Previously unrecorded deferred income tax assets are recognized only to the extent to which it is probable that the taxable income generated in the future would enable their realization.

Deferred income tax assets and provisions are measured using the tax rates, which according to expectations will be applicable in the year in which the asset is realized or the provision released, determined on the basis of tax rates (and tax provisions) legally or factually binding as at the end of the reporting period.

The current and deferred income tax is recorded directly in equity when it relates to items which were recorded in equity in the same or a different reporting period.

Deferred income tax assets and provisions are offset when and only when the Bank has a legally enforceable right to offset current tax assets against current tax liabilities and when the deferred income taxes relate to the same taxpayer and the same fiscal authority.

### 2.3.23 Combinations of entities under common control

The purchase method of accounting is used for all business combinations (except to entities under common control), regardless of whether the purchased shares, interests and other net assets meet the definition of a business unit.

The acquisition of subsidiaries by the Bank are accounted for using the acquisition method in accordance with IFRS 3 according to which: recognized separately from goodwill, the identifiable assets acquired, the liabilities assumed and any non-controlling interest in the acquiree. Investments in subsidiaries and associates are measured at cost less accumulated impairment losses.

The purchase price of the business entity provides:

- the fair value of the assets given;
- liabilities presented to the former owners of the business;
- issued by the parent company share capital;
- the fair value of any assets and liabilities arising from contingent payments;
- the fair value of shares previously reported in the subsidiary.

Identifiable assets acquired and liabilities assumed are measured at their fair values at the acquisition date. For each business combination, any non-controlling interest in the acquired entity are measured at fair value or at the proportionate share of the identifiable net assets

of the acquired entity. The expenses associated with the acquisition are recognised in the profit when incurred.

Goodwill is recognized at the acquisition date measured as the excess of the sum of:

- the consideration transferred measured at fair value at the acquisition date;
- the amount of any non-controlling interest in the acquire;
- in the case of a merger carried out in stages, the fair value at the acquisition date of the share capital of the acquiree previously held by the Bank, over the net amount, determined at the acquisition date, the identifiable assets acquired and liabilities assumed at fair value at the acquisition date. In the opposite case the difference is recognized directly in the income statement as a gain from the occasional purchase.

Contingent payments are recognized as financial liabilities or equity. Financial liabilities in this respect are valued at their fair value and the change in this value is recognized in financial result.

Transactions under common control are excluded from IFRS 3. according to accounting policy adopted by the Bank with respect to IAS8 point 10, the settlement of the merger under common control accounting rule is the use of so-called "predecessor value" method ("predecessor accounting"), which is the recognition of the acquired of assets and liabilities recognized in the consolidated financial statements of the senior management, including the goodwill arising on acquisition of the unit.

## 2.4 Changes in accounting policies

### **Changes in accounting standards**

The accounting policies adopted in the preparation of the financial statements are consistent with the accounting policies applied in the preparation of the financial statements for the financial year ended 31 December 2015, except for the following amendments to standards and new interpretations binding for IFRS financial statements prepared for the annual periods starting on or after 1 January 2016:

- Annual IFRS Improvements 2010 – 2012

In December 2013, the International Accounting Standards Board published the Annual Improvements to IFRS 2010-2012 which affect 7 standards. In the course of the cycle, amendments to the following standards were introduced: to IFRS 2 as regards changing the definitions of "vesting conditions" and "market condition", and adding the definitions of "service condition" and "performance condition"; to IFRS 3 as regards clarifying the classification of contingent consideration by the acquirer; to IFRS 8 as regards the requirement to disclose information on the judgements made by management in applying the criteria for aggregating operating segments and disclosing the reconciliation of the sum of assets of the reporting segments to the total assets; to IFRS 13 as regards clarifying the doubts concerning the possibility of simplified valuation of short-term receivables and liabilities disregarding the discounting effect where the effect of non-discounting is immaterial, IAS 16 and IAS 38 as regards proportionate restatement of accumulated depreciation/amortization of property, plant and equipment or intangible assets when such assets are subject to revaluation; amendments to IAS 24 relating to the identification of related entities which provide key management personnel services to the reporting entity or the parent company.

The above improvements do not significantly affect the financial statements of the Bank.

- Amendments to IAS 19, Defined Benefit Plans: Employee Contributions.

The standard was published by the International Accounting Standards Board on 21 November 2013 and endorsed by the European Union on 17 December 2014. It is binding for annual periods starting on or after 1 July 2014, and in the European Union it is binding at the latest for annual periods starting on or after 1 February 2015. The amendment to the standard is only related to contributions towards defined benefit plans paid by the employees or third parties. The purpose of the amendment to the standard is to clarify and simplify the accounting requirements concerning contributions independent of the employees' employment period, i.e. contributions constituting a fixed percentage of salary, a fixed amount during the period of employment and contributions dependent on an employee's age. According to the amendment, such contributions should be recorded as a reduction in the cost of employment in the period in which an employee performs work, instead of allocating the contributions to the employment periods.

The Bank believes that the application of this amended standard will not have a significant effect on the financial statements in the period of its first application.

- Annual IFRS Improvements 2012 – 2014

They were published by the International Accounting Standards Board on 25 September 2014 and endorsed by the European Union on 15 December 2015. They are binding for annual periods starting on or after 1 January 2016. In the course of the cycle, amendments to four standards were introduced: IFRS 5 in a situation in which an asset is reclassified from "held for sale" to "held for distribution to owners" or vice versa, this does not constitute a change in the plan of disposal or distribution, therefore, the former requirements concerning classification will not change. Additionally, when assets no longer meet the criterion of held for distribution to owners nor do they meet the criteria for being held for sale, the entity should cease to apply the principles binding for assets held for distribution as it ceases to apply these principles when the assets no longer meet the criteria for being held for sale; IFRS 7 as regards the disclosures to be made when the entity transfers a financial asset to a third party, while retaining the right to service that asset for a fee that is included in a service contract, whether the service contract constitutes continuing involvement in the transferred asset. Moreover, IFRS 7 explains that disclosures relating to the offsetting of financial assets and liabilities are not required for all interim periods, unless it is required by IAS 34 and IAS 19 to explain that high quality corporate bonds used for estimating the discount rate of liabilities in respect of post-employment benefits should be issued in the same currency as the said liabilities. Thus, an assessment of whether there is a developed market for such corporate bonds should be made at the level of a specific currency and not a given country; IAS 34 as regards clarifying the meaning of reference to information disclosed "elsewhere in the interim financial report" and additionally introduces a requirement of including a reference in the interim financial report to another report in which the information is contained.

The Bank believes that the application of these amended standards will not have a significant effect on the financial statements in the period of their first application.

- Amendments to IFRS 11, Acquisition of an Interest in a Joint Operation

The standard was published by the International Accounting Standards Board on 6 May 2014 and endorsed by the European Union on 24 November 2015. It is binding for annual periods starting on or after 1 January 2016. The amended standard introduces a requirement that when accounting for purchases of shares in a joint operation in which the joint operation is a business as defined in IFRS 3, Business Combinations, an entity must apply all the principles of accounting for business combinations contained in IFRS 3 and in other standards, except for those principles that are contrary to the guidance included in this IFRS standard. This method of recognition shall apply not only on initial acquisition of shares but also on acquisitions of additional shares in a joint operation. Moreover, the acquirer of shares in a joint operation is obliged to disclose information required by IFRS 3 and other standards with respect to business combinations.

The Bank believes that the application of this amended standard will not have a significant effect on the financial statements in the period of its first application.

- Amendments to IAS 16 and IAS 41, Agriculture: Bearer Plants

The amendments were published by the International Accounting Standards Board on 30 June 2014 and endorsed by the European Union on 23 November 2015. They are binding for annual periods starting on or after 1 January 2016. The amended standards IAS 16 and IAS 41 introduce the requirement of recording bearer plants in the same way as property, plant and equipment items and apply to them the regulations of IAS 16 measuring them at cost or revalued amount. Agricultural products produced by bearer plants will continue to be measured at fair value less costs to sell in accordance with IAS 41. Farm animals are not covered by the amendments.

The Bank believes that the application of these amended standards will not have a significant effect on the financial statements in the period of their first application.

- Amendments to IAS 16 and to IAS 38, Acceptable methods of depreciation and amortization

They have been published by the International Accounting Standards Board on 12 May 2014 and endorsed by the European Union on 2 December 2015. They are binding for annual periods starting on or after 1 January 2016.

The amended IAS 16 prohibits the application of the revenue-based depreciation method for property, plant and equipment. Applying the revenue-based depreciation method is not appropriate because revenue generated from operations in which a given asset is used reflects factors other than the consumption of economic benefits generated by the asset. The amended standard IAS 38 introduces an assumption that the revenue-based amortization method of intangible assets is inappropriate for the same reasons as in the case of property, plant and equipment, presented in the amendments to IAS 16. However, in the case of the amended IAS 38 standard the assumption can be rebutted in two instances: if it can be shown that revenue from a given asset is strongly correlated to the consumption of economic benefits contained in these assets and if a given intangible asset is expressed as a right to obtain a specific amount of revenue.

The Bank believes that the application of these amended standards will not have a significant effect on the financial statements in the period of their first application.

- Amendments to IAS 27, Equity method in separate financial statements

They have been published by the International Accounting Standards Board on 12 August 2014 and endorsed by the European Union on 18 December 2015. They are binding for annual periods starting on or after 1 January 2016. The amended standard IAS 27 restores the possibility of applying the equity accounting method in recording investments in subsidiaries, joint ventures and associates in separate financial statements. The entity may now record investments in subsidiaries, joint ventures and associates in its separate financial statements at cost or in accordance with IFRS 9, or under the equity accounting method as described in IAS 28. Dividend from subsidiaries, associates and joint ventures is recorded in the income statement or as an adjustment of the present value of the investment when the investment is recorded using the equity accounting method.

The Bank believes that the application of this amended standard will not have a significant effect on the financial statements in the period of its first application.

- Amendments to IFRS 10, IFRS 12 and IAS 28, Investment Entities: Applying the Consolidation Exception

They were published by the International Accounting Standards Board on 18 December 2014 and are effective for annual periods starting on or after 1 January 2016.

The amendments to IFRS 10, IFRS 12 and IAS 28 release the entity from the requirement of preparing consolidated financial statements of the parent company if the medium or ultimate level parent company prepares IFRS financial statements available to the public, in which subsidiaries are consolidated or measured to fair value through profit or loss. Additionally, the consolidation requirement was limited to a situation where the investment entity has a subsidiary which is not an investment entity itself and the main objective of which is to provide services related to investment activities of the parent company. Moreover, when applying the equity method in an associate or a joint venture which is an investment entity, the investor may continue to apply fair value measurement which the associate or a joint venture had applied to its own subsidiaries.

The Bank believes that the application of these amended standards will not have a significant effect on the financial statements in the period of their first application.

- Amendments to IAS 1, Disclosure Initiative

They were published by the International Accounting Standards Board on 18 December 2014 and endorsed by the European Union on 18 December 2015. They are binding for annual periods starting on or after 1 January 2016. Amendments to IAS 1 comprise clarifications concerning the materiality of information, especially taking into account limiting of immaterial information in the financial statements. Moreover, specific financial statement items may be subject both to aggregation and disaggregation in the financial statements, depending on their materiality. IAS 1 was also supplemented for requirements concerning the presentation of subtotals in the financial statements. Additionally, information disclosed in the notes to the financial statements may be presented in a sequence established by the entity, however, when determining the sequence of presentation in the notes, the entity should take into account the clarity and comparability of information in the financial statements. The amendments to IAS 1 have also removed guidance concerning the identification of significant areas of the accounting policies.

The Bank believes that the application of this amended standard will not have a significant effect on the financial statements in the period of its first application.

### **New standards and interpretations, which have been published but not yet effective as at the balance sheet date**

- Amendments to IAS 7: Disclosure Initiative

They were published by the International Accounting Standards Board on 29 January 2016 and are effective for annual periods starting on or after 1 January 2017. The amendments to IAS 7 introduce the requirement of disclosing changes in liabilities arising from financing activities in the statement of cash flows, including both changes arising from cash flows and non-cash changes. To satisfy the requirement, the standard prescribes reconciliation of the opening and closing balances of the individual liabilities presented in the statement of financial position which qualify as financing activities in the statement of cash flows.

The Bank believes that the application of this amended standard will not have a significant effect on the financial statements in the period of its first application.

- IFRS 9, Financial Instruments

On 24 July 2014, the International Accounting Standards Board (IASB) published a new International Financial Reporting Standard – IFRS 9, Financial Instruments, binding for annual periods starting on or after 1 January 2018, which will replace the existing International Accounting Standard 39, Financial Instruments: Recognition and Measurement. By Regulation no. 2016/2067 of 22 November 2016, the European Commission adopted the International Financial Reporting Standard 9, Financial Instruments (IFRS 9) in the version published by IASB on 24 July 2014.

IFRS 9 introduces a new financial asset impairment model based on the "expected loss" concept, changes in the principles of classification and measurement of financial instruments (in particular financial assets) and a new approach to hedge accounting.

In March 2016, the Bank began the project of implementing IFRS 9, actively involving the Bank's business units responsible for the areas of accounting, financial reporting and risk management, and business, IT and organizational departments.

The Bank is at the stage of designing necessary solutions for the individual requirements based on the results of a gap analysis and general methodological assumptions adopted. The Bank plans to complete the design works by the end of the third quarter of 2017.

### **Summary of key principles contained in IFRS 9**

Classification and measurement of financial instruments

#### **Financial assets**

According to IFRS 9, upon initial recognition, financial assets are classified to the following measurement categories:

- 1.financial assets measured at amortized cost;
- 2.financial assets measured at fair value through other comprehensive income;
- 3.financial assets measured at fair value through profit or loss.

Financial assets are classified to one of the above measurement categories upon initial recognition in the balance sheet based on:

- 1.the Bank's business model for financial asset management which is defined on a level reflecting the methods of managing groups of financial assets in aggregate in order to achieve a specific business objective; and
- 2.characteristics of contractual cash flows from a financial asset aimed at verifying whether the contractual terms result in cash flows arising on specific dates, which are solely payments of principal and interest (SPPI criterion).

Financial assets measured at amortized cost are financial assets which meet the two conditions below, unless the Bank has designated them as measured at fair value through profit or loss:

- 1.financial asset is held in line with a business model the objective of which is holding financial assets for the purpose of obtaining contractual cash flows; and
- 2.the contractual terms relating to a given financial asset give rise to cash flows on specific dates which constitute solely payments of principal and interest.

Financial assets measured at fair value through other comprehensive income are financial assets which meet the two conditions below, unless the Bank has designated them as measured at fair value through profit or loss:

- 1.financial asset is held in line with a business model the objective of which is both holding financial assets for the purpose of obtaining contractual cash flows and selling financial assets (the sale is an integral part of the business model); and
- 2.the contractual terms relating to a given financial asset give rise to cash flows on specific dates which constitute solely payments of principal and interest.

Financial assets measured at fair value through profit or loss are assets which:

- 1.do not meet the criteria for classifying them as measured at amortized cost or at fair value through other comprehensive income (the business model for managing these assets is based on fair value changes or the contractual terms give rise to cash flows on specific dates which do not constitute solely payments of principal and interest);
- 2.they have been designated to this category by the Bank's decision upon initial recognition and the designation of a financial asset to the category of measured at fair value through profit or loss upon initial recognition is irrevocable and only possible when through this the Bank eliminates or significantly reduces the measurement or recognition mismatch ("the accounting mismatch") which would otherwise arise on the valuation of assets or liabilities or recognition of the related profit or loss based on different principles.

Upon initial recognition, the entity should analyse whether a given instrument contains an embedded derivative. A derivative instrument embedded in a hybrid contract where the host contract is a financial asset covered by the scope of IFRS 9 is not separated, and the entire hybrid contract is recognized in line with IFRS 9 requirements relating to the classification of financial assets. Whereas, a derivative instrument embedded in a hybrid contract where the host contract is not a financial asset covered by the scope of IFRS 9, should be assessed to establish whether it should be separated.

Financial assets can be reclassified only when the Bank changes the business model of managing financial assets. In such instance, the assets which were affected by the change of the business model are subject to reclassification.

### **Financial liabilities**

IFRS 9 does not introduce any significant changes in the classification and measurement of financial liabilities compared with the principles introduced by IAS 39 – financial liabilities are classified to the following categories upon their acquisition or origination:

1. financial liabilities measured at fair value through profit or loss;

2. other financial liabilities (stated at amortized cost).

Moreover, according to IFRS 9, financial liabilities cannot be reclassified.

### **Impairment**

IFRS 9 replaces the impairment model introduced by the provisions of IAS 39 which is based on the "incurred loss" concept, and introduces a new model based on the expected credit loss (ECL) concept. The direct consequence of this change will be the need to calculate impairment losses based on expected credit losses and take into account forecasts and expected future economic conditions in the context of credit risk assessment of the loan exposure, which was not permitted under IAS 39.

The new impairment model will apply to financial assets classified, in accordance with the provisions of IFRS 9, as financial assets measured at amortized cost or at fair value through other comprehensive income, with the exception of equity instruments.

The change in the incurred loss concept (IAS 39) to the expected loss concept will have far reaching consequences for the modelling of the credit risk parameters and the final amount of allowances recorded. The currently applied Loss Identification Period will no longer be used and with it the category of Incurred But Not Reported losses (IBNR) will be eliminated. According to IFRS 9 instead of the IBNR allowances and allowances for non-performing exposures, impairment losses will be established in the following categories:

1. Bucket one – 12-month expected credit loss – the expected credit loss which will arise from the possible events of default within 12 months from the reporting date;
2. Buckets two and three –expected credit loss over the full lifetime of a financial asset – the expected loss which will arise from all the possible events of default over the expected lifetime of a financial asset.

The measurement of the expected credit loss over the lifetime of a financial asset will apply to all exposures in the case of which from the moment of their initial recognition until the balance sheet date a considerable increase in credit risk was identified (Bucket two) or impairment was identified (Bucket three). In bucket one, the measurement of the 12-month expected credit loss will be performed for all exposures in the case of which no significant increase in credit risk and no impairment were identified from the date of their initial recognition until the balance sheet date.

The calculation of impairment of financial assets will also affect the recognition of interest income. In particular, under the general approach, income from assets classified to buckets 1 and 2 will be established based on the gross exposure, whereas in the case of bucket 3 it will be established on a net basis (as in the case of assets with identified impairment under IAS 39).

### **Hedge accounting**

In accordance with the provisions of IFRS 9, the Bank may, solely on the date of implementing IFRS 9, make a decision constituting an element of its accounting policy to continue applying hedge accounting requirements in line with IAS 39, instead of the requirements provided in IFRS 9.

IFRS 9 requires that the Bank should ensure the consistency of the relevant hedge relationships with the risk management strategy adopted by the Bank and its objectives. IFRS 9 introduces new provisions concerning, among other things, evaluating the effectiveness of the hedging relationship and the mechanism for restoring the balance of the hedging relationship (rebalancing of a hedging relationship), and it also eliminates the possibility of ceasing to apply hedge accounting based on the Bank's subjective decision

(i.e. when there are no circumstances justifying ceasing to apply hedge accounting, as defined in the Standard).

### **Potential effect of IFRS 9 on the Bank's financial standing and equity**

1. Quantitative estimations of the effect of IFRS 9 on the Bank's financial standing and equity

As at 31 December 2016, the aggregate effect of implementing the requirements of IFRS 9 on the Bank's financial standing and equity cannot be estimated. In the Bank's opinion, the disclosure of quantitative data which do not reflect the potential effect of all the aspects of IFRS 9 on the Bank's financial standing and equity may have a negative effect on the information value of the financial statements for their recipients. In view of the above, the Bank decided only to disclose qualitative information concerning the Bank's approach to implementing the requirements of IFRS 9, which in the Bank's opinion will enable the recipients of the financial statements to obtain an understanding of the effect of IFRS 9 on the Bank's financial position and capital management.

2. The qualitative data enabling the recipients of the financial statements to assess the effect of IFRS 9 on the Banks financial position and capital management

### **Classification and measurement of financial instruments**

#### **Financial assets**

In order to ensure the possibility of making classification decisions in respect of the financial assets held by the Bank in line with IFRS 9 as at 1 January 2018, as part of the IFRS 9 implementation project the Bank performs a review of its financial assets which will be in its possession after 31 December 2017, by:

1. identifying and allocating groups of financial assets to appropriate business models based on an assessment of the adopted approach to the management of financial asset portfolios performed, among other things, by:
  - a) reviewing and evaluating significant and objective qualitative data affecting the allocation of the asset portfolios to the relevant business models (such as, for example: the method of evaluating yield from the portfolios of financial assets and the method of reporting the results of such evaluation to the Bank's key management, analysing the types of risk affecting the effectiveness of the financial asset portfolios and ways of managing the identified risks, the rules of rewarding the managers of financial asset portfolios and reasons for sales of financial assets from a given portfolio made in the past);
  - b) reviewing and evaluating significant and objective quantitative data affecting the allocation of the asset portfolios to the relevant business models (such as, for example: value of sales of financial assets made as part of the portfolios in previous reporting periods (if there were such sales) and the frequency of sales of financial assets made as part of the portfolios (if there were such sales);
  - c) analysis of expectations as to the planned future value of sales of financial assets and their frequency as part of the portfolios;
2. determining, through identification and analysis of the contractual provisions of a financial asset which may result in the financial asset's failure to meet the SPPI criterion,

whether the contractual terms of the financial asset (that is held in accordance with the business model the objective of which assumes holding financial assets in order to obtain contractual cash flows, or held in accordance with the business model the objective of which assumes both holding the financial asset to obtain contractual cash flows and selling the financial asset) enable concluding that a given financial asset meets the SPPI criterion.

As a result of implementing the IFRS 9 requirements, the Bank anticipates changes in the classification of some loans and advances to customers measured at amortized cost in accordance with IAS 39, which will have to be measured at fair value through profit or loss due to their failure to fulfil the SPPI criterion.

The quantitative data relating to the effect of the above change in the classification of loans on the Bank's results of operations and equity can only be estimated on completing work on the fair value measurement model for these instruments, however, based on the current information, the Bank does not anticipate that the said change in their classification should have a significant effect on the results of operations and level of equity.

As at 31 December 2016, the Bank has equity instruments (shares) which are classified as "available-for-sale financial assets" according to IAS 39. In the case of these assets, upon initial recognition the Bank will be able to classify them to financial assets measured at fair value through profit or loss (unless according to the intention of the entities managing them they constitute a strategic investment) or to make an irrevocable choice of recognizing them at fair value through other comprehensive income. If the Bank elects to recognize equity instruments at fair value through other comprehensive income, the result of the fair value measurement will be recognized in other comprehensive income, the impairment loss will not be recognized in the income statement and on their sale the gain or loss will not be taken to the income statement. As at the moment of preparing the financial statements, the Bank had not made a decision in this scope.

### **Financial liabilities**

As a result of implementing the requirements of IFRS 9, the Bank does not anticipate any changes in the classification of financial liabilities compared with the current classification according to IAS 39 that could have a significant effect on the Bank's balance sheet and/or results.

### **Impairment**

The Bank assumes that implementing the new impairment model based on the ECL concept will affect the amount of impairment allowances at the Bank, especially as regards exposures classified to bucket 2. IFRS 9, contrary to IAS 39, does not require identifying indications of impairment in order to estimate losses in the lifetime horizon in bucket 2. Instead, the Bank is obliged to continually estimate the amount of credit losses from the moment of recognizing a given asset until its derecognition. In the event of a significant increase in credit risk compared with the moment of recognizing a given asset in the balance sheet, it is necessary to calculate the losses over the lifetime horizon – bucket 2. Such an approach will result in recognizing the expected credit losses earlier, which will eventually translate into increasing the amount of the allowances and thus ultimately affect the results. It should be emphasized that as at the moment of implementing IFRS 9, the one-off change arising from adopting the new models will not be taken to profit or loss but will be recorded in the revaluation reserve.

As part of the IFRS 9 implementation project, the Bank is working on implementing the new methodology of calculating allowances and on implementing the relevant changes in the IT systems and processes operating in the Bank, in particular on the assumptions of the impairment model, obtaining the required data and designing the process and tool and performing a detailed estimate of the effect of IFRS 9 requirements on the amount of allowances. The methodology-related works focus on expanding the currently applied solutions and on implementing completely new elements. The works on expanding the solutions comprise adapting the current PD, LGD, EAD and CCF models so that they can be used for estimating expected losses. As regards new solutions, the works mainly comprise developing the criteria for transfers between the buckets and taking economic forecasts into account when estimating the allowance amounts.

In the Bank's opinion, implementing the new standards requires applying credit risk assessment models with a higher level of complexity and better possibilities of prediction that require a considerably wider range of data compared with the currently used models.

An assessment of the effect of the new standard on the Bank's financial standing and capital management is quite difficult at present. The difficulties arise from the fact that methodology-related works are in progress with respect to adapting the credit risk models to the requirements of the new standard, as well as a lack of clear cut interpretations of the new provisions and a common market practice. On the legislative level, the supervisory authorities and regulatory bodies are working on updating the prudential requirements, which will be binding for the Bank. These works are at an early stage, therefore, the effect of IFRS 9 on the Bank's financial standing and capital adequacy ratios cannot be clearly determined.

### **Hedge accounting**

On 1 January 2018, the Bank intends to make a decision on transferring to IFRS 9 as regards hedge accounting. Bank estimates that the impact on the Bank will not be significant.

- Amendments to IAS 12, Recognition of Deferred Tax Assets for Unrealized Losses

They were published by the International Accounting Standards Board on 19 January 2016 and are effective for annual periods starting on or after 1 January 2017. The amendments to IAS 12 clarify the requirements for recognizing deferred tax assets on unrealized losses on debt instruments measured at fair value. The amendments introduce guidance on the identification of deductible temporary differences. In particular, the standard confirms that a decrease below cost in the carrying amount of debt instruments with a fixed interest rate measured at fair value the tax base of which remains on the level of their cost, results in deductible temporary differences arising regardless of whether the instrument holder intends to hold it or sell it.

The Bank believes that the application of this amended standard will not have a significant effect on the financial statements in the period of its first application.

- Amendments to IFRS 2, Share-based Payment

The amendment introduces, among other things, guidance on the fair value measurement of liabilities related to share-based payments settled in cash, guidance on changing the

classification of share-based transactions settled in cash to share-based transactions settled in equity instruments and guidance on recognizing employees' taxation liabilities in respect of share-based transactions. The amendment will apply to financial statements prepared after 1 January 2018.

- IFRS 15, Revenue from Contracts with Customers

The standard applies to annual periods starting on or after 1 January 2018 – by the date of approving these financial statements, not endorsed by the EU.

The principles set out in IFRS 15 will apply to all contracts resulting in revenue. The new standard introduces the core principle that revenue must be recognized when the goods or services are transferred to the customer, at the transaction price. Any bundled goods or services that are distinct must be separately recognized, and any discounts or rebates on the transaction price must generally be allocated to the separate elements. When the value of revenues varies for any reason, under the new standard the variable amounts must be recognized as revenues providing that it is highly probable that the recognition of the revenues will not be reversed in the future as a result of remeasurement. Additionally, according to IFRS 15 costs incurred to secure contracts with customers have to be capitalized and amortized over the period when the benefits of the contract are consumed.

The above amendments may result in changes in accounting for deferred revenue and will require additional disclosures in the financial statements.

- IAS 16, Leasing

The standard applies to annual periods starting on or after 1 January 2019 – by the date of approving these financial statements, not endorsed by the EU. The new standard sets the principles for recognition, measurement, presentation and disclosures concerning leases. All lease transactions result in the lessee obtaining the right to use an asset and a liability arising from the obligation to pay. Thus, IFRS 16 cancels the classification into operating and finance leases in accordance with IAS 17 and introduces one accounting model for leases on the part of the lessee. The lessee will be obliged to recognize: (a) assets and liabilities for all lease transactions concluded for a period of more than 12 months, except for situations when a given asset is of low value; and (b) depreciation of the leased asset separately from interest on the lease liability in the statement of profit or loss.

In the Bank's opinion, applying the new standard will not affect the recognition, presentation, measurement or disclosure of assets under operating leases and the corresponding liabilities in the financial statements of the Bank as a lessee.

- Amendments to IFRS 4, Insurance Contracts in the context of applying IFRS 9

The amendments apply to annual periods starting on 1 January 2018. The amendments address the issue of applying the new standard IFRS 9, Financial Instruments, before implementing the new standard concerning insurance operations on which the IASB is currently working. In order to prevent temporary fluctuations of results in connection with implementing IFRS 9, amendments to IFRS 4 introduce two acceptable approaches: overlay approach and deferral approach.

The amended standard allows:

- companies that issue insurance contracts to recognize in OCI rather than profit or loss, the volatility that may arise when IFRS 9 is applied before the forthcoming insurance contracts Standard is issued;
- temporary exemption from IFRS 9 until 2021 for companies whose predominant activity is related to insurance.

The companies which defer application of IFRS 9 will apply the currently binding IAS 39.

- Amendments to IAS 40, Investment Property

Applies to annual periods starting on 1 January 2018. The amendments clarify that transferring an asset to or from investment property requires change in use. The conclusion that there was a change in use must be based on evidence.

- IFRS Improvements 2014 – 2016

They apply to annual periods starting on 1 January 2018. Amendments are introduced to 3 standards: IFRS 1 as regards specifying short-term exemption for first-time adopters of IFRS within the scope of IFRS 7, IAS 19 and IFRS 10; IFRS 12 as regards clarifying the objective of the standard. The amendments shall apply retrospectively to annual periods starting on or after 1 January 2017; IAS 28 as regards measuring associates or joint ventures at effective fair value.

- IFRIC 22, Foreign Currency Transactions

This applies to annual periods starting on 1 January 2018. The IFRIC applies to foreign currency transactions or a part of these transactions when they are denominated or measured in foreign currencies. The interpretation provides guidance both for a single payment and for multiple payments made. The objective of the guidance is to reduce diversity in practice.

The following standards and interpretations have been published by the International Accounting Standards Board or the International Financial Reporting Interpretations Committee, but are not yet effective and will not have a significant effect on the Bank's financial statements:

- Amendments to IFRS 10 and IAS 28 concerning sales or contributions of assets between an investor and its associates or joint ventures

The amendments were published by the International Accounting Standards Board on 11 September 2014. Their effective date was postponed indefinitely by the Accounting Standards Board. The amendments to IFRS 10 and IAS 28 eliminate the existing inconsistency between the requirements of these standards and clarify the accounting treatment of loss of control over a subsidiary which has been contributed to an associate or a joint venture. The accounting treatment depends on whether the assets sold or contributed to an associate or a joint venture meet the definition of a business according to IFRS 3, Business Combinations. If the assets meet the definition of a business, the amendments introduce a requirement to recognize the full gain or loss on the transaction. When the transaction is related to assets which do not constitute a business, a partial gain or loss should be recognized up to the level of equity interest of other entities.

## 2.5 Changes in presentation

In relation to the published financial statements as of 31.12.2015 in this report changed the presentation of the assets pledged as collateral and extracted pledged assets. Extracting additional line clarifies and has no significant effect on the readability of this statement.

Were presented

Assets	As at 31.12.2015
Assets pledged as collateral	628 332

Actual

Assets	As at 31.12.2015
Assets pledged as collateral	628 332
incl pledged assets	576 534

### 3. Operating segments

The Bank divides its operations into the following reporting segments for the purpose of management accounting:

- retail segment;
- corporate segment;
- treasury activity;
- reconciling items.

The Bank provides services to retail (individual) and business customers, by offering them a full range of banking services.

The basic products for individual customers cover:

- loan products: cash loans, credit cards, overdraft facilities, housing loans;
- deposit products: term deposits, savings accounts;
- brokerage products and investment funds;
- personal accounts;
- transaction services: cash deposits and withdrawals, transfers;
- FX transactions.

Basic products for business customers include:

- loan products: overdraft facilities, working capital loans, investment loans, credit cards;
- deposit products: term deposits;
- current and auxiliary accounts;
- transaction services: cash deposits and withdrawals, transfers;
- treasury products: FX transactions (also at set date), derivatives.

The basic element of segment analysis is the profitability of the Retail Segment and Business Segment. The profitability includes:

- margin revenue less financing costs (a rate at which a branch makes settlements with the Treasury Department);
- commission income;
- income from treasury and foreign exchange transactions concluded by customers;
- other operating income and expenses.

Revenues of the retail segment also include revenues from the sale of brokerage products (such as revenues from maintaining brokerage accounts, agency services in trading in securities and revenue from the distribution of investment fund units).

Revenues of the business segment also include revenues from the sale of car loans.

The Treasury Activity segment covers the results on managing the global position – the liquidity and currency positions – arising from the activities of the Bank.

Reconciliation items include:

- internal net interest income/(expenses) calculated on net impairment losses;
- commission costs not allocated to business units (including cash management fees, ATM sharing commission, domestic and foreign transfers);
- other operating income and expenses not related directly to operating segments.

### Results and volumes by segments for the financial year ended 31 December 2016

Segment report	Retail customers	Corporate customers	Treasury	Total corporate segments	Reconciling items	Total Bank
<b>External interest income</b>	<b>1 299 671</b>	<b>546 502</b>	<b>93 684</b>	<b>1 939 857</b>	<b>2 017</b>	<b>1 941 874</b>
external income	1 640 530	1 190 069	101 242	2 931 841	2 017	2 933 858
external expense	-340 859	-643 567	-7 558	-991 984	0	-991 984
<b>Internal interest income</b>	<b>-43 001</b>	<b>-12 581</b>	<b>61 793</b>	<b>6 211</b>	<b>-6 211</b>	<b>0</b>
internal income	532 717	256 492	1 259 074	2 048 283	25	2 048 308
internal expense	-575 718	-269 073	-1 197 281	-2 042 072	-6 236	-2 048 308
<b>Net interest income</b>	<b>1 256 670</b>	<b>533 921</b>	<b>155 477</b>	<b>1 946 068</b>	<b>-4 194</b>	<b>1 941 874</b>
Fee and commission income	239 210	290 809	517	530 536	61 801	592 337
Fee and commission expense	-122 886	-56 587	-34 954	-214 427	-43 553	-257 980
<b>Net fee and commission income</b>	<b>116 324</b>	<b>234 222</b>	<b>-34 437</b>	<b>316 109</b>	<b>18 248</b>	<b>334 357</b>
<b>Dividend income</b>	<b>0</b>	<b>0</b>	<b>0</b>	<b>0</b>	<b>68</b>	<b>68</b>
<b>Trading result</b>	<b>3 885</b>	<b>53 031</b>	<b>262 863</b>	<b>319 779</b>	<b>0</b>	<b>319 779</b>
<b>Net gain (realized) on other financial instruments</b>	<b>105 447</b>	<b>133 596</b>	<b>-217 124</b>	<b>21 919</b>	<b>0</b>	<b>21 919</b>
Other operating income	138 825	17 551	5 161	161 537	-59 523	102 014
Other operating expenses	-13 859	-64	-1 686	-15 609	-36 111	-51 720
<b>Net other operating income</b>	<b>124 966</b>	<b>17 487</b>	<b>3 475</b>	<b>145 928</b>	<b>-95 634</b>	<b>50 294</b>
<b>Total result before impairment losses</b>	<b>1 607 292</b>	<b>972 257</b>	<b>170 254</b>	<b>2 749 803</b>	<b>-81 512</b>	<b>2 668 291</b>
<b>Impairment losses</b>	<b>-479 566</b>	<b>-288 937</b>	<b>0</b>	<b>-768 503</b>	<b>-26 232</b>	<b>-794 733</b>
<b>Total result after impairment losses</b>	<b>1 127 727</b>	<b>683 322</b>	<b>170 253</b>	<b>1 981 302</b>	<b>-107 744</b>	<b>1 873 558</b>
<b>Profit from acquisition of the demerged business of Bank BPH</b>	<b>0</b>	<b>0</b>	<b>0</b>	<b>0</b>	<b>508 056</b>	<b>508 056</b>
<b>General administrative expenses</b>	<b>-1 240 676</b>	<b>-429 420</b>	<b>-4 254</b>	<b>-1 674 350</b>	<b>1</b>	<b>-1 674 349</b>
<b>Profit before tax</b>	<b>-112 949</b>	<b>253 902</b>	<b>165 999</b>	<b>306 952</b>	<b>400 313</b>	<b>707 265</b>
<b>Income tax</b>	<b>0</b>	<b>0</b>	<b>0</b>	<b>0</b>	<b>-75 190</b>	<b>-75 190</b>
<b>Net profit (loss)</b>	<b>-112 949</b>	<b>253 902</b>	<b>165 999</b>	<b>306 952</b>	<b>325 123</b>	<b>632 075</b>
<b>Amortization/ depreciation</b>						<b>-101 832</b>
<b>Assets</b>	<b>36 446 241</b>	<b>24 205 092</b>	<b>37 145</b>	<b>60 688 478</b>	<b>523 371</b>	<b>61 211 849</b>
<b>Liabilities</b>	<b>34 664 532</b>	<b>20 302 076</b>	<b>9 253</b>	<b>54 975 861</b>	<b>13 125</b>	<b>54 988 986</b>

### Results and volumes by segments for the financial year ended 31 December 2015

Segment report	Retail customers	Corporate customers	Treasury	Total corporate segments	Reconciling items	Total Bank
<b>External interest income</b>	<b>967 638</b>	<b>390 823</b>	<b>138 235</b>	<b>1 496 696</b>	<b>0</b>	<b>1 496 696</b>
external income	1 279 821	594 203	521 144	2 395 168	0	2 395 168
external expense	-312 183	-203 380	-382 909	-898 472	0	-898 472
<b>Internal interest income</b>	<b>51 319</b>	<b>10 779</b>	<b>-22 766</b>	<b>39 332</b>	<b>-39 332</b>	<b>0</b>

internal income	444 880	229 092	958 435	1 632 407	-18 748	1 613 659
internal expense	-393 561	-218 313	-981 201	-1 593 075	-20 584	-1 613 659
<b>Net interest income</b>	<b>1 018 957</b>	<b>401 602</b>	<b>115 469</b>	<b>1 536 028</b>	<b>-39 332</b>	<b>1 496 696</b>
Fee and commission income	225 891	251 069	686	477 646	68 009	545 655
Fee and commission expense	-125 718	-42 208	-19 511	-187 437	-26 589	-214 026
<b>Net fee and commission income</b>	<b>100 173</b>	<b>208 861</b>	<b>-18 825</b>	<b>290 209</b>	<b>41 420</b>	<b>331 629</b>
<b>Dividend income</b>	<b>0</b>	<b>0</b>	<b>0</b>	<b>0</b>	<b>74</b>	<b>74</b>
<b>Trading result</b>	<b>-1 109</b>	<b>52 001</b>	<b>217 684</b>	<b>268 576</b>	<b>0</b>	<b>268 576</b>
<b>Net gain (realized) on other financial instruments</b>	<b>91 902</b>	<b>120 025</b>	<b>-199 004</b>	<b>12 923</b>	<b>0</b>	<b>12 923</b>
Other operating income	198 247	10 495	1 595	210 337	-130 845	79 492
Other operating expenses	-68 303	-216	-527	-69 046	38 831	-30 215
<b>Net other operating income</b>	<b>129 944</b>	<b>10 279</b>	<b>1 068</b>	<b>141 291</b>	<b>-92 014</b>	<b>49 277</b>
<b>Total result before impairment losses</b>	<b>1 339 867</b>	<b>792 768</b>	<b>116 391</b>	<b>2 249 026</b>	<b>-89 851</b>	<b>2 159 175</b>
<b>Impairment losses</b>	<b>-478 134</b>	<b>-169 018</b>	<b>0</b>	<b>-647 152</b>	<b>-24 620</b>	<b>-671 772</b>
<b>Total result after impairment losses</b>	<b>861 733</b>	<b>623 750</b>	<b>116 391</b>	<b>1 601 874</b>	<b>-114 471</b>	<b>1 487 403</b>
<b>General administrative expenses</b>	<b>-809 002</b>	<b>-286 972</b>	<b>-2 847</b>	<b>-1 098 821</b>	<b>0</b>	<b>-1 098 821</b>
<b>Profit before tax</b>	<b>52 731</b>	<b>336 778</b>	<b>113 544</b>	<b>503 053</b>	<b>-114 471</b>	<b>388 582</b>
<b>Tax income</b>	<b>0</b>	<b>0</b>	<b>0</b>	<b>0</b>	<b>-77 167</b>	<b>-77 167</b>
<b>Income tax</b>	<b>52 731</b>	<b>336 778</b>	<b>113 544</b>	<b>503 053</b>	<b>-191 638</b>	<b>311 415</b>
<b>Amortization/ depreciation</b>						<b>-85 223</b>
<b>Assets</b>	<b>24 110 839</b>	<b>15 601 765</b>	<b>22 800</b>	<b>39 735 404</b>	<b>274 015</b>	<b>40 009 419</b>
<b>Liabilities</b>	<b>23 465 925</b>	<b>12 995 213</b>	<b>7 238</b>	<b>36 468 376</b>	<b>21 776</b>	<b>36 490 152</b>

Income and expense are realized mainly within Poland. Opened a branch in Romania in 2016 incurred a loss before tax of PLN 6 166 thousand.

## Notes to the income statement

### 4. Net interest income

<b>4.1. Net interest income by entity</b>	<b>1.01.2016- 31.12.2016</b>	<b>1.01.2015- 31.12.2015</b>
<b>Interest income</b>	<b>2 933 858</b>	<b>2 395 168</b>
financial sector	422 531	397 219
non-financial sector	2 411 190	1 930 660
central and local government institutions	100 137	67 289
<b>Interest expense</b>	<b>-991 984</b>	<b>-898 472</b>
financial sector	-506 611	-478 404
non-financial sector	-477 363	-415 289
central and local government institutions	-8 010	-4 779
<b>Net interest income</b>	<b>1 941 874</b>	<b>1 496 696</b>

<b>4.2. Net interest income by product</b>	<b>1.01.2016- 31.12.2016</b>	<b>1.01.2015- 31.12.2015</b>
<b>Interest income</b>	<b>2 933 858</b>	<b>2 395 168</b>
Interest income from financial instruments measured at amortized cost including the effective interest rate method	2 482 318	1 969 346
term deposits	1 494	241
loans	2 329 825	1 847 472
financial assets available for sale	128 274	91 393
receivables acquired	11 564	27 381
other	11 161	2 859

Other interest income	451 540	425 822
current accounts	18 958	15 197
overnight deposits	1 185	1 309
derivatives	431 397	409 316
<b>Interest expense</b>	<b>-991 984</b>	<b>-898 472</b>
Interest expense from financial instruments measured at amortized cost including the effective interest rate method	-544 329	-489 506
term deposits	-400 454	-368 574
repo transactions in securities	-13 837	-14 088
cash deposits	-3 446	-2 187
own issue	-124 139	-102 005
other	-2 453	-2 652
Other interest expense	-447 655	-408 966
current deposits	-48 402	-37 891
derivatives	-399 253	-371 075
<b>Net interest income</b>	<b>1 941 874</b>	<b>1 496 696</b>

Interest income comprises mainly interest on loans and interest and discount on bonds. Interest expense relates mainly to term deposit for retail banking customers.

In the years 2016 and 2015, interest income on loans with recognized impairment amounted to PLN 142,974 thousand and PLN 105,969 thousand.

## 5. Net fee and commission income

	1.01.2016- 31.12.2016	1.01.2015- 31.12.2015
<b>Fee and commission income</b>	<b>592 337</b>	<b>545 655</b>
brokerage commissions	78 162	73 746
payment cards services	114 232	89 911
revenue from bancassurance activity	74 079	94 622
loans and advances	63 727	66 347
accounts maintenance	114 339	85 333
transfers	41 609	36 307
remittances and withdrawals services	27 368	21 404
acquired receivables	8 970	11 890
guarantees, letters of credit, collections, promises	14 261	14 980
other commissions	55 590	51 115
<b>Fee and commission expense</b>	<b>-257 980</b>	<b>-214 026</b>
brokerage commissions	-3 699	-3 888
costs of card transactions and ATM , including costs of payment card issue	-83 610	-61 190
insurance of bank products	-21 855	-21 693
commissions for ATM sharing	-22 336	-24 256
fees paid under service agreements	-12 112	-9 510
compensation and awards to customers	-24 191	-17 513
commissions paid to agents	-28 600	-24 308
assistance services	-4 101	-4 189
costs of customers acquisition	-6 411	-19 552
other commissions	-51 065	-27 927
<b>Net fee and commission income</b>	<b>334 357</b>	<b>331 629</b>

## Custody operations

In connection with the business combination between Alior Bank S.A. and a demerged business unit of Bank BPH S.A., the acquired assets included custody operations which are currently being continued.

As part of the custody services provided, the Bank performs the following tasks:

- storing of customer assets – based on agreements and the relevant rules and regulations, the Bank maintains security accounts for its Customers on which it maintains a record of securities stored at Alior Bank SA and institutions with which the Bank concluded appropriate agreements; these are in particular: securities subject to public offering and securities not subject to public offering both dematerialized and in a physical form, domestic and foreign; all securities stored and recorded on behalf of the Customers are kept separately from the Bank's assets and from assets of other Customers of the Bank;
- settling of and accounting for transactions – the Bank settles and accounts for Customers' transactions in securities concluded in Poland both on and outside the regulated market and on foreign markets; the settlements are made based on internal documents, documents provided by the Customer and by other institutions serving the Customer (for example, brokerage offices through which transactions are concluded); external accounting documents are verified against information held by the Bank, the Bank also acts as a representative for remote members of the Warsaw Stock Exchange; as at the end of December 2016, the Bank serviced four remote participants of the WSE whose share in stock exchange trading on the cash market of all the remote participants of the WSE in 2016 was approx. 18%;
- payment of benefits from securities – the Bank services payments of dividend and interest from securities recorded on Customer accounts, which includes registering the balances of securities held as at the date of establishing rights to dividend or interest, provides information to the tax payers about any tax due or calculates and remits the taxes on its own in line with the relevant legal regulations and pays out the amounts received from the issuers;
- reporting the balances held by the customers – the Bank periodically provides the customers with information on the securities held by them at the Bank and informs them of operations related to securities performed by them; the communication is made in a manner agreed with the Bank by post or by electronic information carriers, such as SWIFT;
- acting as a depositary – in line with the binding regulations of the law concerning acting as a depositary for investment funds and the contracts concluded with those entities, the Bank, in particular, performs reviews of the correctness of net asset valuations for these entities and of investment restrictions; the Bank also offers valuations of the stored assets for the remaining Customers; at the end of 2016, the Bank acted as a depositary for 31 investment subfunds and funds (including two investment funds in liquidation).

As at 31 December 2016, the Bank provided custodian services to individuals, Polish and international financial institutions and to legal persons not being financial institutions.

As at 31 December 2016, the Bank maintained 99 securities accounts.

## 6. Trading result

	1.01.2016- 31.12.2016	1.01.2015- 31.12.2015
FX transactions	231 844	217 286
Interest rate transactions	75 266	49 582
Ineffective part of hedge accounting	-899	1 084
Other instruments	13 568	624
<b>Trading result</b>	<b>319 779</b>	<b>268 576</b>

The result on foreign exchange transactions includes the results on: forex, SWAP (FX swap and CIRS with capital exchange), FX forward, currency options and revaluation of assets and liabilities expressed in foreign currencies.

The result on interest rate transactions includes interest rate swaps, FRA and the result on interest rate options (cap/floor).

The result on other financial instruments is the result on trading in equity securities, the result on commodity derivatives (including forwards and futures), the result on options for exchange indices, index baskets and commodities.

## 7. Net result realized on other financial instruments

	1.01.2016- 31.12.2016	1.01.2015- 31.12.2015
Available-for-sale financial assets	20 970	12 931
Own issue	971	-14
- repurchase income	1 011	570
- repurchase losses	-40	-584
Investment certificates	-22	6
<b>Net result realized on other financial instruments</b>	<b>21 919</b>	<b>12 923</b>

## 8. Net other operating income and expenses

	1.01.2016- 31.12.2016	1.01.2015- 31.12.2015
<b>Other operating income from:</b>	<b>102 014</b>	<b>79 492</b>
management of third party assets	6 921	7 630
income from contracts with business partners	21 465	15 705
acquisition of receivables	9 119	7 734
reimbursement of costs of claim enforcement	21 440	20 073
reimbursement of fees by customers	17 881	14 844
received compensations	2 032	4 984
other	23 156	8 522
<b>Other operating expenses due to:</b>	<b>-51 720</b>	<b>-30 215</b>
management of third party assets	-1 417	-1 322
paid compensations, fines and penalties	-3 665	-4 860
awards given to customers	-1 689	-413
paid compensations, settlements, complaints	-7 344	-8 368
fees and costs of claim enforcement	-18 501	-8 456
other	-19 104	-6 796
<b>Net other operating income and expenses</b>	<b>50 294</b>	<b>49 277</b>

## 9. General administrative expenses

	1.01.2016- 31.12.2016	1.01.2015- 31.12.2015
<b>Employee expenses</b>	<b>-877 750</b>	<b>-549 621</b>
remuneration due to employment contracts	-529 629	-460 548
remuneration surcharges *	-92 781	-80 131
share-based payments	0	-727
retention programs	-56 378	0
revaluation of management option plan – part settled in cash	-12 075	0
costs of bonus for senior executives settled in phantom shares	-14 126	0
restructuring provision	-167 000	0
Other	-5 761	-8 215

<b>General administrative expenses</b>	<b>-556 882</b>	<b>-457 779</b>
IT costs	-73 154	-44 856
lease and building maintenance expenses	-146 166	-140 390
marketing costs	-56 773	-52 510
training costs	-22 738	-13 880
cost of advisory services	-44 652	-20 191
costs of Banking Guarantee Fund	-86 564	-117 120
costs of lease of property, plant and equipment and intangible assets	-4 287	-3 493
costs of telecommunications services	-18 983	-15 941
external services	-40 981	-25 748
provision for restructuring	-32 668	0
other	-29 916	-23 650
<b>Amortization and depreciation</b>	<b>-101 832</b>	<b>-85 223</b>
property, plant and equipment	-64 436	-50 922
intangible assets	-37 396	-34 301
<b>Taxes and fees</b>	<b>-6 992</b>	<b>-6 198</b>
<b>Total general administrative expenses</b>	<b>-1 543 456</b>	<b>-1 098 821</b>

\*In 2016 the costs of social security contributions amounted to PLN 79 209 thousand, costs of contributions to Labour Fund and Fund of Guaranteed Employee Benefits amounted to PLN 13 099 thousand. In 2015 the costs of social security contributions amounted to PLN 56 996 thousand, costs of contributions to Labour Fund and Fund of Guaranteed Employee Benefits amounted PLN 11 268 thousand

In 2016, the Bank recognized the cost of annual charges to the Bank Guarantee Fund in accordance with the provisions of Interpretation no. 21. The amendment to the Act on the Bank Guarantee Fund introduced in March 2016 changed the method of calculating and allotting mandatory fees to the quarterly cycle, applicable from the first quarter of 2016.

The subject of the Bank's leases are passenger cars, all the agreements are operating lease agreements.

As at 31 December 2016, the Bank had 802 car lease agreements.

<b>Future liabilities from operating lease of cars by date of payment</b>	<b>1.01.2016- 31.12.2016</b>	<b>1.01.2015- 31.12.2015</b>
Up to 1 year	11 191	3 797
From 1 to 3 years	13 557	2 420
More than 3 years	51	0
<b>Total</b>	<b>24 799</b>	<b>6 217</b>

The Bank is also a lessee of office space. Rental costs constitute a considerable portion of the Bank's overheads. In renting its premises, the Bank concludes contracts for a period of at least 5 years (approx. 70% of signed lease contracts are for a 5-year period). Lease contracts provide for the possibility of a change in the lease instalments depending on the inflation fluctuations in a given lease year. All lease contracts are concluded on an arm's length basis.

<b>Future commitments under lease contracts by date of payment</b>	<b>1.01.2016- 31.12.2016</b>	<b>1.01.2015- 31.12.2015</b>
Up to 1 year	154 786	75 017
From 1 to 3 years	205 742	145 937
More than 3 years	34 790	15 335
<b>Total</b>	<b>395 318</b>	<b>236 289</b>

## 10. Net impairment allowance and write-downs

**1.01.2016- 31.12.2016**      **1.01.2015- 31.12.2015**

Impairment losses on impaired loans and advances to customers	-730 640	-649 137
financial sector	-2 467	-5 995
non-financial sector	-728 173	-643 142
retail customers	-474 733	-446 218
business customers	-253 440	-196 924
Debt securities	-6 975	-7 981
IBNR for customers without impairment losses	-32 021	-1 726
financial sector	-108	-842
non-financial sector	-31 913	-884
retail customers	-10 417	-1 683
business customers	-21 496	799
Off-balance reserve	-2 382	-560
Property, plant and equipment and intangible assets	-22 715	-12 368
<b>Net impairment losses &amp; provisions</b>	<b>-794 733</b>	<b>-671 772</b>

## 11. Income tax

<b>11.1 Presented in the income statement</b>	<b>1.01.2016- 31.12.2016</b>	<b>1.01.2015- 31.12.2015</b>
<b>Current tax</b>	<b>231 011</b>	<b>161 210</b>
current year	231 011	161 210
<b>Deferred tax</b>	<b>-155 821</b>	<b>-84 043</b>
origination and reversal of temporary differences	-155 821	-84 043
<b>Accounting tax recognized in the income statement</b>	<b>75 190</b>	<b>77 167</b>

<b>11.2 Effective tax rate calculation</b>	<b>1.01.2016- 31.12.2016</b>	<b>1.01.2015- 31.12.2015</b>
<b>Profit before tax</b>	<b>707 265</b>	<b>388 582</b>
<b>Income tax at 19%</b>	<b>134 380</b>	<b>73 831</b>
<b>Non-tax deductible expenses</b>	<b>61 633</b>	<b>14 398</b>
Representation costs	219	152
State Fund for Rehabilitation of Persons with Disabilities	1 185	1 140
Impairment losses on loans in the part not covered with deferred tax	26 617	4 047
Prudential fee to Bank Guarantee Fund	4 977	4 071
Costs of provisions for management options	0	138
The tax on certain financial institutions	24 870	0
Donations	26	7
Other	3 739	4 843
<b>Non-taxable revenues</b>	<b>-106 881</b>	<b>-6 356</b>
Release of loan impairment allowances in the part not covered with the deferred tax	-935	-73
Profit from the acquisition of demerged business of Bank BPH	-96 531	0
Other	-9 415	-6 283
<b>Tax deductible expenses not being accounting expenses</b>	<b>-6 540</b>	<b>0</b>
Costs related to spending on capital increase	-6 540	0
<b>Recognition of tax loss</b>	<b>141</b>	<b>0</b>
Recognition of assets due to the contribution of receivables to a debt collection company	643	-3 038
<b>Other</b>	<b>-8 186</b>	<b>-1 668</b>
<b>Accounting tax recognized in the income statement</b>	<b>75 190</b>	<b>77 167</b>
<b>Effective tax rate</b>	<b>10,63%</b>	<b>19,86%</b>

### 11.3 Deferred tax asset and provision

Deferred tax assets	31.12.2015	Changes recognized in profit or loss	Changes recognized in equity	Changes recognized in goodwill (BPH)	31.12.2016
Deferred revenue	144 815	51 391	0	97 618	293 824
Interest accrued on deposits	26 772	-5 334	0	2 143	23 581
Interest / discount accrued on securities	29 225	14 838	0	994	45 057
Negative valuation of securities	5 375	1 288	12 775	0	19 438
Interest accrued on derivatives	23 584	699	0	339	24 622
Negative valuation of derivatives	682 754	-614 835	-15 247	5 284	57 956
Premium receivable on options	12 760	2 986	0	890	16 636
Accruals	23 154	75 973	0	17 625	116 752
Impairment allowances on loans	157 816	38 343	0	85 460	281 619
Other provisions	-423	6 970	0	-61 495	-54 948
Recognition of assets due to the contribution of receivables	12 297	-5 958	0	0	6 339
Recognition of asset related to tax loss	0	1 030	0	0	1 030
<b>Deferred tax assets</b>	<b>1 118 129</b>	<b>-432 609</b>	<b>-2 472</b>	<b>148 858</b>	<b>831 906</b>

Deferred tax liability	31.12.2015	Changes recognized in profit or loss	Changes recognized in equity	Changes recognized in goodwill (BPH)	31.12.2016
Interest accrued on interbank deposits	-9	-396	0	-1	-406
Interest accrued on loans and advances	-53 419	-15 115	0	-11 332	-79 866
Interest / discount accrued on securities	-9 612	-4 739	0	-920	-15 271
Positive valuation of securities	-855	-8	377	0	-486
Interest accrued on derivatives	-38 177	8 850	0	-1 128	-30 455
Positive valuation of derivatives	-709 056	603 411	22 463	-4 217	-87 399
Difference between accounting and tax amortization/ depreciation	-28 107	427	0	-5 834	-33 514
Income accrued, not received	-4 879	-4 000	0	-52 259	-61 138
<b>Deferred tax liability</b>	<b>-844 114</b>	<b>588 430</b>	<b>22 840</b>	<b>-75 691</b>	<b>-308 535</b>

<b>Deferred tax - per the balance sheet</b>	<b>274 015</b>	<b>155 821</b>	<b>20 368</b>	<b>73 167</b>	<b>523 371</b>
---	----------------	----------------	---------------	---------------	----------------

Deferred tax assets	31.12.2014	Changes recognized in profit or loss	Changes recognized in equity	Changes recognized in goodwill (Meritum )	31.12.2015
Deferred revenue	99 302	24 383	0	21 130	144 815
Interest accrued on deposits	17 294	4 655	0	4 823	26 772
Interest / discount accrued on securities	14 291	14 934	0	0	29 225
Negative valuation of securities	2 888	1 599	874	14	5 375
Interest accrued on derivatives	21 026	2 557	0	1	23 584
Negative valuation of derivatives	475 098	193 705	13 951	0	682 754
Premium receivable on options	11 255	1 505	0	0	12 760
Difference between accounting and tax amortization/ depreciation	0	-253	0	253	0
Accruals	7 390	15 255	0	509	23 154
Impairment allowances on loans	91 534	43 664	0	22 618	157 816
Other provisions	2 953	-2 430	0	-946	-423
Recognition of assets due to the contribution of receivables	10 381	1 916	0	0	12 297

<b>Deferred tax assets</b>	<b>753 412</b>	<b>301 490</b>	<b>14 825</b>	<b>48 402</b>	<b>1 118 129</b>
----------------------------	----------------	----------------	---------------	---------------	------------------

<b>Deferred tax liability</b>	<b>31.12.2014</b>	<b>Changes recognized in profit or loss</b>	<b>Changes recognize d in equity</b>	<b>Changes recognize d in goodwill (Meritum )</b>	<b>31.12.2015</b>
Interest accrued on interbank deposits	-6	-3	0	0	-9
Interest accrued on loans and advances	-40 953	-9 699	0	-2 767	-53 419
Interest / discount accrued on securities	-5 455	-4 129	0	-28	-9 612
Positive valuation of securities	-126	242	-727	-244	-855
Interest accrued on derivatives	-31 728	-6 438	0	-11	-38 177
Positive valuation of derivatives	-502 286	-194 129	-12 641	0	-709 056
Difference between accounting and tax amortization/ depreciation	-20 543	-3 788	0	-3 776	-28 107
Income accrued not received	-5 376	497	0	0	-4 879
<b>Deferred tax liability</b>	<b>-606 473</b>	<b>-217 447</b>	<b>-13 368</b>	<b>-6 826</b>	<b>-844 114</b>
<b>Deferred tax - per the balance sheet</b>	<b>146 939</b>	<b>84 043</b>	<b>1 457</b>	<b>41 576</b>	<b>274 015</b>

<b>Deferred tax recognized directly in equity</b>	<b>1.01.2016- 31.12.2016</b>	<b>1.01.2015- 31.12.2015</b>
Negative valuation of securities	12 775	874
Negative valuation of derivatives	-15 247	13 951
Positive valuation of securities	377	-727
Positive valuation of derivatives	22 463	-12 641
<b>Total</b>	<b>20 368</b>	<b>1 457</b>

## 12. Earnings per share

	<b>1.01.2016- 31.12.2016</b>	<b>1.01.2015- 31.12.2015</b>
Net profit	632 075	311 415
Weighted average number of ordinary shares	102 218 667	72 088 316
Share options	2 568 564	2 568 564
Adjusted weighted average number of shares	104 787 231	74 656 880
<b>Net earnings per ordinary share (PLN)</b>	<b>6.18</b>	<b>4.32</b>
<b>Diluted earnings per one share (PLN)</b>	<b>6.03</b>	<b>4.17</b>

In accordance with IAS 33 the Bank prepares a calculation of diluted earnings per share, taking into account the shares issuable under incentive schemes described in Note 37. The calculation does not include those elements of the incentive schemes, which were antidilutive in the years presented, and which in the future could potentially affect the dilution of earnings per share. Basic earnings per share is calculated by dividing the profit attributable to the Bank's shareholders and the weighted average number of ordinary shares during the year. Diluted earnings per share is calculated based on the profit attributable to shareholders of the Bank to the weighted average number of ordinary shares adjusted in such a way as if they were converted into shares of all potentially dilutive potential ordinary shares. The Bank has one category causing dilution of potential ordinary shares: share options.

## Notes to the statement of financial position

## 13.Cash and balances with the central bank

	As at 31.12.2016	As at 31.12.2015
Current account with the Central Bank	16 959	1 559 981
Overnight deposits with the Central Bank	344 009	0
Cash	722 023	190 154
<b>Cash and balances with the central bank</b>	<b>1 082 991</b>	<b>1 750 135</b>

The Bank maintains the mandatory reserve in a current account with the National Bank of Poland, in an amount that complies with the decisions of the Monetary Policy Board. As of 31 December 2010, the rate of the mandatory reserve is 3.5%.

## 14.Available-for-sale financial assets and investment securities held to maturity

14.1 By type	As at 31.12.2016	As at 31.12.2015
<b>Debt instruments</b>	<b>9 339 005</b>	<b>4 239 445</b>
issued by the State Treasury	6 197 981	3 773 380
T-bonds	6 197 981	3 773 380
issued by monetary institutions	2 691 128	0
Bonds	91 590	0
money bills	2 599 538	0
issued by other financial institutions	156 746	176 995
Bonds	59 880	60 486
Eurobonds	96 866	116 509
issued by companies	293 150	289 070
Bonds	293 150	289 070
<b>Equity instruments</b>	<b>18 729</b>	<b>13 674</b>
<b>Available-for-sale financial assets</b>	<b>9 357 734</b>	<b>4 253 119</b>

14.2 By maturity	As at 31.12.2016	As at 31.12.2015
without set maturity date	18 729	13 675
≤ 1M	3 031 043	0
> 1M ≤ 3M	16 922	17 088
≤ 6M > 3M ≤ 6M	578 434	254 486
> 6M ≤ 1Y	196 645	366 016
> 1Y ≤ 2Y	1 331 405	1 134 855
> 2Y ≤ 5Y	3 496 332	1 940 564
> 5Y ≤ 10Y	688 224	526 435
<b>Available-for-sale financial assets</b>	<b>9 357 734</b>	<b>4 253 119</b>

14.3 Impairment allowance on debt instruments	As at 31.12.2016		As at 31.12.2015	
	Gross amount	Impairment allowance	Gross amount	Impairment allowance
Bonds issued by companies	94 861	21 447	101 122	14 472

14.4 Change in the balance of debt instruments impairment allowances	As at 31.12.2016	As at 31.12.2015
Opening balance	14 472	6 491
Changes during the year:	6 975	7 981
Increases	6 975	7 981
<b>Impairment allowances at the end of the period</b>	<b>21 447</b>	<b>14 472</b>

The schedules below show the prioritization of the measurement methods of available-for-sale financial assets measured at fair value as at 31 December 2016 and comparative data as at 31 December 2015.

In accordance with IFRS 13, the Bank classified:

- to level 1 – all securities for which quotations are available from active financial markets.

The group includes mainly debt Treasury securities. The fair value is determined based on the purchase price from the quotations on the interbank market, brokers' quotations and BondSpot quotations.

- to level 2 – instruments for which prices are not directly observable, but the prices used for measurement are based on quotations from active transaction markets.

The group includes NBP bills and commercial debt securities. The fair value is determined based on the discounted future cash flows method which assumes that the profitability curves will be based on quotations of profitability of securities on the interbank market.

Debt commercial securities are measured based on profitability curves adjusted by the credit spread, if the spread can be determined on the basis of observable market quotations, e.g. based on quotations of credit swaps.

Debt commercial securities quoted on exchanges, with low transaction volumes on the market, were also recognized on this level.

- to level 3 – instruments for which at least one of the factors which impact its price is not observable on the market.

This group shows the Bank's position in debt commercial securities whose fair value is impacted not only by the parameters resulting from market quotations, but also by the credit spread amount, which is not observable. Spread is determined based on the primary market price or the price at the moment of concluding the transaction. It is subject to periodical revaluation in the periods when reliable market quotations occur or prices are obtained from transactions that are comparable in terms of volume. The amount of spread also changes based on information about changes in the issuer's financial standing. As at the end of 2016, the sensitivity of valuation of such assets to credit spread increases by 1 base point amounted to PLN 97 thousand.

Transfers of instruments between valuation levels are performed as at the end of a reporting period. Such transfers are performed in the situations described in the International Financial Reporting Standards, in connection with such factors as e.g. the availability of quotations of a given instrument on an active market, availability of quotations of valuation factors, or impact of unobservable factors on the fair value.

In 2016, the Bank did not reclassify financial instruments between the levels.

14.5 Fair value	As at 31.12.2016	As at 31.12.2015
<b>Level 1</b>	<b>6 386 868</b>	<b>3 889 889</b>
Instrumenty kapitałowe	431	0
T-bonds	6 197 981	3 773 380
Other bonds	188 456	116 509
<b>Level 2</b>	<b>2 599 538</b>	<b>0</b>
Money bills	2 599 538	0

Level 3	371 328	363 230
Equity instruments	18 298	13 674
Other bonds	353 030	349 556
<b>Valuation of available for sale financial assets by level</b>	<b>9 357 734</b>	<b>4 253 119</b>

14.6 Movements on financial assets available for sale classified as level 3	As at 31.12.2016	As at 31.12.2015
Opening balance	363 230	374 601
Increases, including	42 209	118 223
Acquisition	42 029	117 161
Revenue recognised in income statement	170	0
Fair value adjustment	10	400
Foreign exchange differences	0	662
Decreases, including	-34 111	-129 594
Sale	-20 888	-121 381
Other changes recognised in income statement	-7 252	-8 213
Fair value adjustment	-5 971	0
<b>Financial assets available for sale classified as level 3 at the end of the period</b>	<b>371 328</b>	<b>363 230</b>

The measurement of available-for-sale assets is presented in the revaluation reserve, interest and discount income is presented in interest income, and profit/(loss) from sales is presented in the result on other financial instruments.

### Investment securities held to maturity

Bank in the position Investment securities held to maturity presented securities, which are not secured loan in the European Investment Bank.

14.7 1 By type	As at 31.12.2016	As at 31.12.2015
<b>Debt instruments</b>	<b>1 954</b>	<b>0</b>
issued by the State Treasury	1 954	0
T-bonds	1 954	0
<b>Investment securities held to maturity</b>	<b>1 954</b>	<b>0</b>

14.8 By maturity	As at 31.12.2016	As at 31.12.2015
> 2Y ≤ 5Y	1 954	0
<b>Investment securities held to maturity</b>	<b>1 954</b>	<b>0</b>

14.9 Fair value	As at 31.12.2016	As at 31.12.2015
<b>Level 1</b>	<b>1919</b>	<b>0</b>
T-bonds	1 919	0
<b>Investment securities held to maturity</b>	<b>1 919</b>	<b>0</b>

## 15. Loan and advances to customers

15.1 By type	As at 31.12.2016	As at 31.12.2015
<b>Retail segment</b>	<b>25 891 222</b>	<b>17 595 314</b>
Working capital facility	293 951	167 635
Consumer loans	13 956 654	8 699 017
Consumer finance loans	1 253 001	748 948
Loans for purchase of securities	125 117	119 069

Credit card loans	970 319	225 629
Loans for residential real estate	8 407 632	6 717 911
Other mortgage loans	833 485	896 008
Other receivables	51 063	21 097
<b>Corporate segment</b>	<b>20 388 627</b>	<b>13 318 676</b>
Working capital facility	11 114 177	7 361 826
Car loans	131 971	70 394
Investment loans	7 517 095	5 487 618
Acquired receivables (factoring)	794 087	376 403
Reverse Repo/BSB	680 780	0
Other receivables	150 517	22 435
<b>Loans and advances to customers</b>	<b>46 279 849</b>	<b>30 913 990</b>

15.2 By gross amounts and carrying amounts	As at 31.12.2016	As at 31.12.2015
<b>Retail segment</b>	<b>25 891 222</b>	<b>17 595 314</b>
Loans for residential real estate	8 407 632	6 717 911
not impaired	8 270 924	6 593 746
impaired	214 637	189 075
IBNR	-3 572	-4 811
Impairment allowance	-74 357	-60 099
Consumer finance loans	1 253 001	748 947
not impaired	1 245 377	737 841
impaired	41 410	50 221
IBNR	-3 457	-1 456
Impairment allowance	-30 329	-37 659
Other retail loans	16 230 589	10 128 456
not impaired	15 684 976	9 732 180
impaired	2 226 673	1 378 919
IBNR	-196 949	-120 367
Impairment allowance	-1 484 111	-862 276
<b>Corporate segment</b>	<b>20 388 627</b>	<b>13 318 676</b>
not impaired	19 298 046	12 741 034
impaired	2 329 832	1 428 322
IBNR	-99 151	-39 248
Impairment allowance	-1 140 100	-811 432
<b>Loans and advances to customers</b>	<b>46 279 849</b>	<b>30 913 990</b>

The provision for losses incurred but not reported (IBNR) amounted to: PLN 303,129 thousand as at 31 December 2016 and PLN 165,882 thousand as at 31 December 2015.

15.3 Loans and advances to customers (impaired)	As at 31.12.2016	As at 31.12.2015
<b>Receivables from customers individually assessed</b>	<b>1 076 943</b>	<b>546 026</b>
<b>Retail segment</b>	<b>1 198</b>	<b>9 512</b>
Amounts due from customers	9 240	87 157
Impairment allowance	-8 042	-77 645
<b>Corporate segment</b>	<b>1 075 745</b>	<b>536 514</b>
Amounts due from customers	1 819 924	1 095 419
Impairment allowance	-744 179	-558 905
<b>Receivables from customers collectively assessed</b>	<b>1 006 712</b>	<b>729 045</b>
<b>Retail segment</b>	<b>892 725</b>	<b>648 669</b>
Amounts due from customers	2 473 480	1 531 058
Impairment allowance	-1 580 755	-882 389
<b>Corporate segment</b>	<b>113 987</b>	<b>80 376</b>
Amounts due from customers	509 908	332 903
Impairment allowance	-395 921	-252 527
<b>Receivables from customers impaired</b>	<b>2 083 655</b>	<b>1 275 071</b>

15.4 Change in the balance of loans and advances, impairment allowances and IBNR	As at 31.12.2016	As at 31.12.2015
Opening balance	1 937 348	1 289 770

Change due to demerged part of BPH SA (2016) or the acquired Meritum Bank ICB SA (2015)	786 851	416 951
Change due to the acquired SKOK	32 845	0
Changes during the year:	762 661	650 863
Increases	1 852 854	2 093 853
Retail segment	1 290 653	1 616 744
Corporate segment	562 201	477 109
Decreases	-1 090 193	-1 442 990
Retail segment	-805 502	-1 168 843
Corporate segment	-284 691	-274 147
Transfer to costs	-490 966	-419 473
Other changes	3 287	-763
<b>Impairment allowances and IBNR at the end of the period</b>	<b>3 032 026</b>	<b>1 937 348</b>

<b>15.5 By maturity (as at the balance sheet date)</b>	<b>As at 31.12.2016</b>	<b>As at 31.12.2015</b>
<b>Retail segment</b>	<b>25 891 222</b>	<b>17 595 314</b>
≤ 1M	2 916 186	2 013 348
> 1M ≤ 3M	633 692	389 891
> 3M ≤ 6M	853 902	547 084
> 6M ≤ 1Y	1 616 066	1 007 076
>1Y ≤ 2Y	2 617 666	1 534 368
>2Y ≤ 5Y	5 712 326	3 473 595
>5Y ≤ 10Y	5 418 912	3 554 046
>10Y ≤ 20Y	3 497 105	2 819 119
>20Y	2 625 367	2 256 787
<b>Corporate segment</b>	<b>20 388 627</b>	<b>13 318 676</b>
≤ 1M	5 563 041	4 798 766
> 1M ≤ 3M	1 141 897	759 175
> 3M ≤ 6M	1 193 177	593 919
> 6M ≤ 1Y	2 143 239	1 141 133
>1Y ≤ 2Y	2 174 464	1 303 699
>2Y ≤ 5Y	4 085 045	2 286 486
>5Y ≤ 10Y	3 240 797	1 820 024
>10Y ≤ 20Y	846 967	615 474
<b>Loans and advances to customers</b>	<b>46 279 849</b>	<b>30 913 990</b>

<b>15.6 By currency</b>	<b>As at 31.12.2016</b>	<b>As at 31.12.2015</b>
<b>Retail segment</b>	<b>25 891 222</b>	<b>17 595 314</b>
PLN	24 338 453	16 343 892
EUR	1 125 543	933 316
GBP	201 010	124 376
USD	41 047	20 706
CHF	184 298	173 018
Other	871	6
<b>Corporate segment</b>	<b>20 388 627</b>	<b>13 318 676</b>
PLN	16 362 596	10 675 538
EUR	3 755 500	2 542 871
GBP	3 778	5 210
USD	193 329	61 924
CHF	55 242	33 133
Other	11 942	0
<b>Total receivables</b>	<b>46 279 849</b>	<b>30 913 990</b>

Loans in CHF represented 0,5% of the total balance of loans in 2016 (2015: 0.7%).

<b>15.7 Ten largest credit exposures</b>	<b>Currency</b>	<b>As at 31.12.2016</b>
Company 1	EUR,PLN	365 461
Company 2	EUR,PLN	240 607
Company 3	EUR	145 992
Company 4	EUR	142 639
Company 5	PLN	124 800

Company 6	EUR	121 210
Company 7	PLN	115 853
Company 8	EUR	114 255
Company 9	PLN	106 047
Company 10	PLN	104 703

15.8 Ten largest credit exposures	Currency	As at 31.12.2015
Company 1	EUR	242 414
Company 2	EUR	234 544
Company 3	PLN	149 776
Company 4	EUR,GBP,PLN	144 458
Company 5	EUR	129 233
Company 6	PLN	123 952
Company 7	PLN	120 873
Company 8	EUR	113 248
Company 9	PLN	112 744
Company 10	PLN	97 351

The two tables above present the loan balance at its nominal value. The principles relating to concentration limits are described in Note 46.

In 2016, the Bank sold loans for a total gross amount of PLN 506 468 thousand, the provision recorded for the loans portfolio amounted to PLN 401 196 thousand, and the result on sales amounted to PLN 1 212 thousand. All the benefits and risks were transferred to the buyer. In 2015, the Bank sold loans for a total gross amount of PLN 547 452 thousand, the provision recorded for the loans portfolio amounted to PLN 403 546 thousand, and the result on sales amounted to PLN 3 988 thousand. All the benefits and risks were transferred to the buyer.

## 16. Amounts due from banks

16.1 By type	As at 31.12.2016	As at 31.12.2015
Current accounts	386 766	339 131
Term deposits	237 396	113 062
Reverse Repo	583 012	0
Deposits as derivative transactions (ISDA) collateral	145 141	171 406
Other	11 911	18 941
<b>Amounts due from banks</b>	<b>1 364 226</b>	<b>642 540</b>

16.2 By maturity (as at the balance sheet date)	As at 31.12.2016	As at 31.12.2015
≤ 1M	1 364 226	642 345
> 1M ≤ 3M	0	90
> 3M ≤ 6M	0	105
<b>Amounts due from banks</b>	<b>1 364 226</b>	<b>642 540</b>

16.3 By currency	As at 31.12.2016	As at 31.12.2015

PLN	600 224	25 810
EUR	286 143	126 831
GBP	29 238	86 572
USD	321 306	183 566
CHF	8 890	75 986
Other currencies	118 425	143 775
<b>Amounts due from banks</b>	<b>1 364 226</b>	<b>642 540</b>

The security deposits granted relate to security transferred to other banks under the settlements related to CSA (Credit Support Annex).

## 17. Property, plant and equipment

As at 31.12.2016	Fixed assets under construction	Plant and machinery (including IT equipment)	Leasehold improvements	Own buildings	Other	Total
<b>Value at cost as at 01.01.2016</b>	<b>13 112</b>	<b>231 629</b>	<b>176 468</b>	<b>22 775</b>	<b>82 843</b>	<b>526 827</b>
Changes due to:	9 963	142 355	25 735	121 723	14 223	313 999
Purchases in 2016	13 009	22 020	11 014	588	1 326	47 957
Demerged part of BPH S.A.	3 379	101 457	17 731	112 541	12 409	247 517
Fair Value Measurement	0	15 699		4 089	3 372	23 160
Reclassifications in 2016	-6 409	4 434	-2 977	763	1 476	-2 713
Sales in 2016	-16	-1 255	-33	-45	-4 360	-5 709
Other changes	0	0	0	3 787	0	3 787
<b>Value at cost as at 31.12.2016</b>	<b>23 075</b>	<b>373 984</b>	<b>202 203</b>	<b>144 498</b>	<b>97 066</b>	<b>840 826</b>
<b>Accumulated depreciation as at 01.01.2016</b>	<b>0</b>	<b>153 126</b>	<b>86 260</b>	<b>42</b>	<b>58 132</b>	<b>297 560</b>
Depreciation for 2016	0	33 116	23 025	666	7 629	64 436
Other changes	0	-2 015	-2 915	918	-2 258	-6 270
<b>Accumulated depreciation as at 31.12.2016</b>	<b>0</b>	<b>184 227</b>	<b>106 370</b>	<b>1 626</b>	<b>63 503</b>	<b>355 726</b>
<b>Impairment allowances as at 01.01.2016</b>	<b>0</b>	<b>1 121</b>	<b>494</b>	<b>0</b>	<b>19</b>	<b>1 634</b>
Changes in impairment allowances in 2016	0	188	2 030	0	168	2 386
Other changes	0	-175	-2 177	0	-88	-2 440
<b>Impairment allowances as at 31.12.2016</b>	<b>0</b>	<b>1 134</b>	<b>347</b>	<b>0</b>	<b>99</b>	<b>1 580</b>
<b>Net value as at 01.01.2016</b>	<b>13 112</b>	<b>77 382</b>	<b>89 714</b>	<b>22 733</b>	<b>24 692</b>	<b>227 633</b>
<b>Net value as at 31.12.2016</b>	<b>23 075</b>	<b>188 623</b>	<b>95 486</b>	<b>142 872</b>	<b>33 464</b>	<b>483 520</b>

As at 31.12.2015	Fixed assets under construction	Plant and machinery (including IT equipment)	Leasehold improvements	Own buildings	Other	Total
<b>Value at cost as at 01.01.2015</b>	<b>7 094</b>	<b>196 229</b>	<b>155 293</b>	<b>0</b>	<b>72 450</b>	<b>431 066</b>
Change due to the acquisition of Meritum Bank ICB S.A.	0	2 256	-579	0	4 135	5 812
Other changes in 2015 due to:	6 018	23 431	18 024	22 775	394	70 642
Purchases in 2015	8 729	20 175	27 570	22 775	1 376	80 625
Reclassifications in 2015	-2 557	1 545	601	0	410	-1
Sales in 2015	0	0	0	0	-310	-310
Other changes	-154	1 711	-10 147	0	-1 082	-9 672
<b>Value at cost as at 31.12.2015</b>	<b>13 112</b>	<b>221 916</b>	<b>172 738</b>	<b>22 775</b>	<b>76 979</b>	<b>507 520</b>
<b>Accumulated depreciation as at 01.01.2015</b>	<b>0</b>	<b>121 777</b>	<b>68 785</b>	<b>0</b>	<b>46 067</b>	<b>236 629</b>
Depreciation for 2015	0	24 584	18 645	42	7 651	50 922
Other changes	0	-2 948	-4 900	0	-1 450	-9 298

<b>Accumulated depreciation as at 31.12.2015</b>	<b>0</b>	<b>143 413</b>	<b>82 530</b>	<b>42</b>	<b>52 268</b>	<b>278 253</b>
<b>Impairment allowances as at 01.01.2015</b>	<b>0</b>	<b>577</b>	<b>2 006</b>	<b>0</b>	<b>19</b>	<b>2 602</b>
Changes in impairment allowances in 2015	0	544	-1 512	0	0	-968
<b>Impairment allowances as at 31.12.2015</b>	<b>0</b>	<b>1 121</b>	<b>494</b>	<b>0</b>	<b>19</b>	<b>1 634</b>
<b>Net value as at 01.01.2015</b>	<b>7 094</b>	<b>73 875</b>	<b>84 502</b>	<b>0</b>	<b>26 364</b>	<b>191 835</b>
<b>Net value as at 31.12.2015</b>	<b>13 112</b>	<b>77 382</b>	<b>89 714</b>	<b>22 733</b>	<b>24 692</b>	<b>227 633</b>

## 18. Intangible assets

As at 31.12.2016	Goodwill	Capital expenditure	Computer software and licences	Trademark	Other	Total
<b>Value at cost as at 01.01.2016</b>	<b>106 036</b>	<b>59 355</b>	<b>408 971</b>	<b>3 667</b>	<b>5 589</b>	<b>583 618</b>
Changes in intangible assets due to	10 252	49 143	26 663	0	42 061	128 119
Purchases in 2016	0	48 991	15 758	0	110	64 859
Demerged part of BPH S.A	0	51 554	93 385	0	0	144 939
Fair Value Measurement	0	-49 556	-47 969	0	0	-97 525
Recognition of fair value of customer relationships	0	0	0	0	42 100	42 100
Reclassifications in 2016	10 252	-29 887	11 374	0	-149	-8 410
Capitalized costs of salaries	0	28 190	4 395	0	0	32 585
Other changes	0	-149	-50 280	0	0	-50 429
<b>Value at cost as at 31.12.2016</b>	<b>116 288</b>	<b>108 498</b>	<b>435 634</b>	<b>3 667</b>	<b>47 650</b>	<b>711 737</b>
Accumulated amortization as at 01.01.2016	0	0	189 846	0	3 045	192 891
Amortization for 2016	0	0	33 552	0	3 844	37 396
Other changes	0	0	-26 745	0	-91	-26 836
<b>Accumulated amortization as at 31.12.2016</b>	<b>0</b>	<b>0</b>	<b>196 653</b>	<b>0</b>	<b>6 798</b>	<b>203 451</b>
<b>Impairment allowances as at 01.01.2016</b>	<b>1 668</b>	<b>1 630</b>	<b>4 242</b>	<b>3 367</b>	<b>0</b>	<b>10 907</b>
impairment changes in 2016	10 252	913	9 071	0	93	20 329
Other changes	0	-2 526	-1 244	0	-93	-3 863
<b>Impairment allowances as at 31.12.2016</b>	<b>11 920</b>	<b>17</b>	<b>12 069</b>	<b>3 367</b>	<b>0</b>	<b>27 373</b>
<b>Net value as at 01.01.2016</b>	<b>104 368</b>	<b>57 725</b>	<b>214 883</b>	<b>300</b>	<b>2 544</b>	<b>379 820</b>
<b>Net value as at 31.12.2016</b>	<b>104 368</b>	<b>108 481</b>	<b>226 912</b>	<b>300</b>	<b>40 852</b>	<b>480 913</b>

As at 31.12.2015	Goodwill	Capital expenditure	Computer software, licences and development costs	Trademark	Other	Total
<b>Value at cost as at 01.01.2015</b>	<b>2 321</b>	<b>35 704</b>	<b>306 765</b>	<b>300</b>	<b>809</b>	<b>345 899</b>
Change due to the acquisition of Meritum Bank ICB S.A.	104 368	1 843	25 298	3 367	4 184	139 060
Changes in intangible assets due to	-653	21 808	46 028	0	76	67 259
Purchases in 2015	0	22 016	15 463	0	76	37 555
Reclassifications in 2015	0	-11 459	11 459	0	0	0
Capitalized manufacturing costs	0	11 240	12 340	0	0	23 580
Other changes	-653	11	6 766	0	0	6 124
<b>Value at cost as at 31.12.2015</b>	<b>106 036</b>	<b>59 355</b>	<b>378 091</b>	<b>3 667</b>	<b>5 069</b>	<b>552 218</b>
<b>Accumulated amortization as at 01.01.2015</b>	<b>0</b>	<b>0</b>	<b>127 886</b>	<b>0</b>	<b>734</b>	<b>128 620</b>
Amortization for 2015	0	0	32 510	0	1 791	34 301
Other changes	0	0	-1 429	0	0	-1 429
<b>Accumulated amortization as at 31.12.2015</b>	<b>0</b>	<b>0</b>	<b>158 967</b>	<b>0</b>	<b>2 525</b>	<b>161 492</b>
<b>Impairment allowances as at 01.01.2015</b>	<b>2 321</b>	<b>27</b>	<b>342</b>	<b>0</b>	<b>0</b>	<b>2 690</b>

changes in impairment allowances in 2015	-653	1 603	3 900	3 367	0	8 217
<b>Impairment allowances as at 31.12.2015</b>	<b>1 668</b>	<b>1 630</b>	<b>4 242</b>	<b>3 367</b>	<b>0</b>	<b>10 907</b>
<b>Net value as at 01.01.2015</b>	<b>0</b>	<b>35 677</b>	<b>178 537</b>	<b>300</b>	<b>75</b>	<b>214 589</b>
<b>Net value as at 31.12.2015</b>	<b>104 368</b>	<b>57 725</b>	<b>214 882</b>	<b>300</b>	<b>2 544</b>	<b>379 820</b>

Expenditure on intangible assets which are owned or co-owned by the Bank and are earmarked for holding and using for the Bank's purposes or for sale, are included in costs directly related to assembly in progress or commissioning for use of new or improved intangible assets. These, among other things, comprise the costs of:

- purchase, in Poland or abroad, or creating proprietary intangible assets and their transport, assembly, correction and implementation tests;
- preparing the place to implement the intangible assets;
- design documentation.

## 19. Other assets

<b>19.1 Other assets</b>	<b>As at 31.12.2016</b>	<b>As at 31.12.2015</b>
<b>Sundry debtors</b>	<b>690 338</b>	<b>363 771</b>
Other settlements	244 422	90 154
Receivables related to the sale of service (including insurance)	86 699	113 114
Guarantee deposits	12 254	11 813
Settlements of payment cards	202 007	148 690
Receivables from the settlement of the purchase of a separate part of BPH S.A.	144 956	0
<b>Deferred costs</b>	<b>57 178</b>	<b>34 504</b>
Settlements of rental charges and utilities	1 797	1 484
Maintenance and support of systems, servicing of plant and equipment	14 207	4 330
Other deferred costs	41 174	28 690
<b>Settlements of VAT</b>	<b>20 362</b>	<b>17 239</b>
<b>Other assets (gross)</b>	<b>767 878</b>	<b>415 514</b>
Impairment allowances	-61 844	-28 689
<b>Other assets (net)</b>	<b>706 034</b>	<b>386 825</b>
including financial assets (gross)	690 338	363 771

<b>19.2 Change in the balance of other assets impairment allowances</b>	<b>As at 31.12.2016</b>	<b>As at 31.12.2015</b>
Opening balance	28 689	7 204
Change due to the purchase of a demerged part of BPH S.A.	29 053	0
Changes during the year:	1 535	21 485
Increases	2 285	21 523
Decreases	-750	-38
Other changes	2 567	0
<b>Impairment allowances at the end of the period</b>	<b>61 844</b>	<b>28 689</b>

The receivables related to the sale of goods and services cover mainly fees from insurance companies for servicing insurance.

## 20. Amounts due to customers

20.1 By type	As at 31.12.2016	As at 31.12.2015
Current deposits	25 794 022	12 481 435
Term deposits	22 325 534	18 541 682
Own issue of banking securities	2 768 672	2 259 230
Other liabilities	516 620	392 329
<b>Total amounts due to customers</b>	<b>51 404 848</b>	<b>33 674 676</b>

20.2 By customer type and segment	As at 31.12.2016	As at 31.12.2015
<b>Retail segment</b>	<b>32 035 389</b>	<b>21 409 075</b>
Current deposits	17 264 837	8 485 256
Term deposits	13 908 933	12 666 033
Own issue of banking securities	628 246	54 280
Other liabilities	233 373	203 506
<b>Corporate segment</b>	<b>19 369 459</b>	<b>12 265 601</b>
Current deposits	8 529 185	3 996 179
Term deposits	8 416 601	5 875 649
Own issue of banking securities	2 140 426	2 204 950
Other liabilities	283 247	188 823
<b>Total amounts due to customers</b>	<b>51 404 848</b>	<b>33 674 676</b>

In 2016, the Bank issued own securities amounted to PLN 1 106 334 thousand; securities purchased before maturity amounted to PLN 148 587 thousand.

In 2015, the Bank issued own securities amounted to PLN 1 485 767 thousand; securities purchased before maturity amounted to PLN 208 591 thousand.

20.3 By maturity (as at the balance sheet date)	As at 31.12.2016	As at 31.12.2015
<b>Retail segment</b>	<b>32 035 389</b>	<b>21 409 075</b>
≤ 1M	21 811 318	11 358 478
> 1M ≤ 3M	3 163 975	4 296 204
> 3M ≤ 1Y	5 878 511	5 122 282
> 1Y ≤ 5Y	1 017 041	622 687
>5Y	164 544	9 424
<b>Corporate segment</b>	<b>19 369 459</b>	<b>12 265 601</b>
≤ 1M	13 700 922	7 729 311
> 1M ≤ 3M	1 443 070	1 343 848
> 3M ≤ 1Y	2 188 383	1 326 868
> 1Y ≤ 5Y	2 013 363	1 858 131
>5Y	23 721	7 443
<b>Total amounts due to customers</b>	<b>51 404 848</b>	<b>33 674 676</b>

20.4 By currency	As at 31.12.2016	As at 31.12.2015
<b>Retail segment</b>	<b>32 035 389</b>	<b>21 409 075</b>
PLN	27 417 980	18 622 111
EUR	2 324 200	1 356 917
GBP	464 471	236 508
USD	1 592 740	1 010 704
CHF	104 991	70 709
Other	131 007	112 126
<b>Corporate segment</b>	<b>19 369 459</b>	<b>12 265 601</b>
PLN	16 352 164	10 967 006
EUR	2 009 282	968 998
GBP	82 434	42 636
USD	742 870	255 253
CHF	30 206	8 159

Other	152 503	23 549
<b>Total amounts due to customers</b>	<b>51 404 848</b>	<b>33 674 676</b>

20.5.1 Ten largest depositors (without banks)	Currency	As at 31.12.2016
Company 1	EUR, PLN, USD	375 748
Company 2	EUR, PLN, USD	221 481
Company 3	PLN, USD	156 883
Company 4	PLN	100 056
Company 5	PLN	100 053
Company 6	CZK, EUR, PLN	98 910
Company 7	EUR, PLN, USD	93 721
Company 8	PLN	91 909
Company 9	EUR, PLN	85 421
Company 10	PLN	79 992

20.5.2 Ten largest depositors (without banks)	Currency	As at 31.12.2015
Company 1	PLN, EUR, USD	212 810
Company 2	PLN	203 355
Company 3	PLN, EUR, USD	175 389
Company 4	PLN	101 339
Company 5	PLN	94 042
Company 6	PLN, USD	92 645
Company 7	PLN	88 692
Company 8	PLN	72 845
Company 9	PLN, EUR, USD	72 606
Company 10	PLN	69 078

## 21. Amounts due to banks

21.1 By type	As at 31.12.2016	As at 31.12.2015
Current deposits	32 304	11 012
Overnights	856	30 701
Term deposits	0	197 826
Own issue of banking securities	20 004	32 666
Credit received	133 549	0
Other liabilities	164 710	203 262
Repo	29 812	575 561
<b>Total liabilities</b>	<b>381 235</b>	<b>1 051 028</b>

21.2 By maturity (as at the balance sheet date)	As at 31.12.2016	As at 31.12.2015
≤ 1M	227 682	918 074
> 1M ≤ 3M	0	100 288
> 3M ≤ 1Y	0	0
> 1Y ≤ 5Y	20 004	32 666
>5Y	133 549	0
<b>Total amounts due to banks</b>	<b>381 235</b>	<b>1 051 028</b>

21.3 By currency	As at 31.12.2016	As at 31.12.2015
PLN	304 280	830 987
EUR	41 366	31 401
USD	35 540	178 225

GBP	49	10 415
<b>Total amounts due to banks</b>	<b>381 235</b>	<b>1 051 028</b>

## 22. Provisions

	Provisions for disputed claims	Provisions for employee benefits	Off-balance reserve	Restructuring provision	Total provisions
As at 1 January 2016	3 219	1 070	5 512	0	9 801
Change due to the purchase of a demerged part of Bank BPH S.A.	4 439	23 594	9 642	54 714	92 389
Provisions recorded	1 321	2 273	18 630	199 668	221 892
Provisions released	-360	-16 437	-16 233	-307	-33 337
Provisions utilized	-876	0	0	-4 300	-5 176
Other changes	957	230	35	0	1 222
<b>As at 31 December 2016</b>	<b>8 700</b>	<b>10 730</b>	<b>17 586</b>	<b>249 775</b>	<b>286 791</b>

	Provisions for disputed claims	Provisions for employee benefits	Off-balance reserve	Total provisions
As at 1 January 2015.	2 513	824	4 974	8 311
Change due to the purchase of Meritum Bank ICB S.A.	705	54	0	759
Provisions recorded	3 617	301	9 551	13 469
Provisions released	-105	-109	-8 992	-9 206
Provisions utilized	-3 399	0	0	-3 399
Other changes	-112	0	-21	-133
<b>As at 31 December 2015</b>	<b>3 219</b>	<b>1 070</b>	<b>5 512</b>	<b>9 801</b>

The provision for old age and disability allowance is recognized for each employee based on an actuarial valuation prepared by an independent actuarial company. The basis for determining the value of the provision is the expected value of the old age or disability allowance which the Bank commits to paying based on the Remuneration Regulations.

In accordance with IAS 19, the financial discounting rate used to calculate provisions has been established based on market rates of return on T-bonds, whose currency and maturity are the same as those prevailing for the Bank's liabilities under employee benefits.

Alior Bank also established a restructuring provision allocated to the statutory severance pay in connection with the termination of the employment relationship within of collective dismissal and so-called additional compensation resulting from the agreement contained with the unions and the provision for costs related to the restructuring of the branch network and leave located too close to the franchised outlets (provision includes the cost of compensation and expenses related to the physical leaving the institution and restoring it to its original state). The restructuring program was announced by the Bank and its implementation began in December 2016.

Below is presented distribution of the restructuring provision at 31.12.2016 (in PLN thousand):

Severance pay for employees	174 201
The reorganization of the distribution network	75 574
	<b>249 775</b>

## 23. Other liabilities

	As at 31.12.2016	As at 31.12.2015
Interbank settlements	592 835	183 574
Taxation, customs duty, social and health insurance payables and other public settlements	38 380	25 473
Liabilities in respect of payment card settlements	65 006	4 980
Other settlements	110 710	89 810
<i>including settlements with insurers</i>	22 755	66 941
Settlements of banking certificates of deposits	112 858	680
Accruals	156 408	51 416
Income received in advance	78 286	50 356
Provision for bancassurance resignations	71 175	94 045
Provision for bonuses	74 361	9 048
Provision for unused holidays	32 169	14 166
Provision for bonuses settled in phantom shares	14 126	0
Provision for retention programs	56 378	0
Revaluation of management option plan – part settled in cash	12 075	0
Other provisions employee	870	973
Other liabilities	18 123	1 872
<b>Total other liabilities</b>	<b>1 433 760</b>	<b>526 393</b>
including financial liabilities	768 551	278 364

Settlements with insurers comprise insurance premiums relating to the cover granted by the Bank to its Customers under one of the group insurance contracts (concluded by the Bank with insurers and offered to its Customers).

As of 31 December 2016 and 31 December 2015, there were no such liabilities in respect of which the Bank did not settle its payment liabilities resulting from the contracts concluded.

In connection with the acquisition of a demerged part of Bank BPH Spółka Akcyjna with its registered office in Gdańsk comprising the core business of Bank BPH excluding operations related to mortgage loans pursuant to art. 529 § 1.4 of the Commercial Companies Code on terms specified in the Share Purchase Agreement, the Supervisory Board agreed on 29 June 2016 on the principles for the transaction bonus for the Bank's Management Board Members in order to specially motivate the Bank's Board Members to actively cooperate in the process of preparing and conducting the Transaction, to ensure timely execution of the Transaction in line with the strategic objectives. The bonus can be granted and paid once the conditions related to executing the Transaction and the Operational Merger between the banks have been fulfilled.

The Management Board of Alior Bank also launched a bonus programme for the persons that are key to carrying out the Transaction and Operational Merger processes. The bank is also continuing programmes which were launched before the Transaction date and which cover the employees of the former Bank BPH. Their purpose was to both carry out the Transaction and prepare the Operational Merger process and in the case of employees involved in the sales processes – securing the portfolio value and customer retention. Costs incurred in connection with these programs (to PLN 16 million) will be transferred to GE Capital EMEA Services Limited the Ark.

In the case of persons authorized to obtain a bonus and covered by the provisions of the Variable Salary Component Policy, the payments will be made in line with the provisions of the Variable Salary Component Policy binding at Alior Bank.

## 24. Financial assets and financial liabilities held for trading

The Bank classified derivative instruments and securities (shares, bonds) to financial assets and financial liabilities held for trading as at 31 December 2016 and 31 December 2015. Derivative transactions are concluded for trading purposes and for the purpose of managing market risk. The Bank concludes the following types of derivative transactions: FX-Forward, FX-Swap, IRS, CIRS, FRA, Commodity Futures, Commodity Forwards and Forward security transactions. Derivative financial instruments are measured on a daily basis using the discounted cash flow method. The valuation of options is performed using internal valuation models or market prices.

24.1 Derivative financial instruments (nominal value)	As at 31.12.2016	As at 31.12.2015
Interest rate transactions	21 843 663	20 013 372
SWAP	20 209 412	17 249 149
FRA	0	1 000 000
Cap Floor Options	1 634 251	1 764 223
Foreign exchange transactions	9 808 111	6 922 921
FX swap	3 655 450	1 535 293
FX forward	2 630 344	1 881 094
CIRS	1 351 094	2 639 757
FX options	2 171 223	866 777
Other options	5 857 380	4 312 272
Other instruments	725 823	618 590
<b>Derivative financial instruments (nominal value)</b>	<b>38 234 977</b>	<b>31 867 155</b>

24.2 Financial assets held for trading	As at 31.12.2016	As at 31.12.2015
Shares	6 312	1 335
Bonds	294	311
Certificates	557	1 610
Interest rate transactions	189 703	198 578
SWAP	186 532	193 522
Cap Floor Options	3 171	5 056
Foreign exchange transactions	174 953	132 012
FX swap	32 156	14 713
FX forward	60 051	49 768
CIRS	60 669	58 407
FX options	22 077	9 124
Other options	28 736	34 555
Other instruments	18 996	22 168
<b>Financial assets held for trading</b>	<b>419 551</b>	<b>390 569</b>

24.3 By maturity	As at 31.12.2016	As at 31.12.2015
Without specified maturity date	7 163	2 953

≤ 1W	8 696	4 266
> 1W ≤ 1M	33 550	35 643
> 1M ≤ 3M	44 602	24 146
> 3M ≤ 6M	22 729	38 524
> 6M ≤ 1Y	67 523	46 351
> 1Y ≤ 2Y	52 458	67 000
> 2Y ≤ 5Y	134 378	131 639
> 5Y ≤ 10Y	48 452	40 047
<b>Financial assets held for trading</b>	<b>419 551</b>	<b>390 569</b>

<b>24.4 Financial liabilities held for trading</b>	<b>As at 31.12.2016</b>	<b>As at 31.12.2015</b>
Interest rate transactions	159 056	194 355
SWAP	155 885	188 999
FRA	0	289
Cap Floor Options	3 171	5 067
Foreign exchange transactions	92 169	61 849
FX swap	22 999	1 917
FX forward	25 276	7 747
CIRS	20 948	43 058
FX options	22 946	9 127
Other options	28 693	34 555
Other instruments	18 396	19 421
<b>Financial liabilities held for trading</b>	<b>298 314</b>	<b>310 180</b>
<b>24.5 By maturity</b>	<b>As at 31.12.2016</b>	<b>As at 31.12.2015</b>
≤ 1W	4 542	1 828
> 1W ≤ 1M	30 133	9 134
> 1M ≤ 3M	36 112	17 125
> 3M ≤ 6M	25 424	54 686
> 6M ≤ 1Y	34 911	31 535
> 1Y ≤ 2Y	54 208	47 421
> 2Y ≤ 5Y	79 381	120 159
> 5Y ≤ 10Y	33 603	28 292
<b>Financial liabilities held for trading</b>	<b>298 314</b>	<b>310 180</b>

The listing below shows the hierarchy of measurement methods of financial instruments held for trading measured to fair value as at 31 December 2016 and comparative data as at 31 December 2015.

In accordance with IFRS 13, the Bank introduced the following classification:

- to level 1 – all instruments for which price quotations on active financial markets are available;
- to level 2 – instruments for which prices are not directly observable, but the prices used for measurement are based on market quotations.

To instruments of this level the discounted cash flows method is used, on the assumption that profitability curves are based on interbank market quotations (including: deposit rates, rates from: FRA, OIS, IRS, basis swap, fx swap; Forex transactions) and options measured based on internal valuation models.

- to level 3 – instruments for which at least one factor affecting the price is not based on observable market data.

Instruments of this level include options embedded in deposit certificates issued by the Bank and options concluded on the interbank market to hedge embedded option positions. The fair value is determined on the basis of the market price.

As the market risk position in respect of the specified options is in exact opposition, changes in the adopted model assumptions have no impact on changes in the fair value of the Bank's position in respect of level 3 option transactions. A change in the valuation of options on the financial assets side due to a 1% increase in the price of the base instrument will amount to PLN 5.6 million and it will be offset precisely by the change in the valuation of the option on the financial liabilities side.

In the period from 1 January to 31 December 2016, no financial instruments were reclassified from one level in the hierarchy to another.

24.6 Valuation of financial assets	As at 31.12.2016	As at 31.12.2015
<b>Level 1</b>	<b>14 625</b>	<b>13 061</b>
Shares	6 312	1 335
Bonds	294	311
Certificates	557	1 610
Other instruments	7 462	9 805
<b>Level 2</b>	<b>375 242</b>	<b>342 953</b>
SWAP	186 531	193 522
Cap Floor Options	3 171	5 056
FX swap	32 156	14 713
FX forward	60 051	49 768
CIRS	60 669	58 407
FX options	21 130	9 124
Other instruments	11 534	12 363
<b>Level 3</b>	<b>29 684</b>	<b>34 555</b>
FX options	948	0
Other options	28 736	34 555
<b>Total financial assets</b>	<b>419 551</b>	<b>390 569</b>

24.7 Movements on financial assets classified as level 3	As at 31.12.2016	As at 31.12.2015
<b>Opening balance</b>	<b>34 555</b>	<b>81 198</b>
<b>Increases, including</b>	<b>20 342</b>	<b>76 253</b>
Valuation of derivatives	6 190	28 947
Derivatives transactions	14 152	47 306
<b>Decreases, including</b>	<b>-25 213</b>	<b>-122 896</b>
Valuation of derivatives	-5 377	-78 953
Settlement/redemption	-19 836	-43 943
<b>Financial assets classified as level 3 at the end of the period</b>	<b>29 684</b>	<b>34 555</b>

24.8 Valuation of financial liabilities	As at 31.12.2016	As at 31.12.2015
<b>Level 1</b>	<b>12 289</b>	<b>15 716</b>
Other instruments	12 289	15 716
<b>Level 2</b>	<b>260 533</b>	<b>259 909</b>
SWAP	155 885	188 999
FRA	0	289

Cap Floor Options	3 171	5 067
FX swap	22 999	1 917
FX forward	25 276	7 747
CIRS	20 948	43 058
FX options	21 848	9 127
Other instruments	10 406	3 705
<b>Level 3</b>	<b>25 492</b>	<b>34 555</b>
FX options	1 098	0
Other options	24 394	34 555
<b>Total financial liabilities</b>	<b>298 314</b>	<b>310 180</b>

24.9 Movements on financial liabilities classified as level 3	<b>As at 31.12.2016</b>	<b>As at 31.12.2015</b>
<b>Opening balance</b>	<b>34 555</b>	<b>81 198</b>
<b>Increases, including</b>	<b>16 160</b>	<b>76 248</b>
Valuation of derivatives	6 336	28 942
Derivatives transactions	9 824	47 306
<b>Decreases, including</b>	<b>-25 223</b>	<b>-122 891</b>
Valuation of derivatives	-5 370	-78 948
Settlement/redemption	-19 853	-43 943
<b>Financial liabilities classified as level 3 at the end of the period</b>	<b>25 492</b>	<b>34 555</b>

The valuation and result realized on derivative transactions are presented in the trading result.

## 25. Hedge accounting

The Bank uses the principles of hedge accounting for cash flow. The objective of the hedging strategy is to hedge against interest rate risk arising from the volatility of cash flows from floating interest rate assets, using IRS transactions in PLN. Under the established hedge relationships, the hedged items are cash flows from the portfolio of PLN loans bearing floating interest rates, and the hedging items are IRS transactions under which the Bank receives fixed rate interest and pays floating rate interest. The hedged items are measured at amortized cost and the hedging items are measured at fair value.

<b>25.1. Hedging instruments (nominal value)</b>	<b>As at 31.12.2016</b>	<b>As at 31.12.2015</b>
Interest rate transactions	6 969 200	10 795 000
SWAP	6 969 200	10 795 000
<b>Hedging instruments (nominal value)</b>	<b>6 969 200</b>	<b>10 795 000</b>

<b>25.2. Financial assets held for trading-hedging instruments</b>	<b>As at 31.12.2016</b>	<b>As at 31.12.2015</b>
Level 2	71 684	139 578
Interest rate transactions	71 684	139 578
SWAP	71 684	139 578
<b>Financial assets held for trading-hedging instruments</b>	<b>71 684</b>	<b>139 578</b>

<b>25.3. By maturity</b>	<b>As at 31.12.2016</b>	<b>As at 31.12.2015</b>
> 1M ≤ 3M	13 866	2 608
> 3M ≤ 6M	21 139	62 334

> 6M ≤ 1Y	865	3 262
> 1Y ≤ 2Y	20 462	47 062
> 2Y ≤ 5Y	15 352	24 312
<b>Financial assets held for trading-hedging instruments</b>	<b>71 684</b>	<b>139 578</b>

<b>25.4. Financial liabilities held for trading-hedging instruments</b>	<b>As at 31.12.2016</b>	<b>As at 31.12.2015</b>
Level 2	6 119	0
Interest rate transactions	6 119	0
SWAP	6 119	0
<b>Financial liabilities held for trading-hedging instruments</b>	<b>6 119</b>	<b>0</b>

<b>25.5. By maturity</b>	<b>As at 31.12.2016</b>	<b>As at 31.12.2015</b>
> 6M ≤ 1Y	39	0
> 2Y ≤ 5Y	3 705	0
> 5Y ≤ 10Y	2 375	0
<b>Financial liabilities held for trading-hedging instruments</b>	<b>6 119</b>	<b>0</b>

<b>25.6 Other comprehensive income as regards cash flow hedges</b>	<b>31.12.2016</b>	<b>31.12.2015</b>
<b>Other comprehensive income at the beginning of the period, gross</b>	27 209	34 104
Gains transferred to other comprehensive income in the period	<b>-52 950</b>	14 828
Amount transferred from other comprehensive income to the income statement in the period, of which:	14 972	-21 723
- interest income	14 972	-21 723
<b>Accumulated other comprehensive income at the end of the period, gross</b>	<b>-10 769</b>	<b>27 209</b>
Tax effect	<b>2 046</b>	<b>-5 170</b>
<b>Accumulated other comprehensive income at the end of the period, net</b>	<b>-8 723</b>	<b>22 039</b>
Ineffective part of cash flow hedges recognized in the income statement	899	1 083
<b>Effect on other comprehensive income in the period, gross</b>	<b>-37 978</b>	<b>-6 895</b>
Deferred tax on cash flow hedges	7 216	1 310
<b>Effect on other comprehensive income in the period, net</b>	<b>-30 762</b>	<b>-5 585</b>

## 26. Subordinated liabilities

On 12 October 2011, the Bank signed a subordinated loan agreement with Erste Group Bank AG for EUR 10,000 thousand. The loan agreement was concluded for a period of 8 years, and the interest rate is based on 3M EURIBOR. The loan may be repaid early with 30 days prior written notice. On 15 November 2011, the Polish Financial Supervision Authority granted its permission to include the subordinated loan in Tier 2 capital. As at 31 December 2016 and 31 December 2015, the carrying amount of the loan was PLN 44,428 thousand, and PLN 42,818 thousand respectively.

On 26 September 2014, the Bank issued F-series bonds with a total nominal value of PLN 321,700 thousand. The bonds were issued for a period of 10 years (redemption date: 26 September 2024), and they bear interest based on 6M WIBOR. In accordance with the CRR Regulation, the bonds satisfy the conditions for being included in Tier 2 capital. On 28 October 2014, the Bank received the PFSA's consent to include the bonds in the Tier 2 capital

calculation. As at 31 December 2016 and 31 December 2015, the carrying amount of the bonds was PLN 325,915 thousand, and PLN 325,924 thousand respectively.

On 31 March 2015, the Bank issued G-series bonds with a total nominal value of PLN 192,950 thousand. The bonds were issued for a period of 6 years (the redemption date is 31 March 2021) and the interest rate is based on 6M WIBOR. In accordance with the CRR Regulation, the bonds satisfy the conditions for being included in Tier 2 capital. The carrying amount of the bonds as at 31 December 2016 and 31 December 2015 was 195,551 and PLN 195,555 thousand respectively.

On 4 December 2015, the Bank issued I- and I1-series bonds with a total nominal value of PLN 183,350 thousand. The bonds were issued for a period of 6 years (the redemption date is 6 December 2021) and the interest rate is based on 6M WIBOR. In accordance with the CRR Regulation, the bonds satisfy the conditions for being included in Tier 2 capital. The carrying amount of the bonds as at 31 December 2016 and 31 December 2015 was 184,076 and PLN 184,074 thousand respectively.

On 30 June 2015, in connection with the business combination with Meritum Bank, Alior Bank entered into the rights and obligations arising from the subordinated bonds issued by Meritum Bank:

- B-series bonds (with the code ISIN PLMRTMB00026) with a total nominal value of PLN 67,200 thousand issued on 29 April 2013 under the Program of Issuing Subordinated Bonds of Meritum Bank for a period of 8 years (the redemption date is 29 April 2021). The interest rate on the bonds is based on 6M Wibor. On 28 June 2013, the PFSA gave its consent to including the bonds in the Bank's Tier 2 capital. As at 31 December 2016, the carrying amount of the bonds was PLN 67,706 thousand and 31 December 2015 was PLN 67,616 thousand.

- C-series bonds (marked with the code ISIN PLMRTMB00034) with a total nominal value of PLN 80,000 thousand issued on 21 October 2014 for a period of 8 years (the redemption date is 21 October 2022). The interest rate on the bonds is based on 6M Wibor. In accordance with the CRR Regulation, the bonds satisfy the conditions for being included in Tier 2 capital. As at 31 December 2016, the carrying amount of the bonds was PLN 80,311 thousand and 31 December 2015 was PLN 80,401 thousand.

On 4 February 2016, the Bank issued EUR001-series bonds with a total nominal value of EUR 10 million. The bonds were issued for a period of 6 years (the redemption date is 4 February 2022) and the interest rate is based on 6M LIBOR. In accordance with the CRR Regulation, the bonds satisfy the conditions for being included in Tier 2 capital. As at 31 December 2016, the carrying amount of the bonds was PLN 45,331 thousand.

On 27 April 2016, the Bank issued P1A-series subordinated bonds with a total nominal value of PLN 150,000 thousand. The bonds were issued for a period of 6 years (the redemption date is 16 May 2022) and the interest rate is based on 6M WIBOR. In accordance with the CRR Regulation, the bonds satisfy the conditions for being included in Tier 2 capital. As at 31 December 2016, the carrying amount of the bonds was PLN 150,961 thousand.

On 29 April 2016, the Bank issued, P1B-series subordinated bonds with a total nominal value of PLN 70,000 thousand. The bonds were issued for a period of 8 years (the redemption date is 16 May 2024) and the interest rate is based on 6M WIBOR. In accordance with the CRR

Regulation, the bonds satisfy the conditions for being included in Tier 2 capital. As at 31 December 2016, the carrying amount of the bonds was PLN 70,425 thousand.

	As at 31.12.2016	As at 31.12.2015
<b>Liabilities included in own funds</b>	<b>1 164 794</b>	<b>896 298</b>
Subordinated loan	44 428	42 818
F-series bonds	325 915	325 924
G-series bonds	195 551	195 555
I-series bonds	150 594	150 592
I1-series bonds	33 482	33 482
Meritum Bank bonds- series B	67 706	67 616
Meritum Bank bonds- series C	80 401	80 311
EUR001-series bonds	45 331	0
P1A -series bonds	150 961	0
P1B-series bonds	70 425	0
<b>Subordinated loans</b>	<b>1 164 794</b>	<b>896 298</b>

## 27. Equity

<b>27.1 Equity</b>	<b>As at 31.12.2016</b>	<b>As at 31.12.2015</b>
Share capital	1 292 578	727 075
Supplementary capital	4 184 953	2 280 668
Other reserves	184 894	184 894
Revaluation reserve	-71 615	15 215
On measurement of available for sale assets	-62 892	-6 824
On measurement of hedging derivatives	-8 723	22 039
Foreign currency translation differences	-22	0
Current year profit/loss	632 075	311 415
<b>Total equity</b>	<b>6 222 863</b>	<b>3 519 267</b>

<b>27.2 Revaluation reserve</b>	<b>As at 31.12.2016</b>	<b>As at 31.12.2015</b>
Valuation of financial assets available for sale	-62 892	-6 824
treasury bonds	-75 156	-8 102
other bonds	-2 489	-323
deferred tax	14 753	1 601
Valuation of hedging instruments	-8 723	22 039
IRS	-10 769	27 209
deferred tax	2 046	-5 170
<b>Revaluation reserve</b>	<b>-71 615</b>	<b>15 215</b>

## 27.3 Structure of the share capital of Alior Bank S.A. as at 31 December 2016 and 31 December 2015

Share capital as at 31 December 2016

<b>Series</b>	<b>Type of shares</b>	<b>Number of shares</b>	<b>Nominal value of shares</b>	<b>Series amount by nominal value (in PLN)</b>
Series A	ordinary	50 000 000	10	500 000 000
Series B	ordinary	1 250 000	10	12 500 000
Series C	ordinary	12 332 965	10	123 329 650
Series D	ordinary	410 704	10	4 107 040
Series G	ordinary	6 358 296	10	63 582 960
Series H	ordinary	2 355 498	10	23 554 980

Series I	ordinary	56 550 249	10	565 502 490
Series J	ordinary	51	10	510
<b>Total</b>		<b>129 257 763</b>		<b>1 292 577 630</b>

#### Share capital as at 31 December 2015

Series	Type of shares	Number of shares	Nominal value of shares	Series amount by nominal value (in PLN)
Series A	ordinary	50 000 000	10	500 000 000
Series B	ordinary	1 250 000	10	12 500 000
Series C	ordinary	12 332 965	10	123 329 650
Series D	ordinary	410 704	10	4 107 040
Series G	ordinary	6 358 296	10	63 582 960
Series H	ordinary	2 355 498	10	23 554 980
<b>Total</b>		<b>72 707 463</b>		<b>727 074 630</b>

The following events occurred in the reporting period:

- On 5 May 2016, the Extraordinary General Shareholders' Meeting of the Bank passed a resolution on increasing the Bank's share capital by issuing I-series shares as part of the closed subscription conducted through a public offering, establishing 23 May 2016 as the date of exercising the pre-emptive rights to I-series shares, granting to the Supervisory Board the competence to approve the conclusion of the subissue contract, dematerialization and applying for the admission of pre-emptive rights, rights to shares and I-series shares to trading on the regulated market run by the WSE and changing the Articles of Association, as well as authorizing the Supervisory Board to agree upon the text of the consolidated Articles of Association – in the audited period, the share capital of the Bank was increased by 56 550 249 ordinary bearer I-series shares with a par value of PLN 10.00 each. On 27 June 2016, the shares were registered by the National Deposit of Securities.
- On 29 July 2016, the Extraordinary General Shareholders' Meeting of the Bank passed a resolution to increase the Bank's share capital by issuing a total of 51 J-series ordinary bearer shares with a total nominal value of PLN 510 in connection with the demerger of Bank BPH pursuant to art. 529 § 1.4 of the Commercial Companies Code. On 23 November 2016, the shares were registered by the National Deposit of Securities.

## 28. Fair value

The Bank adjusts the value of derivatives for counterparty credit risk. The amount of such adjustment is equal to the change in the valuation of derivatives resulting from the insolvency of each of the parties to the transaction (Bilateral Credit Value Adjustment). The BCVA adjustment as at 31 December 2016 amounted to PLN - 12,558 thousand. The total amount of the BCVA adjustment comprises the CVA adjustment (reflecting counterparty insolvency risk only) in the amount of PLN -13,001 thousand, and the DVA adjustment (reflecting the risk of the Bank's insolvency) in the amount of PLN 413 thousand. The BCVA adjustment as at 31 December 2015 amounted to PLN - 1,047 thousand. The total amount of the BCVA adjustment comprises the CVA adjustment (reflecting counterparty insolvency risk only) in the amount of PLN -1,366 thousand, and the DVA adjustment (reflecting the risk of the Bank's insolvency) in the amount of PLN 319 thousand

## Fair value measurement for the purposes of disclosures

The carrying amounts and fair values of assets and liabilities which are not shown in the balance sheet at fair value are presented below.

Financial instrument	Fair value hierarchy level	As at 31.12.2016		As at 31.12.2015	
		Carrying amount	Fair value	Carrying amount	Fair value
Cash and balances with the Central Bank	level 1	1 082 991	1 082 991	1 750 135	1 750 135
Loans and advances to customers	level 3	46 279 849	45 583 509	30 913 990	30 271 934
<b>Retail segment (carrying amount)</b>					
Loans for purchase of securities		125 117	125 165	119 069	119 069
Consumer loans		13 956 654	14 016 117	8 699 017	8 538 699
Consumer finance loans		1 253 001	1 246 010	748 948	755 044
Working capital facility		293 951	294 734	167 635	167 635
Credit card borrowings loans		970 319	985 514	225 629	225 349
Loans for residential real estate		8 407 632	7 874 080	6 717 911	6 317 227
Other mortgage loans		833 485	791 519	896 008	845 181
Other receivables		51 063	51 096	21 097	21 086
<b>Corporate segment (carrying amount)</b>					
Working capital facility		11 114 177	11 047 390	7 361 826	7 306 525
Car loans		131 971	135 064	70 394	70 390
Investment loans		7 517 095	7 396 298	5 487 618	5 506 929
Acquired receivables (factoring)		794 087	794 975	376 403	376 403
Reverse Repo/ BSB		680 780	680 780	0	0
Other receivables		150 517	144 766	22 435	22 397
Amounts due from banks	level 2	1 364 226	1 364 226	642 540	642 540
Assets pledged as collateral	level 1	366 984	363 067	628 332	628 332
Other assets	level 3	690 338	690 338	363 771	363 771
Amounts due to		51 786 083	51 781 044	34 725 704	34 735 315
Banks	level 2				
Current deposits		32 304	32 304	11 012	11 012
Overnights		856	856	30 701	30 701
Term deposits		0	0	197 826	197 826
Own issue of banking securities		20 004	20 004	32 666	33 008
Received Loan		133 549	133 549	0	0

Other liabilities	164 710	164 710	203 262	203 262
Repo	29 812	29 812	575 561	575 561
<hr/>				
Customers	level 3			
Current deposits	25 794 022	25 794 022	12 481 435	12 481 435
Term deposits	22 325 534	22 325 534	18 541 682	18 541 682
Own issue of banking securities	2 768 672	2 763 633	2 259 230	2 268 499
Other liabilities	516 620	516 620	392 329	392 329
Subordinated liabilities	level 3	1 164 794	1 164 794	896 298
Other liabilities	level 3	768 551	768 551	278 364
Financial guarantees	level 3	3 413	3 413	1 060

Loans and advances to customers:

In the method for calculating the fair value of loans and advances to customers customers (with the exception of overdraft facilities) the Bank compares the margins earned on newly extended loans (in the month preceding the reporting date) with the margins on the whole loan portfolio. If the margins on newly extended loans are higher than the margins on the current portfolio, the fair value of the loan is lower than its carrying amount.

All loans and advances to customers customers were classified to level 3 in the fair value hierarchy due to the fact that the valuation model with material unobservable input data, i.e. current margins obtained on newly extended loans, was applied.

Amounts due to customers and banks:

The Bank assumed that the fair values of deposits of customers and other banks and other financial liabilities with maturities below 1 year approximate their carrying amounts. Deposits are accepted daily as part of the Bank's ongoing operations; therefore, their terms are similar to the current market terms of identical transactions. Their time to maturity is short, therefore, there is no significant difference between their carrying amount and fair value.

For the purposes of disclosure, the Bank determines the fair values of financial liabilities with residual maturities (or reassessment of variable rate) above 1 year. This group of liabilities includes own issues and subordinated loans. When determining the fair value of this group of liabilities, the Bank assesses the present value of expected payments based on the current percentage curves and the original issue spread.

Own issues and subordinated loans were all classified to level 3 in the fair value hierarchy due to the fact that the valuation model with material unobservable input data was applied, including the original issue spread over the market curve. With respect to issues and subordinated loans with residual maturities (or rate reassessment) below 1 year, the carrying amount appropriately reflected the fair value of the instrument.

For the remaining financial instruments, the Bank assumes that the fair value approximates the carrying amount. This applies to the following items: cash and balances with the Central Bank, assets held for sale, other financial assets and other financial liabilities..

Financial assets and liabilities measured based on unobservable input data

Measurement for the purposes of disclosures	As at 31.12.2016	Measurement method (techniques)	Material unobservable input data
Loans and advances to customers	45 583 509	comparative valuation, discounted cash flow	margins on newly granted loans
Amounts due to customers and banks	51 781 044	discounted cash flows	issue spread above market curve
Guarantees	3 413	cash flows	future flows taking into account the amount of security
Measurement for the purposes of disclosures	As at 31.12.2015	Measurement method (techniques)	Material unobservable input data
Loans and advances to customers	30 271 934	comparative valuation	margins on newly granted loans
Amounts due to customers and banks	34 702 649	discounted cash flows	issue spread above market curve
Guarantees	1 060	cash flows	future flows taking into account the amount of security

#### Financial assets and liabilities measured based on observable input data

	Measurement method (techniques)	Material observable input data
Derivative financial instruments - instruments held for trading	Instruments are measured using the discounted cash flow method, which is based on the assumption that profitability curves are based on interbank market quotations (including: deposit rates, rates from: FRA, OIS, IRS transactions, fx swap points, fx basis swap points).	FX forward transactions: NBP fixing rates, profitability curves based on money market deposit rates and quotations of: FRA, OIS, IRS transactions; FX swap points CIRS transactions: NBP fixing rates, profitability curves based on money market deposit rates and quotations of: FRA, OIS, IRS transactions; FX basis swap points FX options: profitability curves, fx rate variability curves. OIS, IRS, FRA transactions: profitability curves based on money market deposit rates and quotations of: FRA, OIS, IRS transactions, Cap/Floor options: profitability curves, interest rate variability curves. Commodity forward transactions: futures quotation curves
Derivative financial instruments - hedging instruments	Instruments are measured using the discounted cash flow method, which is based on the assumption that profitability curves are based on interbank market quotations (including: deposit rates, rates from FRA, OIS, IRS transactions).	IRS transactions: profitability curves based on money market deposit rates and quotations of: FRA, OIS, IRS transactions
NBP bills	Fair value is determined based on the discounted cash flow method with the assumption of profitability curves	money market deposit rates

## 29. Off-balance-sheet items

29.1 Off-balance sheet contingent liabilities granted to customers	As at 31.12.2016	As at 31.12.2015
Off-balance sheet liabilities granted	14 614 625	8 941 675
Relating to financing	13 054 317	7 371 753
Guarantees	1 560 308	1 569 922
Performance guarantees	457 515	389 028
Financial guarantees	1 102 793	1 180 894
<b>Off-balance sheet liabilities granted</b>	<b>14 614 625</b>	<b>8 941 675</b>

29.2 By maturity - guarantees	As at 31.12.2016	As at 31.12.2015
≤ 1W	14 869	3 161
> 1W ≤ 1M	217 173	12 805
> 1M ≤ 3M	93 300	246 545
> 3M ≤ 6M	60 988	162 675
> 6M ≤ 1Y	233 649	249 422

> 1Y ≤ 2Y	365 396	241 726
> 2Y ≤ 5Y	182 922	275 080
> 5Y ≤ 10Y	360 120	377 746
> 10Y ≤ 20Y	31 891	762
<b>Off-balance sheet liabilities granted in respect of guarantees</b>	<b>1 560 308</b>	<b>1 569 922</b>

<b>29.3 By maturity - Relating to financing</b>	<b>As at 31.12.2016</b>	<b>As at 31.12.2015</b>
≤ 1W	2 378 831	2 266 042
> 1W ≤ 1M	731 965	12 145
> 1M ≤ 3M	423 456	307 386
> 3M ≤ 6M	682 732	184 031
> 6M ≤ 1Y	2 143 218	524 558
> 1Y ≤ 2Y	1 948 494	1 090 516
> 2Y ≤ 5Y	2 735 338	1 963 511
> 5Y ≤ 10Y	1 232 111	419 842
> 10Y ≤ 20Y	534 040	410 826
> 20Y	244 132	192 896
<b>Off-balance sheet liabilities granted in respect of financing</b>	<b>13 054 317</b>	<b>7 371 753</b>

The Bank offers to its individual customers contingent liabilities in respect of renewable checking account overdraft facilities, which are granted for an indefinite period; at the same time, close monitoring of cash inflows to the account is conducted.

Contingent liabilities in respect of credit cards are granted to individual customers for a period of three years.

The Bank grants contingent liabilities to business customers in respect of:

- current account limits for a period of 12 months;
- guarantees, for a maximum period of 6 years;
- credit cards for a period of up to 3 years;
- loans launched in tranches for a period of up to 2 years.

The guarantee amounts shown in the table above reflect the maximum possible loss which would be disclosed as at the reporting date had all customers defaulted.

## 30. Acquisition of the demerged business of Bank BPH SA

### 30.1 Description of the transaction

On 31 March 2016, the Bank signed with the sellers of Bank BPH, namely GE Investments Poland sp. z o.o., DRB Holdings B.V. and Selective American Financial Enterprises, Inc. – a Share Sale and Demerger Agreement concerning executing the transaction (in aggregate "the Transaction") comprising:

- acquisition of shares by the Bank from the Sellers of Bank BPH through an invitation to subscribe for the sale or conversion of shares in Bank BPH;
- the demerger of Bank BPH pursuant to art. 529 § 1.4 of the Commercial Companies Code carried out by transferring the Core Activities of Bank BPH to Alior Bank (demerger by spin-off) on terms discussed in the demerger plan ;
- issuing new shares of Alior Bank for the shareholders of Bank BPH indicated in the Demerger Plan (i.e. with the exception of Alior Bank, the Sellers of Bank BPH and their related entities).

Pursuant to the Share Sale and Demerger Agreement, Alior Bank acquired the Core Business of Bank BPH on 4 November 2016, i.e. on the date of the competent registration court registering the share capital increase of the Bank (through the issue of 51 ordinary shares of series J) in connection with the Demerger of Bank BPH pursuant to art. 529 § 1.4 of the Commercial Companies Code. The core business of Bank BPH will constitute a business unit comprising all the assets and liabilities of Bank BPH, with the exception of the Mortgage Operations of Bank BPH, which comprise mainly the portfolio of mortgage loans of Bank BPH (in particular all mortgage loans in PLN and other currencies granted to individuals for housing purposes).

On 4 November 2016, Alior Bank SA acquired all the primary activities of Bank BPH.

The definition of control contained in IFRS 10 specifies that subsidiaries are entities (including entities other than corporate entities, such as partnerships) controlled by the parent, which means that the parent company has a direct or indirect influence on a given entity's financial and operational policies in order to obtain economic benefits from its operations. The definition of control provides that:

- (i) an investor controls an investee when the investor is exposed, or has rights, to variable returns from its involvement with the investee and has the ability to affect those returns through its power over the investee;
- (ii) an investor controls an investee if and only if the investor has all of the following elements:
  - power over the investee;
  - exposure, or rights, to variable returns from its involvement with the investee; and
  - the ability to use its power over the investee to affect the amount of the investor's returns;
- (iii) to have power over an investee, an investor must have existing rights that give the current ability to direct the relevant activities; in assessing power one must take into account only significant rights, other than protective rights;
- (iv) assessing whether an investor has power over an investee depends on the significant activities, the way decisions are made concerning significant activities, and the rights held by an investor and other entities towards the investee.

Alior Bank is of the opinion that the control of the Core Business of Bank BPH acquired on 4 November 2016. According to the Share Purchase Agreement in the period between completing the Invitation and the earlier of:

- (i) the Demerger Date
- (ii) the date six months after completion of the Invitation,

Alior Bank agreed not to execute any rights arising from the shares of Bank BPH without the prior written consent of the Sellers of Bank BPH, in recognition of any exceptions provided for in the Share Sale and Demerger Agreement. In the Transitional Period, the Sellers of Bank BPH shall remain reference shareholders of Bank BPH.

### **Price**

In the report dated 2 August 2016, the Bank informed that the price for acquiring the Core Business of Bank BPH was adjusted to PLN 1 159 645 000. The Adjusted Price has been determined in accordance with the Share Purchase and Demerger Agreement, based on the book value of tangible assets of the Core Business of Bank BPH as at 30 June 2016.

As part of the Invitation and Compulsory Redemption Bank paid the amount of PLN 305 298 thousand for minority shareholders.

The basis for a final settlement between the sellers Alior Bank and Bank BPH is the book value of the tangible assets of the Core Business of Bank BPH on 4 November 2016 including any additional adjustments provided for in the Share Purchase Agreement. The purchase price payable to the sellers of Bank BPH has been calculated by Alior Bank in the amount of PLN 1 066 883 000. In addition, according to estimates of Alior Bank in order to ensure the CET 1 level of 13.25% (described below), tangible assets of Core Business should be complemented by Bank BPH the amount of PLN 52 194 thousand. Currently being negotiated between the parties of those transactions with regard to confirmation by Alior Banks and sellers Bank's book value of tangible assets of the Core Business of Bank BPH and the final settlement of the purchase price between the parties. Until the date of approval of these financial statements has not yet agree on the final settlement of the purchase price between the parties. If no agreement is reached in this regard the agreed date, the Share Purchase Agreement provides for the settlement of discrepancies between Alior Bank and sellers of Bank BPH by an expert, which will audit company appointed in accordance with the Share Purchase Agreement. Expert decision will be binding for the parties.

## Terms

The execution of the Transaction depended on fulfilling the conditions to obtain the relevant regulatory approvals for the transaction and the operations formal under the Commercial Code.

On 23 June 2016, the President of the Office of Competition and Consumer Protection issued unconditional approval to carrying out the concentration comprising the acquisition of a part of Bank BPH assets by the Bank.

On 19 July 2016, Alior Bank and Bank BPH received a decision from the PFSA on granting its approval for the Demerger of Bank BPH pursuant to art. 529 § 1 clause 4 of the CCC by transferring to Alior Bank a part of the assets Bank BPH in the form of a business unit comprising all the assets and liabilities of Bank BPH, with the exception of the so-called "mortgage activities of Bank BPH". In addition, the transaction required to obtain a number of other decisions of the PFSA by both parties and their main shareholders.

The first notice to shareholders about the Demerger within the meaning of art. 539 § 1 and 2 of the Commercial Code in connection with art. 402 (1) Commercial Code took place on 30 April 2016.

On June 30 2016 the Management Board of Alior Bank SA acting on the basis of disposal referred to the previous sentence the second time informed about the planned demerger of Bank BPH by separation of an organized part of the enterprise of Bank BPH business related other than the called. "Mortgage activity" and its transfer to Alior Bank. The Demerger Plan was established the following share exchange ratio: per 1 (one) share of BPH Bank BPH shareholder (with the exception of the shareholders of GE and Alior Bank) will be issued and allotted 0.44 shares of Alior Bank, subject to adjustment related to the dilution of Alior Bank the share capital resulting from Alior Bank public offering of pre-emptive right before the demerger. Exchange ratio of shares after taking into account the above adjustments related to the dilution of the share capital of Alior Bank was set rounded to 0.51

## Offering based on Pre-emptive Rights

On 10 June 2016, the Bank's Management Board informed that the public offering and issuance of 56 550 249 ordinary bearer I-series shares with a par value of PLN 10 each - came into effect.

On 24 June 2016, the District Court for the Capital City of Warsaw in Warsaw, 13th Business Department of the National Court Register entered in the register of businesses maintained

for the Bank the Bank's share capital increase from PLN 727 074 630 to PLN 1 292 577 120 by this issuing.

For Stock Exchange trading the new shares entered into on 1 July 2016.

### **Invitation**

On 1 August 2016, subscriptions began for the sale of shares of Bank BPH based on the invitation announced by Alior Bank. The subscription lasted until 16 August 2016 and the expected date of the transaction settlement was 24 August 2016.

As a result of Invitation Alior Bank acquired 46 525 228 shares of Bank BPH from sellers of Bank BPH and other shareholders for a total price of PLN 1 451 122 thousand.

### **Squeeze-Out**

On 26 August 2016 entered into force, the agreement between Alior Bank and sellers of Bank BPH, referred to in art. 87.1 point 5 of the Act on Public Offering (the "Agreement") regarding the acquisition of shares of Bank BPH by requests from all other shareholders of Bank BPH sell all their shares of BPH Bank in accordance with art. 82 of the Act on Public Offering ("Compulsory Redemption").

The agreement entered into force in motion by Alior Bank 25 August 2016 to Bank's BPH sellers requests for action to carry out the Squeeze-Out.

As a result of Squeeze-Out Alior Bank purchased 442 923 shares of Bank BPH Group for a total price of PLN 13 815 thousand.

As a result of the entry into force of the Agreement Alior Bank and GE Shareholders crossed the threshold of a total of 90% of the total number of votes at the General Meeting of Bank BPH

### **Additional agreements related to the Share Sale and Demerger Agreement**

On 29 April 2016, the Bank concluded with Bank BPH S.A.: (i) an outsourcing agreement on servicing the portfolio of mortgage receivables of Bank BPH S.A. ("Ops SLA"); and (ii) an outsourcing agreement concerning the provision of IT services to Bank BPH S.A. ("IT SLA") (together "the Agreements").

The IT SLA is related to the provision of IT services to Bank BPH S.A. that are necessary to Bank BPH S.A. in conducting its operations as before after moving the IT platform of Bank BPH S.A. to the Bank as part of the Core Business of Bank BPH. The IT services will comprise: (i) services supporting the business processes of Bank BPH S.A.; (ii) services supporting IT processes of Bank BPH S.A.; (iii) user support services; and (iv) *ad hoc* and project related services. The Bank will be obliged to maintain the dedicated IT platform for the purpose of providing services based on the IT SLA.

Ops SLA is related to the provision of widely defined administration and operational services concerning the servicing of the mortgage portfolio retained by Bank BPH S.A. after the demerger and transferring the Core Business of Bank BPH to the Bank.

In accordance with the Agreements, the Bank will receive reimbursement of the costs actually incurred in connection with the provision of the services, calculated in accordance with the agreed methodology ("the Costs").

Both Agreements were concluded for an indefinite period and shall expire on the earlier of: (i) upon complete settlement of mortgage receivables of Bank BPH S.A.; or (ii) after 30 (thirty) years from the Effective Date. Each Agreement can be terminated earlier on terms agreed between the parties.

### **Strategic justification of the Transaction**

The acquisition of the core business of Bank BPH is in line with the development strategy of Alior Bank which envisages development based on organic growth and acquisitions, in association with achieving a high rate of return from capital. As a result of acquiring the business of Bank BPH, Alior Bank will advance to the position of the 9th largest bank in Poland in terms of assets held. The transaction will bring Alior Bank closer to the execution of its strategic goal of being counted among the 5 or 6 largest banks in Poland within the next few years.

### 30.2 Settlement of the acquisition

The transaction was settled under the acquisition method in accordance with IFRS 3, Business Combinations, the application of which requires, among other things, the recognition and measurement of identifiable assets and liabilities acquired, which were measured at fair value as at the date of acquisition and all non-controlling interests in the acquiree, and recognition and measurement of goodwill or gain on bargain purchase.

The table below shows the identifiable assets and liabilities acquired as at the date of acquisition:

Assets	Balance as at 4.11.2016	Adjustments to the fair value measurement and off	Identifiable acquired assets measured at fair value
Cash and balances with the Central Bank	1 043 097	0	1 043 097
Financial assets designated as at fair value through profit or loss (balancing amount)	3 691 205	0	3 691 205
Amounts due from banks	398 537	0	398 537
Loans and advances to customers	8 844 623	364 995	9 209 618
including: loan impairment provision	-782 145	0	-782 145
Financial assets available for sale	301 110	0	301 110
Property, plant and equipment	247 517	23 160	270 677
Intangible assets	144 939	-55 425	89 514
In this recognized customer relationships	0	42 100	42 100
Income tax asset	137 394	-63 218	74 176
Other assets	197 158	0	197 158
<b>Total assets</b>	<b>15 005 580</b>	<b>269 512</b>	<b>15 275 092</b>

Liabilities	Balance as at 4.11.2016	Adjustments to the fair value measurement and off	Identifiable acquired assets measured at fair value
Amounts due to banks	369 631	0	369 631
Amounts due to clients	12 534 361	0	12 534 361
Liabilities evidenced by certificates	223 813	0	223 813
Provisions	101 326	20 100	121 426
Financial liabilities designated as at fair value through profit or loss	38 249	0	38 249
Other liabilities	136 721	0	136 721
<b>Total liabilities</b>	<b>13 404 101</b>	<b>20 100</b>	<b>13 424 201</b>

	BPH	Changes of accounting principles	Adjustments to the fair value measurement and off	Identifiable acquired assets measured at fair value
<b>Fair Value of net assets</b>	<b>1 601 479</b>	<b>-22 849</b>	<b>249 412</b>	<b>1 828 042</b>

### 30.3 Description of fair value measurement methods

#### Loans and advances to customers

The portfolio of loans and advances granted to customers acquired under the acquisition transaction of Bank BPH SA which was measured at fair value as at the acquisition date was presented in the financial statements without netting off, i.e. the gross value (including fair value adjustment) and impairment allowances were presented as separate line items. This was because the information thus presented is more useful and it reflects the market practice applied by banks.

By type	The fair value of the identifiable receivables from customers
<b>Retail segment</b>	<b>5 522 326</b>
Working capital facility	134 234
Consumer loans	4 882 700
Loans for purchase of securities	9 992
Credit card borrowings loans	466 897
Loans for residential real estate	7 428
Other receivables	21 075
<b>Corporate segment</b>	<b>4 469 437</b>
Working capital facility	2 684 142
Car loans	131 256
Investment loans	772 177
Acquired receivables (factoring)	310 292
Other receivables	571 570
<b>Total impairment allowances and IBNR</b>	<b>-782 145</b>
<b>Amounts due from customers</b>	<b>9 209 618</b>

The fair value measurement of the loan portfolio was performed based on the following assumptions:

1. Fair value was calculated separately for the loan portfolio without indications of impairment (performing) and with indications of impairment (non-performing). This resulted from different characteristics of cash flows for the two portfolios. In the case of performing loans the calculation was based on contractual cash flows adjusted for credit risk and early repayments, where they were material. In the case of non-performing loans the calculation was based on expected recoveries.
2. For products without contractual maturity dates in the portfolio of performing loans (with the exception of credit cards of retail customers) it was adopted that fair value is equal to book value. This resulted from the assumption concerning possible immediate repayment of these liabilities. This applies to the following products: bank overdrafts, credit cards of commercial customers, renewable commercial loans and factoring.
3. Loans with a repayment schedule (and credit cards of retail customers) were measured using the discounted cash flows model.

- a. Contractual cash flows adjusted for credit risk and early repayments were discounted. The discount rate comprised: the market rate, liquidity margin used in the system of transfer funds (STF), margin on cost of capital and margin on costs of servicing the loan portfolio.
- b. The adjustment for credit risk consisted of multiplying the cash flows by the value  $(1 - PD \cdot LGD)$ , where PD is the probability of the customer's default from the cash flow date and LGD is loss given default at the cash flow date.
- c. Market interest rates were taken from the yield curve built based on the money market rates (for example, WIBOR for PLN) and FRA contracts for the short end of the curve and the IRS rate for the long end of the curve. A different yield curve was used for each currency (PLN, EUR, USD, CHF, GBP, SEK) that was appropriate to it.
- d. The liquidity margin has been assigned according to the transfer price system currently binding in Alior Bank. The margin depends on the currency and the payment date of a given cash flow. The margin levels binding at Alior Bank are higher than those in former BPH and have been considered consistent with those commonly used on the market.
- e. The cost of capital has been calculated using the CAPM model and amounted to 8.76%. The margin on the cost of capital at discount has been calculated by multiplying the cost of capital by the proportion of capital in total assets / total equity and liabilities of Core BPH (9.62%) and amounted to 0.8423%.
- f. The margin on the cost of servicing the portfolio has been estimated by the business units. Its amount depends on the customer segment.

4. Commercial and retail loans have been modelled separately.

### **Customer relationships in the area of deposits**

Customer relationships in the area of deposits were analysed for two main products:

- current accounts;
- term deposits and savings accounts.

The valuation of customer relationships was performed on the basis of an analysis of core deposits.

Core deposits represent the hypothetical savings for the Bank arising from the fact that the Bank's customers maintain their cash on low-interest current accounts for a long time, instead of higher-interest term deposits. This enables the Bank to limit the higher-interest rate financing from the market and effectively reduce interest expense.

Fair value estimation of customer relationships based on core deposits is based on the assumption that their value is gradually reduced. Due to difficulties in assessing customer behaviour it was prudently adopted in the estimate that the pace of the core deposits withdrawal will be from 1 to 3 years.

As a result of acquiring the spun off business of Bank BPH, as at 4 November 2016 customer relationships were recognized in an amount of PLN 42.1 million. They are amortized over a period of 2 years. The carrying value of customer relations as at 31 December 2016 was PLN 40.3 million.

### **IT systems**

The IT systems of Bank BPH S.A. have been divided into four groups, depending on the value in use of those systems.

In the case of the purchased systems (external systems), the gross value was established as the sum of financial outlays incurred on their purchase. In the case of internally developed

systems, their gross value constituted the sum of capitalized expenditure incurred on their manufacture. The above system values have been adjusted for the remaining horizon of their operational use, which has been specified as a percentage parameter of the length of the system's economic life cycle compared with the assumed period of operational use. The remaining horizon of the system's use has been established individually for each system and is a ratio of the expected period of the system's use from the measurement date to the system's age calculated from the implementation period until the measurement date.

In the case of systems in the course development, a similar model was adopted as for the purchased and internally developed systems.

Additionally, the fair value of systems in the course of development was adjusted for expenditure incurred on functionalities with respect to which development works have not been completed or which have not been tested and are not ready to be commissioned.

### Property, plant and equipment

The valuation of property (buildings) of the acquired company has been performed under the income method. This approach comprises determining the property's value on the assumption that the price that a buyer will pay for the property depends on the expected income that can be obtained from the property.

The valuation of land was carried out under the comparative approach using the comparison in pairs method or the average price adjustment method. Under the method of comparison in pairs, property subject to valuation, the characteristics of which are known, is compared to similar properties which were traded on the market and their transaction prices, transaction terms and prices of these properties are known.

### Lease agreement

IFRS 3 requires the recognition of the identifiable assets, liabilities and contingent liabilities that meet the recognition criteria at their fair values at the acquisition date. With regard to onerous contracts and other identifiable liabilities of the acquiree, the acquirer uses the present value of amounts due in order to meet its obligations, determined using appropriate current interest rates.

The table below presents the effects of the valuation of lease agreements, which party after the acquisition date became Alior Bank.

assessment of rent	rent to the end of the contract	The amount of "overpayment" regards to the market in PLN	Number of lease agreement	% Rent to the grand total rents (col. B)
above the market rent	54 943	20 763	111	26.24%
market rent or lower	154 480	-1 576	105	73.76%
<b>Total</b>	<b>209 423</b>	<b>19 187</b>	<b>216</b>	<b>100%</b>

For purposes of the above calculation, the following assumptions:

- rents defined in the agreements concluded by Bank BPH compared with market values, based also on the experience of their own at selected locations,
- in order to calculate the value of rents to the end of the contract for permanent contracts assumed duration of one year from the date of the legal merger or dates specified in the restructuring plan.

### The calculation of bargain purchase (ie. Negative goodwill)

Bank made the initial accounting for this business combination and calculated bargain purchase in connection with the acquisition of a demerged part of Bank BPH SA.

**The calculation of a bargain purchase is presented in the table below:**

<b>calculation of a bargain purchase</b>	
the price paid to shareholders of BPH from GE Group	1 159 645
the price paid to the other shareholders of BPH	305 298
receivable from BPH due to adjustments of net assets to a level corresponding to the CET 1 ratio 13.25%	52 194
receivable from GE Group shareholders arising from the adjustment of the purchase price	92 762
the fair value of the net assets of the acquiree	1 828 042
<b>Gain on bargain purchase</b>	<b>508 056</b>

According to Demerger Plan and the terms of the agreement of 17 October 2016 concluded between Bank BPH and Alior Bank concerning the distribution and co-operation after the demerger (org. Demerger Implementation And Post Demerger Cooperation Agreement), the net assets resulting from the demerger of Bank BPH calculated on the basis of risk-weighted assets should provide a CET 1 level equal to 13.25%.

According to Alior Bank's risk-weighted assets presented in the demerger balance on 4 November 2016 year does not meet the conditions described in the above sentence. According to calculations made by Alior Bank the amount of mismatches to outstanding level of CET 1 is PLN 52 194 thousand.

The amount of PLN 92 762 thousand was calculated by Alior Bank based on Share Purchase Agreement according to algorithm used in the calculation of the initial purchase price (paid on August 24, 2016.). In addition, the settlement includes adjustments resulting from the above cited Agreement. The Bank informed the GE Group to draw up a settlement on 9 January 2017. The settlement was rejected by the GE Group on 8 February 2017. Further arrangements in this regard will be carried out in accordance with the principles described in Note 30.1 above (paragraph "Price").

The settlement of the purchase price of demerged part of Bank BPH has been prepared by the Management Board on the basis of the calculation resulting from the agreements. The final settlement, however, will be subject to arrangements between Alior Bank and sellers of demerged part of Bank BPH.

Accordingly the settlement of the purchase price made on 31 December 2016 is preliminary and may change, most probably in the range of PLN 20 to 40 million if Alior Bank becomes aware of new information that will apply as of 31 December 2016 and which are not known at the date of the consolidated financial statements for 2016. in accordance with IFRS 3.45 a maximum period to make changes to the settlement of the purchase price shall expire 12 months from the date of purchase, ie. on 4 November 2017.

Possible changes (if any) will be made retrospectively (will be recognized in shareholders' equity). Currently, a fixed surplus of fair value of acquired assets and liabilities at the acquisition date over the acquisition price, Alior Bank puts it in accordance with IFRS 3.34, directly in result as the gain on bargain purchase (shown as a separate item in the profit and loss account).

The gain on the bargain purchase arose as a result of the Management Board of Alior Bank S.A. negotiating a favourable transaction price. This was possible because GE Group had made decision about quickly withdraw from the banking services in Poland.

The difference between the book value of the acquired assets of the business of BPH SA and the fair value measurement of these assets will be amortized to the income statement over the economic useful life of each asset acquired.

#### 30.4 Other disclosures

In accordance with IFRS 3 because the transaction mergers and acquisitions took place during the reporting period. Below was presented the profit and loss account of demerged part of Bank BPH from acquisition day to 31 December 2016. In this calculation were included cost incurred until 31 December 2016 integration costs in the amount of PLN 37 045 thousand and the cost of restructuring provision of PLN 268 121 thousand.

Also presented the profit and loss account for the twelve months ended December 31, 2016 shown as if the acquisition date of demerged part of Bank BPH SA fell as of 1 January 2016. In this presentation, the following assumptions:

- all items of income and expense presented in the profit and loss account of the acquired entity from the date of acquisition until December 31, 2016 has been multiplied by 6,
- one-off costs, like a restructuring provision included only once,
- banking tax was assessed on the basis of 11 months from 1 February 2016.

The income statement of the acquired company from the date of acquisition until 31 December 2016

	4.11.2016-31.12.2016
Interest income	97 175
Interest expense	-12 573
<b>Net interest income</b>	<b>84 602</b>
<b>Dividend income</b>	<b>0</b>
Fee and commission income	45 319
Fee and commission expense	-27 093
<b>Net fee and commission income</b>	<b>18 226</b>
<b>Trading result</b>	<b>4 173</b>
<b>Net gain (realized) on other financial instruments</b>	<b>9</b>
Other operating income	26 414
Other operating costs	-1 362
<b>Net other operating income</b>	<b>25 052</b>
<b>General administrative expenses</b>	<b>-416 151</b>
<b>Impairment losses &amp; provisions</b>	<b>-12 159</b>
Banking tax	-6 087
<b>Profit before tax</b>	<b>-302 334</b>
Income tax	52 594
<b>Net loss</b>	<b>-249 740</b>

The income statement of Alior Bank presented as though the acquisition date of the units fell as at the start of the reporting period, i.e. 1 January 2016 prepared according rules mentioned above.

	Period from 01.01.2016 to 31.12.2016
Interest income	3 419 735
Interest expense	-1 054 849
<b>Net interest income</b>	<b>2 364 886</b>
<b>Dividend income</b>	<b>68</b>
Fee and commission income	818 932
Fee and commission expense	-393 445

<b>Net fee and commission income</b>	<b>425 487</b>
<b>Trading result</b>	<b>340 644</b>
<b>Net gain (realized) on other financial instruments</b>	<b>21 964</b>
Other operating income	192 084
Other operating costs	-58 530
<b>Net other operating income</b>	<b>133 554</b>
<b>Bargain purchase</b>	<b>508 056</b>
<b>General administrative expenses</b>	<b>-2 283 604</b>
<b>Impairment losses &amp; provisions</b>	<b>-855 528</b>
<b>Banking tax</b>	<b>-158 329</b>
<b>Profit before tax</b>	<b>497 198</b>
<b>Income tax</b>	<b>-48 296</b>
<b>Net profit</b>	<b>448 903</b>

Transaction costs related to the acquisition of demerged part of BPH amounted to PLN 34 294 thousand were recognized directly in profit and loss account. The total costs of issuing of ordinary shares of series I amounted to PLN 41 433 thousand were recognized in supplementary capital.

### 31. Acquisitions of Spółdzielcze Kasy Oszczędnościowo-Kredytowe

On 26 January 2016, the Polish Financial Supervision Authority (PFSA) made a decision concerning the acquisition of Spółdzielcza Kasa Oszczędnościowo-Kredytowa im. Stefana Kard. Wyszyńskiego (SKOK Września) by Alior Bank S.A.

On 27 January 2016, the Management Board of Alior Bank S.A. took up management of the assets of SKOK Września. On 1 March 2016, Alior Bank S.A. (as the acquiring bank) acquired SKOK Września. In accordance with art. 74c clause 4 of the Act on cooperative savings and credit unions, as of the date of acquisition, the acquiring union or national bank enters into all the rights and obligations of the acquired union. Until the date of acquisition by Alior Bank S.A., SKOK Września conducted operations and offered services to its members within the full extent applied so far.

The acquisition of SKOK Września by Alior Bank S.A. will ensure full security of the funds accumulated in the acquired Union and will ensure to the members of SKOK Września access to a wider product offer of Alior Bank S.A.

The acquisition of SKOK Września was accounted for in accordance with IFRS 3. The acquisition did not involve any consideration on the part of the Bank. The process of acquisition of SKOK Września will be carried out with financial support from the BGF pursuant to art. 20g of the Act of 14 December 1994 on the Bank Guarantee Fund. The Bank will obtain support from the BGF in the form of a subsidy to cover the difference between the value of the acquired property rights and the liabilities in respect of guaranteed funds on the deposit accounts the amount of which has been initially determined at PLN 52,534 thousand and recorded in other assets.

Presented below is the value of the acquired assets and liabilities:

<b>Assets</b>	
Amounts due from customers	95 351
Amounts due from banks (including the Central Credit Union [Kasa Krajowa])	11 094
Other financial instruments measured at fair value through profit or loss	3 790
Other assets	1 617
<b>Total assets on acquisition date</b>	<b>111 852</b>

<b>Liabilities and equity</b>	
Amounts due to customers guaranteed by the BGF	164 385
Other liabilities	2 734
<b>Total liabilities on aquisition date</b>	<b>167 119</b>
<b>Total net identifiable assets</b>	<b>-55 267</b>
Received subsidy	52 534
Changes in accounting principles	-935
<b>Goodwill</b>	<b>3 668</b>

In the part not covered by the BGF support (mainly trade payables) and due to significant differences in accounting policies, goodwill of PLN 3 668 thousand has been generated, and the Bank charged the goodwill to the income statement on a one-off basis.

On 26 April 2016, the PFSA made a decision concerning the acquisition of Powszechna SKOK in Knurów (SKOK Knurów) by Alior Bank S.A. As of 27 April 2016, the Management Board of Alior Bank S.A. took up the management of the assets of SKOK Knurów. As of 1 June 2016, SKOK Knurów was acquired by Alior Bank S.A. as the acquirer. In accordance with art. 74c clause 4 of the Act on cooperative savings and credit unions, as of the date of acquisition, the acquiring union or national bank enters into all the rights and obligations of the acquired union. Until the date of acquisition by Alior Bank S.A., SKOK Knurów conducted operations and offered services to its members within the full extent applied so far.

The acquisition of SKOK Knurów was accounted for in accordance with IFRS 3. The process of the acquisition of SKOK Knurów is conducted with financial support granted by the BGF pursuant to art. 20g of the Act of 14 December 1994 on the Bank Guarantee Fund. The Bank will obtain support from the BGF in the form of a subsidy to cover the difference between the value of the acquired property rights and the liabilities in respect of guaranteed funds on the deposit accounts the amount of which has been initially determined at PLN 9 530 thousand.

Presented below are the initial values of the acquired assets and liabilities:

<b>Assets</b>	
Amounts due from customers	15 775
Amounts due from banks (including Kasa Krajowa)	9 691
Other assets	731
<b>Total assets on aquisition date</b>	<b>26 197</b>
<b>Liabilities and equity</b>	
Amounts due to customers guaranteed by BGF	35 507
Other liabilities	5 943
<b>Total liabilities on aquisition date</b>	<b>41 450</b>
<b>Total net identifiable assets</b>	<b>-15 253</b>
Received subsidy	9 530
Changes in accounting principles	-861
<b>Goodwill</b>	<b>-6 584</b>

In the part not covered by the BGF support (mainly trade payables) and due to significant differences in accounting policies, goodwill of PLN 6,584 thousand has been generated. The Bank charged the goodwill to the income statement on a one-off basis.

## 32. Cash flow statement – additional information

In the cash flow statement, cash and cash equivalents cover balances maturing in a period shorter than 3 months.

The Bank's cash flows from operating activities cover mainly lending, deposit activities, foreign exchange and purchase and sale of securities.

The Bank's investing activities cover the purchase and sale of fixed assets and intangible assets.

The Bank's financing activities comprise the loan taken.

The Bank prepares its cash flow statement in respect of operating activities using the indirect method, whereby the net profit/loss for the reporting period is adjusted by the effect of non-cash transactions, prepayments, accruals and deferred income relating to past or future inflows or outflows of funds from operating activities.

32.1 Cash and cash equivalents	As at 31.12.2016	As at 31.12.2015
Cash and balances with the Central Bank	1 082 991	1 750 135
Current accounts with other banks	386 766	339 131
Term accounts with other banks	237 396	112 946
<b>Total</b>	<b>1 707 153</b>	<b>2 202 212</b>

\* without interest

32.2 Operating activities – change in the balance of loans and other receivables	1.01.2016 - 31.12.2016	1.01.2015 - 31.12.2015
Change in receivables from customers – statement of financial position	-15 365 859	-4 313 942
Change in amounts due from banks – statement of financial position	-721 686	-195 443
Change in cash and cash equivalents in the balance sheet – nostro accounts	47 635	47 691
Change in cash and cash equivalents in the balance sheet – deposits up to 3 months	124 334	106 553
<b>Change in the balance of loans and other receivables</b>	<b>-15 915 576</b>	<b>-4 355 141</b>

32.3 Operating activities – change in the balance of other liabilities	1.01.2016 - 31.12.2016	1.01.2015 - 31.12.2015
Increase/(decrease) in other liabilities – statement of financial position	907 367	-248 727
Change in revaluation reserve – statement of financial position	-66 462	-6 211
Change in the balance of other liabilities measured at amortized cost - statement of financial position	-339 123	-136 320
Change in the deferred income tax provision in the revaluation reserve	-20 368	-1 457
Accrued expenses in respect of purchasing fixed assets	-10 057	19 681
Accrued expenses in respect of purchasing intangible assets	-8 167	267
Change due to purchase of BPH shares, net of cash acquired	174 695	0
Other comprehensive income	58 287	38 705
<b>Change in the balance of other liabilities</b>	<b>696 172</b>	<b>-334 063</b>

32.4 Operating activities – change in the balance of other assets	1.01.2016 - 31.12.2016	1.01.2015 - 31.12.2015
Net increase/decrease in other assets – statement of financial position	-394 399	-16 378
<b>Change in the balance of other assets</b>	<b>-394 399</b>	<b>-16 378</b>

32.5 Investing activities – purchase of property, plant and equipment	1.01.2016 - 31.12.2016	1.01.2015 - 31.12.2015
Change in balance – statement of financial position	-317 754	-98 797

<b>Purchase of property, plant and equipment</b>	<b>-317 754</b>	<b>-98 797</b>
<b>32.6 Investing activities – purchase of intangible assets</b>	<b>1.01.2016 - 31.12.2016</b>	<b>1.01.2015 - 31.12.2015</b>
Change in balance – statement of financial position	-154 349	-72 281
<b>Purchase of intangible assets</b>	<b>-154 349</b>	<b>-72 281</b>
<b>32.7 The acquisition of demerged business of Bank BPH, net of cash acquired</b>		<b>As at 4.11.2016</b>
Payment for BPH shares		-1 464 933
Cash and balances with the Central Bank		1 043 097
Current accounts with other banks		73 811
Term accounts with other banks		173 330
<b>Total</b>		<b>-174 695</b>

### 33. Assets pledged as collateral

<b>33.1 Balance sheet value</b>	<b>As at 31.12.2016</b>	<b>As at 31.12.2015</b>
Treasury bonds blocked with REPO transactions	29 783	576 534
Registered pledge on Treasury bonds	118 048	37 060
Deposit as collateral of transactions performed in Alior Trader	1 252	14 738
Investment securities held to maturity	217 901	0
<b>Total</b>	<b>366 984</b>	<b>628 332</b>

In addition to assets pledged as collateral, which are presented in the statement of financial position separately and which the recipient may sell or exchange for another security, the Bank held the following other assets pledged as collateral which did not meet this criterion:

	<b>As at 31.12.2016</b>	<b>As at 31.12.2015</b>
Treasury bonds blocked with BFG	204 411	159 570
Deposits as derivative transactions (ISDA) collateral	145 141	171 406
<b>Total</b>	<b>349 552</b>	<b>330 976</b>

### 34. Transactions with related entities

The parent company of the Bank is Powszechny Zakład Ubezpieczeń S.A. (PZU S.A.) The related parties of the Group PZU SA and its related companies and entities related to members of the Management and Supervisory Board. By PZU S.A., the Bank is indirectly controlled by the Treasury.

In the following tables show the type and value of transactions with affiliates and subsidiaries.

On 31 December 2016, the Bank had the following subsidiaries:

- Alior Services Sp. z o.o. (formerly Alior Raty Sp. z o.o.) – a direct subsidiary (100% interest);
- Alior Leasing Sp. z o.o. – a direct subsidiary (100% interest);
- Meritum Services ICB SA – a direct subsidiary (100% interest);
- NewCommerce Sp. z o.o. – a direct subsidiary (100% interest);

- Absource Sp. z o.o. – a direct subsidiary (100% interest);
- Centrum Obrotu Wierzytelnościami Sp. z o.o. – a direct subsidiary (100 % interest);
- Money Makers S.A. – a direct subsidiary (58.84% interest).

On 31 December 2015, the Bank had the following subsidiaries:

- Alior Services Sp. z o.o. (formerly Alior Raty Sp. z o.o.) – a direct subsidiary (100% interest);
- Alior Leasing Sp. z o.o. – a direct subsidiary (100% interest);
- Meritum Services ICB SA – a direct subsidiary (100% interest);
- NewCommerce Sp. z o.o. – a direct subsidiary (100% interest);
- Centrum Obrotu Wierzytelnościami Sp. z o.o. – a direct subsidiary (98.04% interest);
- Money Makers S.A. – a direct subsidiary (60.49% interest).

The following tables present the type and value of transactions with related entities and subsidiaries.

Subsidiaries	As at 31.12.2016	As at 31.12.2015
<b>Assets</b>		
Loans and advances to customers	370 250	59 263
Other assets	4 760	409
<b>Total assets</b>	<b>375 010</b>	<b>59 672</b>
<b>Liabilities</b>		
Amounts due to customers	40 267	11 134
Provisions	125	0
Other liabilities	854	0
<b>Total liabilities</b>	<b>41 246</b>	<b>11 134</b>

Parent company	As at 31.12.2016	As at 31.12.2015
<b>Liabilities</b>		
Amounts due to customers	24	0
Provisions	4	0
<b>Total liabilities</b>	<b>28</b>	<b>0</b>

Subsidiaries of the parent company	As at 31.12.2016	As at 31.12.2015
<b>Assets</b>		
Available-for-sale financial assets	84 961	0
Loans and advances to customers	41	41
<b>Total assets</b>	<b>85 002</b>	<b>41</b>
<b>Liabilities</b>		
Amounts due to customers	128 703	7 809
Provisions	3	0
<b>Total liabilities</b>	<b>128 706</b>	<b>7 809</b>

Subsidiaries	As at 31.12.2016	As at 31.12.2015
<b>Off-balance sheet liabilities granted to customers</b>	<b>130 972</b>	<b>9 191</b>
Relating to financing	75 230	7 507
Guarantees	55 742	1 684

Parent company	As at 31.12.2016	As at 31.12.2015
----------------	------------------	------------------

<b>Off-balance sheet liabilities granted to customers</b>	<b>15 000</b>	<b>0</b>
Guarantees	15 000	0
<b>Subsidiaries of the parent company</b>	<b>As at 31.12.2016</b>	<b>As at 31.12.2015</b>
<b>Off-balance sheet liabilities granted to customers</b>	<b>9 900</b>	<b>0</b>
Guarantees	9 900	0
<b>Joint control by persons related to the Group</b>	<b>As at 31.12.2016</b>	<b>As at 31.12.2015</b>
<b>Assets</b>		
Loans and advances to customers	0	193
<b>Total liabilities</b>	<b>0</b>	<b>193</b>
<b>Liabilities</b>		
Amounts due to customers	56 176	90 326
Other liabilities	0	60
<b>Total liabilities</b>	<b>56 176</b>	<b>90 386</b>
<b>Joint control by persons related to the Group</b>	<b>As at 31.12.2016</b>	<b>As at 31.12.2015</b>
<b>Off-balance sheet liabilities granted to customers</b>	<b>20</b>	<b>9 191</b>
Relating to financing	20	7 507
Guarantees	0	1 684
<b>Derivative instruments (nominal value)</b>	<b>150</b>	<b>0</b>
Other instruments	150	0
<b>Subsidiaries</b>	<b>1.01.2016- 31.12.2016</b>	<b>1.01.2015- 31.12.2015</b>
Interest income	5 443	533
Interest expense	-65	-232
Fee and commission income	3 710	5
Other operating income	407	1 589
General administrative expenses	-3 041	-3 011
<b>Total</b>	<b>6 454</b>	<b>-1 116</b>
<b>Parent company</b>	<b>1.01.2016- 31.12.2016</b>	<b>1.01.2015- 31.12.2015</b>
Fee and commission income	2	0
General administrative expenses	-3	0
<b>Total</b>	<b>-1</b>	<b>0</b>
<b>Subsidiaries of the parent company</b>	<b>1.01.2016- 31.12.2016</b>	<b>1.01.2015- 31.12.2015</b>
Interest expense	-2 686	0
Fee and commission income	30	0
General administrative expenses	-1	0
<b>Total</b>	<b>-2 657</b>	<b>0</b>
<b>Joint control by persons related to the Group</b>	<b>1.01.2016- 31.12.2016</b>	<b>1.01.2015- 31.12.2015</b>
Interest income	0	54
Interest expense	-1 425	-1 272
Fee and commission income	10	257
Other operating income	0	1 599
General administrative expenses	0	-41 282
<b>Total</b>	<b>-1 415</b>	<b>-40 644</b>

### Nature of transactions with related entities

All transactions with related entities are conducted in accordance with the regulations relating to banking products, on an arm's length basis.

Interest rates on loans granted to related parties were within the range of 4.15% - 14%, while interest rates on deposits were within the range of 0% - 2.1%.

### Transactions with the State Treasury and related entities

Polish Financial Supervision Authority in communication of 6 December 2016 point 5, unanimously recognized the Polish State Treasury of the Republic of the parent entity of Alior Bank S.A. within the meaning of art. 4 paragraph. 1 point 8 letter b and point 14 of the Banking Act, stating that it has the ability to exercise significant influence over Alior Bank S.A. by means of Powszechnego Zakładu Ubezpieczeń S.A.

The following tables present significant transactions with the Treasury and its related entities in accordance with the exception contained in IAS 24.25.

State Treasury and related entities		As at 31.12.2016
<b>Assets</b>		
Available-for-sale financial assets		6 586 920
Investment securities held to maturity		219 855
Amounts due from banks		1 605
Loans and advances to customers		47 203
<b>Total liabilities</b>		<b>6 855 583</b>
<b>Liabilities</b>		
Amounts due to customers		478 789
<b>Total liabilities</b>		<b>478 789</b>

State Treasury and related entities		1.01.2016- 31.12.2016
Interest income		110 958
Interest expense		-5 884
The costs of paid tax		-361 904
<b>Total</b>		<b>256 830</b>

All transactions with the State Treasury and its related entities are conducted at arm's length.

### 35. Offsetting of financial assets and liabilities

The following note presents assets and liabilities which comprise items subject to offsetting in accordance with the principles described in Note 2.3.8.

As at 31.12.2016	Gross book value of financial instruments which are not subject to offsetting	Gross book value of financial instruments which are subject to offsetting	Net values presented in the financial statements	Cash collateral received	Amounts relating to recognized financial instruments which do not meet some or all offsetting criteria (under ISDA agreements signed)	Net exposure
a)	b)	c)=a)-b)	d)	e)	f)=c)+d)+e)	

Assets	521 018	0	521 018	-164 332	-243 046	113 640
Positive value of derivatives (inc. Hedging instruments)	491 235	0	491 235	-164 332	-213 234	113 669
Treasury bonds blocked for REPO transactions	29 783	0	29 783	0	-29 812	-29
Liabilities	334 245	0	334 245	-145 141	-243 046	-53 942
Negative value of derivatives (inc. Hedging instruments)	304 433	0	304 433	-145 141	-213 234	-53 942
Repo transactions	29 812	0	29 812	0	-29 812	0

As at 31.12.2015	Gross book value of financial instruments which are not subject to offsetting	Gross book value of financial instruments which are subject to offsetting	Net values presented in the financial statements	Cash collateral received	Amounts relating to recognized financial instruments which do not meet some or all offsetting criteria (under ISDA agreements signed)	Net exposure
	a)	b)	c)=a)-b)	d)	e)	f)=c)+d)+e)
Assets	1 106 681	0	1 106 681	-203 262	-747 049	156 370
Positive value of derivatives (inc. Hedging instruments)	530 147	0	530 147	-203 262	-171 488	155 397
Treasury bonds blocked for REPO transactions	576 534	0	576 534	0	-575 561	973
Liabilities	885 741	0	885 741	-171 406	-747 049	-32 714
Negative value of derivatives (inc. Hedging instruments)	310 180	0	310 180	-171 406	-171 488	-32 714
Repo transactions	575 561	0	575 561	0	-575 561	0

## 36. Transactions, remuneration and shares held by members of the management and supervisory bodies

All transactions with members of the management and supervisory bodies were concluded in accordance with the rules and regulations relating to bank products on an arm's length basis.

As at 31.12.2016	Supervisory and Management Board members	Supervisory Board	Management Board
------------------	--	-------------------	------------------

<b>Assets</b>			
Loans and advances to customers	7 341	3	7 338
<b>Total assets</b>	<b>7 341</b>	<b>3</b>	<b>7 338</b>
<b>Liabilities</b>			
Amounts due to customers	7 564	842	6 722
Provisions	5	5	0
<b>Total liabilities</b>	<b>7 569</b>	<b>847</b>	<b>6 722</b>

<b>As at 31.12.2016</b>	<b>Supervisory and Management Board members</b>	<b>Supervisory Board</b>	<b>Management Board</b>
<b>Off-balance sheet liabilities granted to customers</b>	<b>47</b>	<b>47</b>	<b>0</b>
Relating to financing	47	47	0

<b>As at 31.12.2015</b>	<b>Supervisory and Management Board members</b>	<b>Supervisory Board</b>	<b>Management Board</b>
<b>Assets</b>			
Loans and advances to customers	13 230	5 688	7 542
<b>Total assets</b>	<b>13 230</b>	<b>5 688</b>	<b>7 542</b>
<b>Liabilities</b>			
Amounts due to customers	36 517	19 762	16 755
Provisions	2	1	1
<b>Total liabilities</b>	<b>36 519</b>	<b>19 763</b>	<b>16 756</b>

<b>As at 31.12.2015</b>	<b>Supervisory and Management Board members</b>	<b>Supervisory Board</b>	<b>Management Board</b>
<b>Off-balance sheet liabilities granted to customers</b>	<b>1 539</b>	<b>944</b>	<b>595</b>
Relating to financing	1 539	944	595

**36.2 Information on the total amount of remuneration paid or payable, broken down by Management and Supervisory Board members** 1.01.2016- 31.12.2016 1.01.2015- 31.12.2015

<b>Management Board</b>		
short-term employee benefits	13 879	8 306
long-term employee benefits	6 701	1 432
<b>Total Management Board</b>	<b>20 580</b>	<b>9 738</b>
<b>Supervisory Board</b>		
short-term employee benefits	1 025	863
<b>Total Supervisory Board</b>	<b>1 025</b>	<b>863</b>

<b>36.3 Number of shares held by the Supervisory Board</b>	<b>As at 31.12.2016</b>	<b>As at 31.12.2015</b>
Helene Zaleski	n/a	210 774
Niels Lundorff	n/a	80 021
Małgorzata Iwanicz- Drozdowska	0	1 465
<b>Total</b>	<b>0</b>	<b>292 260</b>

36.4 Number of shares held by the Management Board	As at 31.12.2016	As at 31.12.2015
Wojciech Sobieraj	435 296	435 296
Krzysztof Czuba	298	168
Witold Skrok	178 421	104 103
Katarzyna Sułkowska	28 612	47 612
<b>Total</b>	<b>642 627</b>	<b>587 179</b>

Contracts with the Management Board Members are concluded for an indefinite period. The contracts may be terminated by any of the parties with 9-months' notice, with effect as at the end of the relevant calendar month.

In the event of the Bank terminating an employment contract with a Management Board Member before expiry of his/her term of office, the Board Member shall be entitled to receive compensation in an amount constituting not less than six-times and not more than twelve-times the gross basic monthly salary.

The contracts contain non-competition provisions based on which the Management Board Members after termination of the employment relationship with the Bank may not conduct any competitive activities for 12 months from the date of contract termination. Therefore, the Management Board Members are entitled to receive remuneration which in aggregate is the equivalent of their gross remuneration for 12 months.

## 37. Incentive program for senior executives

### Management option scheme

On 13 December 2012, on the basis of a power of attorney granted in the Resolution of the Supervisory Board of Alior Bank S.A. of 10 December 2012, preliminary allocation of A, B and C series Subscription Warrants was performed. The said Subscription Warrants entitle their holders to acquire the Bank's shares, in accordance with a Resolution of the General Shareholders' Meeting of Alior Bank S.A. no. 28/2012 of 19 October 2012 on the conditional increase in the Bank's share capital and issue of subscription warrants.

The principles of execution of the incentive scheme are defined in the Incentive Scheme Rules and Regulations, which were adopted by resolution of the Supervisory Board of Alior Bank S.A. of 27 March 2013. The incentive scheme covered the Management Board Members and a group of key managers of the Bank who were not Management Board members.

The Management Option Scheme anticipated that three tranches of subscription warrants (A, B and C-series) and the corresponding three tranches of new shares of the Bank (D, E and F-series) with a total nominal value of up to PLN 33,312,500 would be issued, including:

- up to 1 110 417 A-series subscription warrants, which shall entitle their holders to acquire up to 1 110 417 D-series shares of Alior Bank in a period of five years starting from the first anniversary of the first quotation of the Shares on the WSE;
- up to 1 110 416 B-series subscription warrants which will entitle their holders to take up 1 110 416 E-series shares of Alior Bank over a period of 5 years starting from the day of the second anniversary of the first quotation of the Shares on the WSE;
- up to 1 110 417 C-series subscription warrants which will entitle their holders to take up 1 110 417 F-series shares of Alior Bank over a period of 5 years starting from the day of the third anniversary of the first quotation of the Shares on the WSE.

The Management Option Scheme was binding in the years 2013–2015. In accordance with the Variable Salary Component Policy of Alior Bank Management Members, the Programme will be settled until the year 2020.

The amount of the plan was determined based on the fair value model. The fair value of warrants for shares was determined based on a valuation model Black-Scholes option. It was assumed that share prices change over time in accordance with the process of geometric Brownian motion, assuming a long-term volatility of the Bank and the risk free rate. The volatility was based on historical data. The model takes into account the right to exercise the warrants of series A, B and C for a period of five years respectively from 1, 2 and 3 years from the original issue date.

The program is based on a share of equity-settled.

Details concerning the warrants finally awarded to the Management Board Members are presented in the table below:

Name	Number of A-series warrants allocated	Number of B-series warrants allocated	Number of C-series warrants allocated
Sobieraj Wojciech	222 086	222 086	222 086
Bartler Małgorzata	-	27 656	13 784
Czuba Krzysztof	88 833	88 833	88 833
Krzyżanowska Joanna	-	-	30 440
Skrok Witold	71 066	88 833	88 833
Smalska Barbara	-	-	30 440
Sułkowska Katarzyna	88 833	88 833	88 833
<b>Razem</b>	<b>470 818</b>	<b>516 241</b>	<b>563 249</b>

In connection with the rights issue, on 27 July 2016 the Supervisory Board passed a technical adjustment to the Management Option Scheme aimed at ensuring the economic neutrality of the scheme for the eligible persons. The adjustment involves calculating the decrease in the notional value of the Management Option Scheme and issuing an appropriate number of phantom shares with parameters similar to warrants to the eligible persons.

	Number of subscription warrants	The average share price for the completed subscription warrants	Number of phantom shares	The average share price for the completed phantom shares
Outstanding at beginning of period (1.01.2016)	2 568 564	-	0	-
Granted during the period	0	-	1 389 840	-
Forfeited during the period	0	-	0	-
Completed during the period	0	n/a	0	n/a
Outstanding at end of period (31.12.2016)	2 568 564	-	1 389 840	-
Exercisable at end of period (31.12.2016)	0	-	0	-

	Subscription warrants	Phantom shares
The average fair value of the instruments granted during the period (PLN)	9.87	8.71
The exercise price of the instrument (for instruments outstanding at the end of the period) (PLN)	61.84-66.06	50.43-53.87
The average maturity date of the instrument occurring at the end of the period	02.2020	02.2020

## Bonus Scheme for the Management Board

In connection with the 3-year period of the Original Incentive Scheme based on the Bank's shares coming to an end, the Supervisory Board enacted a Bonus Scheme for the Management Board valid from 2016.

The objective of the Scheme is to create additional incentive stimuli for its participants to effectively perform the duties entrusted to them, in particular, managing the Bank and making efforts aimed at the continued stable development of the Bank and its capital group, while maintaining appropriate and effective risk management at the Bank, stability of the Bank's management personnel and realization of long-term interests of the shareholders by bringing about a stable growth of the stock exchange valuation of the Bank's shares, while maintaining an increase in the net assets of the Bank and its companies.

The Bonus depends on achieving or exceeding the relevant Result Thresholds of the Bank and performance of Individual Objectives.

In accordance with Regulation and assumptions of the Programme, thresholds the result of the Bank for 2016 are calculated as the net profit of the Group Alior Bank after adjustment for profit generated by the acquired part of Bank BPH in the period from 04.11.2016 r. to 31.12.2016, and after adjusting for the value of a bank tax and gain on bargain purchase.

This information is presented in the following table:

	The condensed consolidated income statement of Alior Bank Group as at 31.12.2016	The result of acquired part of BPH in the period from 04.11.2016 to 31.12.2016	Adjustments	The condensed consolidated income statement of Alior Bank Group (the basis of settlement of the bonus scheme)
Interest income	2 938 474	97 175	0	2 841 299
Interest expense	-992 425	-12 573	0	-979 852
<b>Net interest income</b>	<b>1 946 049</b>	<b>84 602</b>	<b>0</b>	<b>1 861 447</b>
<b>Dividend income</b>	<b>68</b>	<b>0</b>	<b>0</b>	<b>68</b>
Fee and commission income	590 701	45 319	0	545 382
Fee and commission expense	-259 567	-27 093	0	-232 474
<b>Net fee and commission income</b>	<b>331 134</b>	<b>18 226</b>	<b>0</b>	<b>312 908</b>
<b>Trading result</b>	<b>320 509</b>	<b>4 173</b>	<b>0</b>	<b>316 336</b>
<b>Net result realized on other financial instruments</b>	<b>21 919</b>	<b>9</b>	<b>0</b>	<b>21 910</b>
Other operating income	113 084	26 414	0	86 670
Other operating expenses	-52 065	-1 362	0	-50 703
<b>Net other operating income and expenses</b>	<b>61 019</b>	<b>25 052</b>	<b>0</b>	<b>35 967</b>
<b>Profit from acquisition the demerged business of Bank BPH</b>	<b>508 056</b>	<b>0</b>	<b>-508 056</b>	<b>0</b>
<b>General administrative expenses</b>	<b>-1 566 560</b>	<b>-416 151</b>	<b>0</b>	<b>-1 150 409</b>
<b>Impairment losses &amp; provisions</b>	<b>-799 887</b>	<b>-12 159</b>	<b>0</b>	<b>-787 728</b>
<b>Bank tax</b>	<b>-130 893</b>	<b>-6 087</b>	<b>124 806</b>	<b>0</b>
<b>Gross profit</b>	<b>691 414</b>	<b>-302 334</b>	<b>-508 056</b>	<b>610 498</b>
Income tax	-73 337	52 594		-125 931
<b>Net profit</b>	<b>618 077</b>	<b>-249 740</b>	<b>-508 056</b>	<b>484 567</b>

In accordance with the Resolution of the PFSA, the assessment takes into account the work results of the Eligible Person over the last three calendar years. The decision to grant the Bonus will be made taking into account the provisions of the Policy, financial and non-financial criteria and an assessment of the results of the entire Bank, as well as an assessment of the Bank's results in the areas of responsibility of the Eligible Person. In accordance with the Resolution of the PFSA, when making a decision on the payment and amount of the Bonus, the Supervisory Board will also take into account the results of the entire Bank for the past

three calendar years. The Bonus can be paid if such decision is supported by the financial standing of the entire Bank.

The Bonus will constitute a specific percentage of the gross annual fixed salary of the Eligible Person.

After deciding upon the amount of the Bonus, it will be paid out on the terms set out below.

- 50% of the Bonus will be paid out in cash in four tranches: 40% will be paid out without deferral, 60% will be deferred and paid out in subsequent years in 20% tranches;
- 50% of the Bonus will be paid in the form of a financial instrument motivating towards special care about the Bank's long-term interests – "phantom" shares. The phantom shares will be cashed and paid out in 4 tranches: 40% will be deferred for 5 months and 60% will be deferred and cashed in three 20% tranches.

The whole or a part of the Bonus may also be paid out in the form of subscription warrants in line with the provisions of the Resolution of the Company's General Meeting.

In connection with the planned changes in the legal and organizational structure of the Bank consisting of an acquisition of the spun off business of Bank BPH Spółka Akcyjna with its registered office in Gdańsk comprising the core business of Bank BPH excluding operations related to mortgage loans pursuant to art. 529 § 1.4 of the Commercial Companies Code on terms specified in the Share Purchase Agreement, the Supervisory Board agreed on 29 June 2016 on the principles for the transaction bonus for the Bank's Management Board Members in order to specially motivate the Bank's Board Members to actively cooperate in the process of preparing and conducting the Transaction, to ensure the timely execution of the Transaction in line with the strategic objectives. The bonus can be granted and paid once the conditions related to the execution of the Transaction and the Operational Merger between the banks have been fulfilled. The Bonus will be paid out in accordance with the provisions of the Variable Salary Component Policy.

### **Annual variable remuneration paid in financial instruments (phantom shares) for senior executives**

The variable remuneration policy applicable to managers at the Bank regulates the principles applied by Alior Bank S.A. with respect to variable components of the remuneration of Alior Bank S.A. managers. The Policy is based on the provisions of Resolution no. 258/2011 of the Polish Financial Supervision Authority of 4 October 2011 on the detailed rules of the risk management system and internal control system and detailed terms and conditions for estimating the internal capital of banks and reviewing the process of estimating and maintaining internal capital and the principles for determining the policy regarding variable remuneration components of the Bank's managers. The policy promotes appropriate and effective risk management and discourages taking excessive risk (exceeding the acceptable risk level approved by the Supervisory Board or Management Board) in order to maintain a sound capital base and pursue the long-term interests of the Bank, its shareholders and customers; it also supports the execution of the Bank's strategy of sustainable development and conservative risk management policy, mitigates conflicts of interest, allows maintaining a transparent relationship between individual performance and individual remuneration – through focusing on the goals relating to responsibility and real influence.

The Variable Remuneration Components Policy for Alior Bank S.A. Managers was approved by Resolution no. 97/2011, which was subsequently amended by Resolutions nos. 33/2013, 55/2015 and 29/2016 of the Bank's Supervisory Board.

The Bank identifies managerial positions to which the Variable Remuneration Components Policy applies. The Policy applies to persons holding the following managerial positions at the Bank:

- Management Board members;
- persons holding other positions indicated by the Management Board in consultation with the Appointments and Remuneration Committee.

The total amount of variable remuneration is determined based on the evaluation of the performance of a person holding a managerial position at the Bank and the Bank's performance in the area for which that person is responsible measured against the performance of the whole Bank. Both financial and non-financial criteria are taken into account in evaluating the individual performance. The following financial and non-financial criteria are taken into consideration: the Bank's net result, return on equity, the Bank's capital adequacy ratios, the Bank's liquidity ratios, the Bank's profitability ratios, compliance with the law and internal regulations, long-term nature of employment and other criteria resulting from the individual performance goals of the individual Employees.

Performance is evaluated once a year with respect to a period of three preceding years, so that the amount of variable remuneration takes into account the entire operating cycle of the Bank and the risk associated with its business activity.

Variable remuneration components that are not covered by the Policy are exceptional, occur only in connection with the recruitment of new employees and are limited to the first year of their employment.

As at the date of granting it, fixed remuneration represents a big enough part of the total remuneration to make it possible to conduct a flexible policy of variable remuneration components, including reducing such components or not granting them at all.

The total variable remuneration granted to persons holding managerial positions at the Bank does not restrict the Bank's ability to increase its capital base.

If the right to compensation in the event of termination is provided in an individual contract, such compensation shall reflect the amount of work, efficiency and quality of work performed in the last three years of holding a managerial position at the Bank.

Fifty percent of variable remuneration is meant to encourage the employee to take particular care of the Bank's long-term interest. Variable remuneration is granted or paid when the financial situation of the whole Bank, its performance, performance of the organizational unit which employed the person concerned and the performance of that person justify it. Variable remuneration should be assessed and paid in a transparent manner, in line with the variable remuneration components policy.

In the event that the Bank takes advantage of an extraordinary public intervention, in particular based on the Act of 12 February 2009 on support granted by the State Treasury to financial institutions (Journal of Laws No. 39, item 308 as amended) and the Act of 12 February 2010 on recapitalization of certain financial institutions (Journal of Laws No. 40, item 226 and Journal of Laws of 2011, No. 38, item 196):

- if maintaining a sound capital base and timely withdrawal of public support are at risk, variable remuneration will not be paid unless the Bank generates net profit;

- the Bank appropriately adjusts the amount and components of the remuneration to support proper risk management and long-term performance growth; this shall include a reduction in the remuneration of the Bank's Management Board;
- variable remuneration is payable to the Management Board only in justified cases;
- variable remuneration components will be granted based on an analysis of how the targets set in the individual programmes are met and evaluation of the Bank's profitability and liquidity, provided that there were no violations of any laws or internal regulations of the Bank

The Bank's results used to determine variable remuneration components should take into account the cost of risk, cost of capital and liquidity risk of the Bank in the long-term perspective.

Managers of the internal audit function, compliance risk management function and functions responsible for risk management and personnel issues receive variable remuneration for achieving targets assigned to their functions; their remuneration is not dependent on the business results achieved by the areas of the Bank's operations controlled by them.

The Bank does not grant to managers retirement benefits not determined in advance, which for the purposes of the Policy are understood as retirement benefits granted by the Bank at its sole discretion to individual employees as part of a variable remuneration package.

Persons holding managerial positions at the Bank must not use their own hedging strategies or insurance relating to remuneration and responsibility, excluding mandatory insurance required under specific regulations aimed at neutralizing the measures taken against such persons as part of the execution of the Policy. Such persons submit written declarations to this effect, which are recorded and kept by the Director of the Remuneration and Benefits Department.

Variable remuneration components are granted to persons holding managerial positions at the Bank in accordance with the following principles:

- At least 50% of the variable remuneration granted constitutes an incentive to take particular care of the Bank's long-term interest and, therefore, consists of financial instruments linked to the Bank's shares, including in particular phantom shares or subscription warrants. The remaining part of the variable remuneration granted to Eligible Persons is payable in cash.
- At least 40% of the variable remuneration of an Eligible Person other than a Management Board member and at least 60% of the variable remuneration of an Eligible Person who is a Management Board member constitutes Deferred Remuneration and is deferred for a period of at least 3 years, i.e. it is vested and payable in at least three equal annual instalments rather than immediately after the end of the Evaluation Period. Each time, a resolution on granting the right to receive a particular tranche of the Deferred Remuneration to the Eligible Person, provided that the requirements defined in the Policy and the PFSA Resolution have been satisfied, is passed by the Supervisory Board with respect to the Management Board members and by the Management Board with respect to Eligible Persons other than Management Board members.

- In accordance with the proportionality principle, the minimum amount of variable remuneration that cannot be deferred or paid in the form of financial instruments is set at a level of PLN 100,000 (gross).

The settlement of the phantom shares shall be in cash.

	Number of phantom shares	The average share price for the completed phantom shares
Outstanding at beginning of period (1.01.2016)	1 767	-
Granted during the period	40 968	-
Forfeited during the period	-	-
Realized during the period	19 288	63,95
Outstanding at end of period (31.12.2016)	23 446	-
Exercisable at end of period (31.12.2016)	-	-

The average maturity date of the instrument occurring at the end of this June 2019.

## 38. Legal claims

The value of proceedings relating to liabilities or receivables of the Bank in progress in 2016 did not exceed 10% of Alior Bank's equity. In the Bank's opinion, the Bank's financial liquidity is not at risk due to any single court, arbitration court or public administration body proceeding in progress in 2016, or all the proceedings jointly.

At the 31 December 2016 the total value of debt collection proceedings brought by the Bank, which were in progress in 2016, amounted to PLN 113 060.3 thousand (with respect to corporate customers) and PLN 536 003.9 thousand (with respect to retail customers).

At the 31 December 2015 the total value of debt collection proceedings brought by the Bank, which were in progress in 2016, amounted to PLN 85 539.3 thousand (with respect to corporate customers) and PLN 391 209.7 thousand (with respect to retail customers).

In case in which the Bank was sued value of the claim as of 31.12.2016 amounted to PLN 167 566, 5 thousand and as at 31.12.2015 PLN 40 883.5 thousand.

The value of provisions for disputed claims amounted to PLN 8 700 thousand as at the end of 2016 and PLN 3 219 thousand as at the end of 2015.

## 39. Significant events after the balance sheet date

On 16 February 2017 Fitch Ratings Ltd. has maintained issuer rating assigned to Alior Bank SA on 5 September 2013 unchanged at BB with a stable outlook.

In its report, Fitch indicated that the evaluation of the profitability of Alior Bank at the level of "BB" reflects the rapid credit expansion and a higher appetite for credit risk than the competitions.

Clear and long-term weakening of the Polish economy (not the base scenario of Fitch) significantly affecting the quality of bank's assets, capitalization and profitability, could lead to underestimation of its profitability.

Fitch does not expect any rating changes in the near future, while indicating that the following factors would be positive for the credit profile of the bank and in combination could lead to update its assessment of profitability: stronger capitalization, moderate growth rates, stable asset quality and longer recording the constant profitability in an environment of low interest rates and banking tax.

## 40. Establishment of the Bond Issue Schemes

On 28 December 2015, the Supervisory Board of the Bank approved the opening of the Public Subordinated Bonds Issue Scheme by the Management Board of Alior Bank S.A. ("the Issue Scheme") and authorized the Bank's Management Board to incur financial liabilities through issuing, in series, up to 800 000 unsecured, subordinated bearer bonds of PLN 1 000 par value each as part of the Issue Scheme.

- The total par value of Bonds issued under the Issue Scheme will not exceed PLN 800 000 000.
- The Bonds will be issued and offered in series over a period not exceeding 12 months from the date of approval of the basic prospectus prepared in connection with the Issue Scheme by the Polish Financial Supervision Authority.
- The bonds issued under the Issue Scheme will have maturities of 5 to 10 years from the date of issue of a given bond series.
- Benefits arising from the bonds will be available only in cash.
- The Bonds will be issued in accordance with Art. 33 (1) of the Act on Bonds.
- The Bonds will not take the form of documents and will be registered in the depository of securities maintained in compliance with the provisions of the Act on Trading based on an agreement with the Central Securities Depository of Poland, (hereinafter: KDPW) or with a company mentioned in Art. 5 (10) of the Act on Trading if the tasks mentioned in Art. 48 (1) of the Act on Trading are outsourced by KDPW to such a company.
- The terms and conditions of issue of each Bond series will contain provisions regarding their classification as equity components in accordance with the provisions 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 (O. J. EU L 176 of 27.6.2013, p. 1).
- The Bank's Management Board will seek the admission and introduction of the Bonds to trading on the regulated market maintained by the Warsaw Stock Exchange, (hereinafter: "WSE") in the Catalyst system or introduction of the Bonds to trading in an alternative trading system maintained by WSE or BondSpot S.A. in the Catalyst system.

At the same time, the Supervisory Board authorized the Bank's Management Board to determine the final terms and conditions for issuing particular Bond series issued under the Issue Scheme, allotting the Bonds to investors and taking all other necessary actions aimed at carrying out the Issue Scheme.

On 12 April 2016, the Polish Financial Supervision Authority approved the Bank's prospectus prepared in connection with: (i) public offerings on the territory of the Republic of Poland of up to 800 000 unsecured, subordinated bearer bonds with PLN 1 000 par value each, issued under the Public Issue Scheme of Alior Bank S.A. Subordinated Bonds; and (ii) the intention to seek the admission and introduction of up to 800 000 Bonds to trading on the regulated market maintained by Giełda Papierów Wartościowych w Warszawie S.A. in the Catalyst system.

On 16 September 2016, the Bank's Management Board passed a resolution on discontinuing, as of 16 September 2016, further public offerings of bonds under the above-mentioned basic prospectus and seeking the admission of further bonds issued under the Public Issue Scheme to trading on a regulated market. As at the date of passing that resolution, such a decision was made due to the fact that the Bank had no intention of issuing any more subordinated bonds as part of public offerings on the basis of the said

prospectus. To avoid any doubts, the Bank's Management Board confirmed in its announcement that its decision did not render the Public Issue Scheme invalid; it was aimed at terminating the validity of the prospectus, which pursuant to Art. 49. 1b (a) of the Act on Public Offering, took place on the date of the publication of the said announcement, i.e. on 16 September 2016.

By 31 December 2016, the Bank carried out the issues of two series of subordinated bonds under the Public Issue Scheme:

Series name	Short name	ISIN	Value series (PLN)	Issue date	Maturity date	Market quotations
P1A	ALR0522	PLALIOR00151	150 000 000	2016-04-27	2022-05-16	RR GPW
P1B	ALR0524	PLALIOR00169	70 000 000	2016-04-29	2024-05-16	RR GPW

## 41. Rating

On 16 February 2017 Fitch Ratings Ltd. has maintained issuer rating assigned to Alior Bank SA on 5 September 2013 unchanged at BB with a stable outlook.

In its report, Fitch indicated that the evaluation of the profitability of Alior Bank at the level of "BB" reflects the rapid credit expansion and a higher appetite for credit risk than the competitions.

### **The Bank's full rating granted by Fitch is as follows:**

1. Long-term Foreign Currency IDR: BB, stable outlook
2. Short-Term Foreign Currency IDR: B
3. National Long-Term Rating: BBB+(pol), stable outlook
4. National Short-Term Rating: F2(pol)
5. Viability Rating (VR): bb
6. Support Rating: 5
7. Support Rating Floor: 'No Floor'

Definitions of the Fitch ratings are available on the Agency's website: [www.fitchratings.com](http://www.fitchratings.com), where ratings, criteria and methodologies are also published.

## Explanatory notes on risk

Risk management is one of the key internal processes in Alior Bank S.A. The ultimate goal of the risk management policy is to ensure early recognition and appropriate management of all material risks in the Bank's operations. The Bank isolated the following types of risks resulting from the operations conducted:

- market risk, also covering the banking book interest risk, liquidity risk, foreign exchange risk and risk of commodity prices;
- credit risk;
- operational risk.

## 42. Market risk

Market risk is defined as the likelihood of the Bank incurring potential losses in the event of unfavourable changes in market prices (share prices, currency exchange rates, profitability curves), market factors (volatility in financial instrument valuations, the correlation of price changes between particular instruments), and customer behaviour (early deposit withdrawals, early loan repayments).

The process of managing market and liquidity risks is based on achieving, *inter alia*, the following goals: significantly mitigating the volatility of results and changes in the economic value of the Bank's equity;

- developing a structure of assets and liabilities (banking book) which is optimal in terms of profitability and the potential impact on the economic value;
- providing customers with core treasury products in order to help them manage the risk underlying their operations (i.e. hedging);
- guaranteeing the solvency and full availability of liquid funds at any moment and even under the assumption of the occurrence of negative market scenarios;
- ensuring that the processes applied by the Bank comply with the regulatory requirements regarding market risk management and the level of equity maintained for that purpose.

The market and liquidity risk management process is carried out within the framework of the Bank's relevant risk management policies covering identification, measurement, monitoring and reporting of risks. It also pertains to control over treasury transactions by determining and verifying the principles on which they are concluded, organized and assessed.

There is a clear segregation of duties, competencies and responsibilities within the individual functions, and the principles are specified in internal regulations. The key role in this respect is played by the Financial Risk Management Department (FRMD) which prepares independent cyclic reports using the risk models and measures adopted by the Bank and submits them to appropriate units, including – periodically – to members of the Management Board, Supervisory Board and ALCO. The duties of the Department include, among other things:

- defining market and liquidity risks management policies;
- analysing and reporting the Bank's risk profile;
- determining the amount of economic capital to cover the market and liquidity risks;
- recommending current activities related to managing the banking book risk;
- creating all regulations which define the process of concluding treasury transactions on the interbank market and with the Bank's customers, including developing documentation templates;
- coordinating the process of introducing new Treasury products and assessing the related risk;
- supporting and servicing ALCO operations.

The Treasury Department is responsible for carrying out treasury transactions with the Bank's customers, and the Interbank Transaction Team is exclusively responsible for concluding transactions on the interbank market and for maintaining open trading book risk positions, and concluding treasury transactions on the Bank's account. The transactions may be concluded to manage trading book risk positions within the limits set up, and pursuing the Bank's policy in respect of managing the banking book risk within the limits set up.

The Operations Department is responsible for the independence of ad hoc controls of internal treasury operations, including transaction settlements. The Operations Department operates as an entity fully independent of the Treasury Department. The leak-proof and accurate supervision conducted by the Operations Department is the basis for mitigating the operating risk of the Bank's treasury operations.

Supervision over the above-mentioned entities of the Bank was separated up to the level of Management Board Member which is an additional factor guaranteeing their independent operations. The full organizational structure and segregation of competencies have been defined in detail by the Bank's Management Board in the Head Office Organizational Regulations. The Management Board, the Supervisory Board and the ALCO take an active role in managing market risks.

The Assets and Liabilities Committee (ALCO) controls market risk, including liquidity risk, on a current basis. It takes all the respective decisions, unless these were previously qualified as being within the sole competence of the Management Board or the Supervisory Board.

ALCO's duties include, among other things:

current control over market risk management, both related to the trading and the banking book, including issuing decisions relating to the risk management of both books;

- current control over market risk management, both related to the trading and the banking book, including issuing decisions relating to the risk management of both books;
- accepting the Bank's operational limits on the monetary and capital markets;
- current control over the Bank's liquidity management, both related to the trading and the banking book;
- commissioning actions to acquire sources of financing for the Bank's operations and supervising the financing plan;
- issuing decisions on managing the model portfolios.

The Bank's basic market and liquidity risks management strategy assumptions as stipulated for a given budget year take the form of an Asset and Liability Management Policy developed annually by the FRMD and submitted by the Management Board to the Supervisory Board for acceptance as part of acceptance of the annual budget. It remains binding until a consecutive update.

The Supervisory Board exercises supervision over risk management, including, but not limited to:

- annual determination of the Bank's strategy in respect of market risk management by accepting the Asset and Liability Management Policy;
- acceptance of the Bank's market risk management strategy, including the key risk limits;
- control over compliance of the Bank's policy in respect of risk acceptance with the Bank's strategy and financial plan through a regular review of the Bank's market risk profile based on the reports received;
- recommendation of actions aimed at changing the Bank's risk profile.

Information on the nature and level of risk is submitted to the Supervisory Board by the Management Board, with the exception of the results of internal control of the market risk management system which is submitted by the Director of the Internal Audit Department.

The Bank's Management Board is responsible, among other things, for:

- supervising the market and liquidity risk management process, monitoring and reporting risks;
- determining the appropriate organization and segregation of duties in the process of concluding treasury transactions;
- accepting policies and instructions regulating market and liquidity risk management within the Bank and efficient operation of the identification systems;
- setting detailed limits for mitigating the Bank's risk and ensuring appropriate mechanisms for their monitoring and notifying cases of exceeding limits.

The Bank's market and liquidity risk exposure is officially mitigated by a system of limits which are updated periodically, introduced by resolutions of the Supervisory Board or the Management Board; the limits cover all measures of market risk whose level is monitored and reported by the Bank's organizational entities independent of the given entity's business. There are three types of limits at the Bank which differ in terms of their scope and the way they operate: basic limits, supplementary limits, and stress-test limits. Market risk management focuses on potential changes in the economic results; unquantifiable risks related to treasury operations are also mitigated through the quality requirements in force at the Bank, related to the risk management process (the internal control system, implementation of new products, analysis of legal risk, analysis of operating risk).

For market risk purposes, the Bank estimates Value-at-Risk using an analytic module of the treasury system. The Bank uses a parametric VaR model in accordance with JP Morgan methodology (RiskMetrics). The estimated 99% one-day VaR may be re-scaled to other periods by multiplying variability by a root of a multiple of the one-day period (e.g. 10-day VaR is determined by multiplying one-day VaR by  $\sqrt{10}$ ).

The following table presents VaR for the Bank (for the banking book and trading book separately) as at the end of 2016 and 2015.

VaR	As at 31.12.2016	As at 31.12.2015
Banking book	11 849	6 361
Trading book	1 909	2 464
<b>Total</b>	<b>12 314</b>	<b>7 492</b>

### 43. Foreign exchange risk

Foreign exchange risk is defined as the risk of potential loss caused by movements in foreign exchange rates. The Bank additionally identifies the impact of foreign exchange movements on its results in the long term, which could occur in the event of converting future foreign currency income and expenses at a potentially less favourable exchange rate. The risk related to future results may be managed under the model currency portfolio.

The basic purpose of foreign exchange risk management is to identify those areas of the Bank's operations which may be exposed to foreign exchange risk, and thus to undertake to mitigate the resulting potential losses to the maximum extent. The Bank's Management Board specifies the foreign exchange risk profile, which must be consistent with the applicable financial plan of the Bank.

Under the foreign exchange risk management process, the Bank is obliged to monitor and report the amounts of all its currency positions and VaR, assessed in accordance with the adopted model, within the set limits. The Bank closes each significant currency position with a counter position on the market, thus eliminating the related foreign exchange risk. Open currency positions are maintained within the limits set by the Supervisory Board. The Bank conducts periodical analyses of potential scenarios which are aimed at providing information on the Bank's exposure to foreign exchange risk in the event of foreign exchange fluctuation shocks.

The Bank may also conduct hedging transactions in respect of future highly probable foreign exchange cash flows (e.g. cost of rent, net interest income denominated in foreign currencies). The purpose of such transactions is to limit the fluctuations of results in the current calendar year to a maximum of 60%.

The key foreign exchange risk management tools at Alior Bank include:

- internal procedures for foreign exchange risk management;
- internal models and measurements of foreign exchange risk;
- foreign exchange risk limits and threshold values;
- limitations on foreign exchange trading transactions;
- stress tests.

The basic tool for the measurement of foreign exchange risk at the Bank is the "Value at Risk" model ("VaR Model"), which enables determining the possible amount of loss stemming from the then current foreign currency positions as a result of fluctuations in foreign exchange rates, measured using an assumed confidence level and time horizons (holding period). The Bank determines VaR using the variance-covariance method and a confidence level of 99%. This amount is determined on a daily basis for particular areas responsible for accepting and managing risk, both on an individual and on an overall basis.

As at the end of December 2016, the maximum loss on the Bank's currency portfolio (managed as part of the trading book) specified in accordance with the VaR Model with a 10-day holding period could amount to PLN 279 628.70, assuming a confidence level of 99%.

	As at 31.12.2016	As at 31.12.2015
Holding period [days]	10	10
VaR [PLN]	279,628.70	106,408.93

#### VaR statistics on the Bank's currency portfolio for 2016 and 2015

VaR (in PLN'000)	As at 31.12.2016	As at 31.12.2015
Min	21.48	18.81
Average	310.62	116.52
Max	4,748.08	1,277.16

The VaR model assumes that the distribution of changes in the values of risk factors is normal, which may in practice lead to underestimating the losses in extreme scenarios ("fat tails"). Therefore, the Bank performs stress tests.

The utilization of the stress-test limit for currency positions calculated as the maximum loss the Bank could incur in the event of the most unfavourable daily foreign exchange rate change of those which occurred within at least the last four years, totalled PLN 38 306.42 as at 31 December 2016, and PLN 135 952 as at the end of 2015.

Stress-test statistics of the currency position in 2016 and 2015 are presented below.

#### Stress-test statistics of the currency position in 2016 (in PLN '000)

Min	Average	Max
7,23	69,41	206,89

#### Stress-test statistics of the currency position in 2015 (in PLN '000)

Min	Average	Max
6,88	95,85	953,41

## 44. Interest rate risk

Interest rate risk is defined as the risk of a negative impact of the levels of market interest rates on the current financial result or the net present value of the Bank's equity. As part of its policy of mitigating the trading book risk, the Bank pays particular attention to specific aspects of interest rate risk that are associated with the banking book, such as:

- repricing risk (i.e. the mismatch of the interest rate tenors of assets and liabilities);
- basis risk, which is defined as the extent to which non-parallel changes in different reference indices that have similar repricing dates can affect the Bank's income;
- modelling accounts with an unspecified maturity date or with an interest rate set by the Bank (e.g. for sight deposits);
- the impact of non-interest bearing items on the risk (e.g. capital, fixed assets).

One of methods of estimating the Bank's exposure to interest rate risk is the determination of BPV. BPV represents the estimated change in the value of a given transaction or position as a result of one basis point change at a given point of the yield curve. BPV values are measured daily for all currencies and at each point of the curve. The BPV estimates as at 31 December 2016 and 31 December 2015 are presented in the tables below:

BPV as at the end of 2016 by tenor

Currency	Up to 6 months	6 months - 1 year	1 year - 3 years	3 - 5 years	5 - 10 years	Total
PLN	-19,2	305,4	604,9	111,3	-433,5	568,9
EUR	-16,4	0,3	-28,8	-43,7	-34,5	-123,1
USD	12,5	11,1	-12,6	-0,2	-0,9	9,9
CHF	-0,6	-0,3	-1,6	-0,2	0	-2,7
GBP	0,1	2,5	0,2	0	0	2,8
Other	-1,6	-5	2,8	-0,1	0	-3,9
<b>Total</b>	<b>-25,2</b>	<b>314</b>	<b>564,9</b>	<b>67,1</b>	<b>-468,9</b>	<b>451,9</b>

BPV as at the end of 2015 by tenor

Currency	Up to 6 months	6 months - 1 year	1 year - 3 years	3 - 5 years	5 - 10 years	Total
PLN	-192,3	17,3	369,8	-140	30,3	85,2
EUR	-19,1	-16,2	-19,7	-13,8	-6,6	-75,4
USD	6,1	11,3	-6,2	-6,8	-0,4	4,0
CHF	0,4	-0,1	-1,4	0	0	-1,1
GBP	0,6	1,7	0,1	0	0	2,5
Other	-0,5	-1,6	0	0	0	-2,1
<b>Total</b>	<b>-204,8</b>	<b>12,4</b>	<b>342,6</b>	<b>-160,6</b>	<b>23,3</b>	<b>13,1</b>

BPV statistics for January – December 2016:

Book	Min	Average	Max
Banking book	-2,458,56	-753,75	-375,22
Trading book	-49,28	-11,39	32,77
ALCO	499,05	969,52	1,814,16
<b>Total</b>	<b>-770,67</b>	<b>204,38</b>	<b>582,90</b>

BPV statistics for January – December 2015

Book	Min	Average	Max
Banking book	-511,97	-213,39	1,60
Trading book	-35,65	-8,42	38,60
ALCO	-235,41	155,36	543,18
<b>Total</b>	<b>-378,96</b>	<b>-66,44</b>	<b>249,33</b>

At the same time, in order to estimate the total level of the interest rate risk, the Bank applies a VaR Model as discussed above. The economic capital to cover the said type of risk measured in this manner as at the end of 2016 and 2015 is shown in the table below (99% VaR assuming a holding period of 10 days).

#### VaR statistics for January – December 2016

Book	Min	Average	Max
Banking book	3 493	10 935	32 883
Trading book	588	1 650	5 485
<b>Total</b>	<b>3 733</b>	<b>11 687</b>	<b>38 120</b>

#### VaR statistics for January – December 2015

Book	Min	Average	Max
Banking book	2 389	7 960	13 498
Trading book	611	1 527	2 622
<b>Total</b>	<b>3 347</b>	<b>8 533</b>	<b>14 973</b>

For the purpose of managing interest rate risk, the Bank specifies trading operations, which cover securities and derivative contracts concluded for trading purposes, and banking operations, which cover other securities, own issues, borrowings, deposits, loans and derivative transactions used to hedge the banking book risk. The Bank also performs analyses of possible scenarios which cover, among other things, the impact of specific changes in interest rates on the future interest results and the economic value of capital. As part of these scenarios the Bank maintains internal limits, the utilization of which is measured daily. Utilization of the limit for changes in the economic value of capital assuming a parallel movement of the interest rate curves of +/- 200 b.p. and non-parallel movements in scenarios of +/- 100/400 b.p. (assuming 1M/10Y tenors, and between them, the shifted linear interpolation) as at the end of December 2016 is shown below (in PLN'000).

Scenario (1M/10Y)	Change in the economic value of capital
+400 / +100	233 976
+100 / +400	30 853
+200 / +200	106 192
- 200 / - 200	-108 574
- 100 / - 400	-44 898
- 400 / - 100	-107 990

## 45. Liquidity risk

The Bank defines liquidity risk as the risk of being unable to fulfil, on conditions favourable for the Bank and at an acceptable cost, its payment obligations resulting from all the Bank's balance sheet and off-balance sheet positions. Therefore, the Bank's liquidity risk management policy consists of maintaining its own liquidity in such a way that it is possible, at any time, to discharge all payment obligations with cash in hand, through the expected contractual inflows from transactions with specified maturity dates or by selling transferable assets and at the same time minimizing liquidity costs.

The Bank has appointed the Assets and Liabilities Committee (ALCO) for the purposes of the management of assets and liabilities. The liquidity risk strategy, including the acceptable risk level, the assumed balance sheet structure and the financing plan, is approved by the Bank's Management Board and subsequently accepted by the Bank's Supervisory Board. Concluding interbank transactions is the responsibility of the Treasury Department, the Operations Department is responsible for the settlement and accounting for transactions, and the Financial Risk Management Department is responsible for liquidity risk monitoring and measurement. The division of competencies in the area of liquidity risk management is clear; the competencies are divided to Management Board member level, which guarantees their full independence. In 2016, treasury operations and liquidity risk management were fully centralized at the Alior Bank S.A. level.

Specifically, as part of its management of liquidity risk, the Bank pursues the following goals:

- ensuring, at all times, that there is capacity to settle all obligations on a timely basis;
- maintaining liquid assets at an appropriate level, i.e. a buffer of unencumbered high quality liquid assets in case of a sudden deterioration in liquidity;
- determining the scale of liquidity risk to be incurred by the Bank, by setting internal liquidity limits and horizon of survival in extreme conditions;
- minimizing the risk of exceeding the liquidity limits defined by the Bank;
- monitoring liquidity, so that the Bank is able to maintain liquidity and activate a relevant emergency plan when necessary;
- ensuring that the processes applied by the Bank comply with the regulatory requirements regarding liquidity risk management.

The goals set out above are pursued independently by appropriate organizational units, the competencies and responsibilities of which are clearly defined in the internal regulations. The Bank applies the following measures in the process of liquidity management:

- develops liquidity procedures and policies, including the financing plan for consecutive years of the Bank's operations;
- manages emergency plans with regard to liquidity;
- manages asset hedges and encumbrances;
- monitors liquidity limits and early warning ratios that identify negative trends which could contribute to an increase in liquidity risk;
- conducts periodical analyses of the categories and factors which impact the current and future liquidity levels in the form of reports;
- performs stress tests for liquidity risk purposes.

Among the liquidity management measurements, the Bank takes into account the following ratios and the related limits for the following types of liquidity:

- financial liquidity – the ability to finance assets and discharge liabilities on a timely basis in the course of the Bank's everyday activities or in other conditions which may be anticipated, without the need to incur losses. In its liquidity management activities, the Bank specifically focuses on a vista and current (up to 7 days) liquidity analysis;
- short-term liquidity defined as the ability to discharge all monetary liabilities which mature within 30 consecutive days;
- medium-term liquidity understood as the ability to settle all liabilities which mature in the period of 1 to 12 months;
- long-term liquidity defined as the ability to settle all monetary liabilities which mature in a period longer than 12 months.

As part of its management of liquidity risk, the Bank also carries out analyses of the maturity profile in a longer term, which to a large extent depends on the assumptions adopted in respect of the development of future cash flows related to asset and liability items. These assumptions specifically take into account:

- stability of liabilities without specified maturities (e.g. current accounts, deposit withdrawals and renewals, level of their concentration);
- option to shorten maturities of specific assets (such as mortgage loans with an early repayment option);
- option to sell assets (liquid portfolio); and they are accepted by ALCO or the Bank's Management Board.

To identify the realigned liquidity gap, the Bank uses model weights of the core deposits/loan repayments, determined based on the implemented statistical model and historical observations of balances for particular products.

Contractual flows of the Bank's liabilities / assets as at 31 December 2016 by maturity (amounts in PLN millions).

2016-12-31	1D	1M	3M	6M	1Y	2Y	5Y	5Y+	Total
<b>ASSETS</b>	<b>11 580</b>	<b>3 860</b>	<b>1 662</b>	<b>2 804</b>	<b>4 739</b>	<b>7 958</b>	<b>18 107</b>	<b>26 061</b>	<b>76 771</b>
Cash and Nostro accounts	1 470	0	0	0	0	0	0	0	1 470
Amounts due from banks	1 501	0	0	0	145	0	0	0	1 646
Loans and advances to customers	8 609	805	1 643	2 154	4 186	6 376	14 378	22 404	60 555
Securities	0	3 055	19	650	408	1 582	3 729	901	10 344
Other assets	0	0	0	0	0	0	0	2 756	2 756
<b>LIABILITIES AND EQUITY</b>	<b>-29 558</b>	<b>-7 401</b>	<b>-4 911</b>	<b>-4 179</b>	<b>-3 527</b>	<b>-3 353</b>	<b>-1 550</b>	<b>-7 014</b>	<b>-61 493</b>
Amounts due to banks	-63	0	-1	-2	-16	-182	-92	-71	-427
Amounts due to customers	-29 495	-5 287	-4 771	-4 026	-3 004	-1 870	-219	-43	-48 715
Own issues	0	-76	-139	-151	-507	-1 301	-1 239	-677	-4 090
Equity	0	0	0	0	0	0	0	-6 223	-6 223
Other liabilities	0	-2 038	0	0	0	0	0	0	-2 038
<b>Balance-sheet gap</b>	<b>-17 978</b>	<b>-3 541</b>	<b>-3 249</b>	<b>-1 375</b>	<b>1 212</b>	<b>4 605</b>	<b>16 557</b>	<b>19 047</b>	<b>15 278</b>
Accumulated Balance-sheet gap	-17 978	-21 519	-24 768	-26 143	-24 931	-20 326	-3 769	15 278	0
Derivative instruments – inflows	0	5 473	1 894	671	1 215	740	423	63	10 479
Derivative instruments – outflows	0	-5 474	-1 875	-669	-1 181	-735	-411	-62	-10 407
<b>Derivative instruments – net</b>	<b>0</b>	<b>-1</b>	<b>19</b>	<b>2</b>	<b>34</b>	<b>5</b>	<b>12</b>	<b>1</b>	<b>72</b>
Guarantee and financial lines	13 873	7	12	19	119	107	13	8	14 157

<b>Off balance-sheet gap</b>	<b>13 873</b>	<b>5</b>	<b>31</b>	<b>20</b>	<b>153</b>	<b>113</b>	<b>25</b>	<b>9</b>	<b>14 229</b>
<b>Total gap</b>	<b>-4 104</b>	<b>-3 537</b>	<b>-3 217</b>	<b>-1 354</b>	<b>1 366</b>	<b>4 717</b>	<b>16 582</b>	<b>19 056</b>	<b>29 509</b>
Total accumulated gap	-4 104	-7 638	-10 855	-12 209	-10 843	-6 126	10 455	29 509	0

Contractual flows of the Bank's liabilities / assets as at 31 December 2015 by maturity (amounts in PLN millions).

2015-12-31	1D	1M	3M	6M	1Y	2Y	5Y	5Y+	Total
<b>ASSETS</b>	<b>7 741</b>	<b>539</b>	<b>1 253</b>	<b>1 811</b>	<b>4 015</b>	<b>5 843</b>	<b>11 730</b>	<b>19 477</b>	<b>52 409</b>
Cash and Nostro accounts	2 089	0	0	0	0	0	0	0	2 089
Amounts due from banks	113	0	0	0	171	0	0	0	284
Loans and advances to customers	5 539	506	1 234	1 512	3 213	4 471	9 491	17 016	42 982
Securities	0	33	19	299	631	1 372	2 239	640	5 233
Other assets	0	0	0	0	0	0	0	1 821	1 821
<b>LIABILITIES AND EQUITY</b>	<b>-14 823</b>	<b>-5 736</b>	<b>-5 442</b>	<b>-4 980</b>	<b>-1 932</b>	<b>-1 602</b>	<b>-1 348</b>	<b>-4 479</b>	<b>-40 342</b>
Amounts due to banks	-815	0	-1	-1	-1	-205	-46	0	-1 069
Amounts due to customers	-14 008	-4 868	-5 429	-4 708	-1 725	-655	-51	-25	-31 469
Own issues	0	0	-12	-271	-206	-742	-1 251	-935	-3 417
Equity	0	0	0	0	0	0	0	-3 519	-3 519
Other liabilities	0	-868	0	0	0	0	0	0	-868
<b>Balance-sheet gap</b>	<b>-7 082</b>	<b>-5 197</b>	<b>-4 189</b>	<b>-3 169</b>	<b>2 083</b>	<b>4 241</b>	<b>10 382</b>	<b>14 998</b>	<b>12 067</b>
Accumulated Balance-sheet gap	-7 082	-12 279	-16 468	-19 637	-17 554	-13 313	-2 931	12 067	0
Derivative instruments – inflows	0	2 455	763	536	1 722	1 108	407	60	7 051
Derivative instruments – outflows	0	-2 428	-753	-551	-1 721	-1 087	-404	-59	-7 003
<b>Derivative instruments – net</b>	<b>0</b>	<b>27</b>	<b>10</b>	<b>-15</b>	<b>1</b>	<b>21</b>	<b>3</b>	<b>1</b>	<b>48</b>
Guarantee and financial lines	8 232	3	10	39	142	104	2	22	8 554
<b>Off balance-sheet gap</b>	<b>8 232</b>	<b>30</b>	<b>19</b>	<b>24</b>	<b>144</b>	<b>126</b>	<b>5</b>	<b>23</b>	<b>8 603</b>
<b>Total gap</b>	<b>1 150</b>	<b>-5 167</b>	<b>-4 169</b>	<b>-3 144</b>	<b>2 227</b>	<b>4 367</b>	<b>10 387</b>	<b>15 021</b>	<b>20 673</b>
Total accumulated gap	1 150	-3 477	-7 645	-10 789	-8 562	-4 195	6 192	20 673	0

The Bank maintains a high buffer of unencumbered high quality liquid assets, investing in Treasury and corporate debt securities with the highest ratings and characterized by high liquidity, maintaining funds on the current account with the National Bank of Poland and other banks (nostro accounts), maintaining cash in hand at the Bank and in the form of interbank deposits within the set limits. Adequacy of the liquid assets buffer is controlled by means of a comparison with the set minimum amount of the liquid assets buffer which is necessary to survive the stress scenario in a horizon of up to 7 or 30 days. As at 31 December 2016, the total unencumbered liquid assets buffer amounted to PLN 11 704 milion, whereas the minimum level resulting from the stress scenario was PLN 8 690 milion. In order to calculate the liquid assets buffer, the Bank reduces the individual buffer components to reflect the market (product) liquidity risk.

The Bank's operations, including the liquid assets portfolio, are mainly financed from the deposit base, which as at the end of 2016 was equal to approx. 90% of the liabilities.

Additionally, the Bank conducts liquidity stress tests that cover internal crisis, external crisis and mixed crisis and prepares a plan for acquiring funds in emergency situations, specifies

and verifies its liquid asset sale policies, taking into consideration the costs of maintaining liquidity. Stress test results are used to determine the minimum buffer of unencumbered high quality liquid assets, prepare emergency plans and determine internal liquidity risk limits. In accordance with Resolution No. 386/2008 of the Polish Financial Supervision Authority dated 17 December 2008, the Bank determines and reports daily the following amounts:

- the short-term liquidity gap (i.e. the minimum surplus of current liquidity) defined as the difference between the sum of the base and supplementary liquidity reserve as at the reporting date, and the value of unstable external funds. As at 31 December 2016, the surplus amounted to PLN 5,714 million;
- the ratio of coverage of non-liquid assets with own funds, calculated as the ratio of the Bank's own funds less total capital requirements relating to market risk, delivery settlement risk and counterparty risk to non-liquid assets;
- the ratio of coverage of non-liquid assets and assets with limited liquidity with own funds and stable external funds, calculated as the ratio of the Bank's own funds less total capital requirements relating to market risk, delivery settlement risk and counterparty risk, and stable external funds to the total of non-liquid assets and assets with limited liquidity;
- the short-term liquidity ratio defined as the total of the base and supplementary liquidity reserve as at the reporting date divided by the value of unstable external funds.

The values of the above-mentioned ratios as at 31 December 2016 were as follows: 4.20, 1.14, 1.95. As at 31 December 2015, they amounted to: 4.72, 1.11, 1.53. The Bank also controls the levels of the basic and supplementary liquidity reserve calculated in accordance with the above-mentioned resolution by determining the ratio of the sum of the basic and supplementary liquidity reserve to the deposit base, which as at 31 December 2016 exceeded 22% as compared to 13% as at the end of 2015.

Moreover, in accordance with the requirements of the above-mentioned Resolution, the Bank performs an in-depth analysis of long-term liquidity, stability and structure of the sources of financing, including the core deposits and concentration levels for term and current deposits. Additionally, the Bank monitors the changes in balance sheet and off-balance sheet items, in particular the amounts of projected outflows relating to credit lines and guarantees granted to the customers.

Furthermore, in accordance with the 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 (Capital Requirements Regulation - CRR), the Bank monitors the Liquidity Coverage Ratio (LCR) and maintains it at an adequate level. As at 31 December 2016, LCR amounted to 127%, whereas the required level was 70%.

On a monthly basis, the Bank also analyses the deposit base concentration in order to indicate the potential risk of excessive dependency on those sources of funding which are insufficiently diversified. To assess the level of concentration, the Bank sets a HCI (High Concentration Indicator) calculated as the ratio of funds accumulated by the largest depositaries to the value of the deposit base. As at 31 December 2016, HCI amounted to 1.70%, which indicates a lack of concentration. As at 31 December 2015, HCI amounted to 2.22%.

The HCI statistics for 2016 and 2015 are shown in the tables below.

### **High Concentration Indicator (HCI) in 2016**

Min	Average	Max
1.66%	2.07%	2.35%

#### High Concentration Indicator (HCI) in 2015

Min	Average	Max
1.97%	3.02%	4.97%

To limit concentration risk, the Bank diversifies the structure of the deposit base into retail, business, and financial customers, central and local government institutions, monitoring and reporting the share of each of the groups in the entire deposit base on a monthly basis.

In 2016 the Bank's liquidity remained at a safe level. The position was monitored and maintained at a level adequate to the Bank's needs by adjusting the deposit base and using additional sources of financing depending on the development of lending activity and other liquidity needs.

The business combination of Alior Bank S.A. with a separated part of Bank BPH, which took place on 4 November 2016, resulted in an increase in the Bank's liquidity due to taking over the excess liquidity of Bank BPH, which is used for the financing of the Bank's core activities. In 2016, Alior Bank S.A. opened its first foreign Branch in Bucharest. The Branch will obtain funds from Alior Bank S.A. and from the local market to finance its lending activity. The liquidity level of the Branch is monitored on an ongoing basis by dedicated organizational units of the Branch and the Bank's Headquarters.

## 46. Credit risk

Credit risk management and maintenance of that risk at a safe level is of fundamental importance for the stability of the Bank's activities. Credit risk is controlled by applying the Bank's regulations, especially a lending methodology and risk measurement models appropriate to individual customer segments, product and transaction types, or the principles for setting and monitoring loan security measures, and debt monitoring and collection processes. The Bank is taking steps to fully centralize and automate these processes as part of the system infrastructure while simultaneously using available external and internal information about the customers.

Credit risk is mitigated within the scope of limitations imposed by external regulations and internal policies determined by the Bank, in particular, those relating to credit exposure to a single customer, a group of entities related by capital or type of internal organization, or to industry sectors.

The credit risk management system is comprehensive and integrated with the Bank's operating processes. The credit risk management process consists of the following basic stages:

1. identification;
2. measurement;
3. monitoring;
4. reporting and controlling.

The process thus identified enables proactive supervision over current and potential risks and effective use of risk management methods and instruments.

The credit risk management system identified internal and external factors indicative of credit risk occurrence. Such factors may be found in certain areas of the Bank's business, namely:

1. Customers – examination of individual customers and groups of customers, verification of homogenous customer groups for quality of the constructed loan portfolio;
2. Products – the area covers all the risks potentially related to a specific product (on a one-off basis or for the entire loan portfolio);
3. Collaterals - in this area of business, the following aspects are verified: the correctness of collateral acceptance, collateral value and timeliness, and the correctness of the preparation of documentation related to the collateral, as well as any subsequent update of collateral value. Significant to the mitigation of credit risk is an examination of the efficiency of implementing the amended regulations on legal collateralization of loans and the application of binding procedures in this area;
4. Processes and regulations – verification of the quality and efficiency of the crediting process, loan administration, monitoring, debt collection and restructuring processes, and cooperation with external debt recovery agencies, as well as verification of the compliance of the Bank's regulations underlying the said processes with the applicable laws;
5. Systems – in particular, verification of credit-support systems and systems supporting debt monitoring and collection, as well as the efficiency of the use of those systems;
6. Distribution channels – verification of the effectiveness (and harmfulness) of the Bank's distribution channels;
7. Employees – examination of proper use of credit competencies granted to employees individually, detection of possible irregularities in the lending process;
8. External conditions – examination of the following external factors, specifically: interest rates level; foreign exchange rates; cash supply volume; unemployment rate; changes on the labour market; economic climate;
9. Credit risk management effectiveness – periodic verification of the effectiveness of the system assumptions concerning the Bank's credit risk management policies.

The Bank analyses risk both individually and on a portfolio basis, and undertakes actions which lead to:

- minimizing the credit risk in respect of individual loans at a stipulated rate of return;
- reducing the overall credit risk resulting from the Bank's defined credit portfolio.

To minimize the risk of a single exposure, each time when granting a loan or another credit product, the Bank:

1. assesses creditability and creditworthiness taking into consideration, among other things, a detailed analysis of the source of repayment of the exposure;
2. assesses collaterals, including the verification of their formal, legal and economic aspects, also taking into consideration their LTV adequacy.

Additionally, to strengthen risk controls over individual exposures, the Bank regularly monitors customers, taking actions aimed at minimizing risk if increased risk factors are discovered.

In respect of minimizing credit risk resulting from holding specific portfolios, the Bank:

1. defines and controls concentration limits;
2. monitors early warning signals from the EWS system;
3. regularly monitors the loan portfolio, controlling all significant credit risk parameters (such as PD, LTV, DTI, CoR, LGD, NPL, Coverage);
4. regularly performs stress tests.

### **Risk assessment in the lending process**

The Bank grants credit products based on crediting methodologies developed for particular customer segments and product types. The assessment of customer credit capacity, preceding the Bank's commitment, is carried out by means of the following tools which support lending: scoring or rating tools, external information (e.g. CBD DZ, CBD BR, BIK, BIG databases), and the Bank's internal databases. Commitments are granted pursuant to the Bank's lending processes determining the appropriate steps to be followed in the process, responsible Bank units and tools to be utilized.

Lending decisions are taken in accordance with the decision making process in force at the Bank (levels of competence adapted to the customer- and transaction-related risk level).

In order to regularly assess the credit risk taken and minimize potential losses on credit exposures, the Bank monitors the customer's position throughout the lending period by identifying early warning signals and periodic, individual reviews of credit exposures.

The monitoring process ends with issuing recommendations relating to the strategy of further cooperation with the Customer.

### **Segregation of competencies**

The Bank pursues the segregation of competencies policy related to acquiring the Customer and selling credit products from the function of credit risk assessment, taking lending decisions and monitoring credit exposures.

### **Concentration risk management**

With a view to protecting the Bank's stability and safety, and ensuring the appropriate quality of its assets, their diversification and profitability, and maintaining an appropriate capital level, the Bank regularly verifies concentration in various areas of activity. Excessive concentration of any individual item accompanied by credit or liquidity risk is considered to have an adverse impact on the Bank's security.

Concentration risk management in the area of the Bank's lending activities relates to:

1. exposures to individual entities or a group of entities related by capital or internal organization (including providers of collateral);
2. exposures to entities operating in the same industry sector, running the same business or trading in similar goods;
3. exposures towards entities from the same province or individual countries;
4. exposures secured with the same type of collateral (including the risk of the Bank establishing collateral on securities with similar characteristics);
5. exposures in the same currency;
6. product specification (including the purpose of financing, lending period, type of product, LtV level);
7. customer segment;
8. distribution channel;
9. special offers and promotions, so-called "statements", exemptions applied;
10. internal concentration.

Being aware of the potential threats resulting from the Bank's exposure concentrations makes it possible to manage assets and liabilities effectively and create a safe loan portfolio structure. To prevent the unfavourable outcome of excessive concentration, the Bank reduces the risk of concentration using various limits and concentration norms as provided in external regulations or internal concentration standards.

The Bank has implemented:

1. principles for identifying loan concentration risk areas;
2. the process of defining and updating limits;
3. the limit management process, specifying procedures to be applied in the event of exceeding acceptable limits;
4. risk concentration monitoring process (including reporting);
5. control measures applicable in the risk concentration management process.

### **Sector concentration – balance sheet and off-balance sheet exposures**

The following table presents the involvement of business customers Alior Bank by industry.

Section according to the Polish Classification of Businesses PKD 2007	Name of section	As at 31.12.2016	As at 31.12.2015
Section A	Agriculture, forestry, hunting and fishing	464 692	169 856
Section B	Mining and excavation	224 400	167 110
Section C	Industrial processing	6 876 624	4 275 844
Section D	Generation and supply of electrical energy, gas, steam and hot water, and air for air-conditioning	2 115 382	1 889 519
Section E	Supplying water; managing waste and sewage, and reclamation and rehabilitation activities	153 724	94 443
Section F	Construction	5 223 464	3 707 790
Section G	Wholesale and resale trading, repair of cars, including motorcycles	5 931 545	3 433 278
Section H	Transport and warehousing	946 704	485 617
Section I	Accommodation and catering activities	1 696 535	1 568 126
Section J	Information and communication	1 059 039	785 548
Section K	Financial and insurance activities	1 864 667	1 178 549
Section L	Activities related to servicing the real estate market	4 730 084	3 379 837
Section M	Professional, academic and technical activities	1 058 141	701 441
Section N	Administration and support activities	615 039	441 375
Section O	Public administration and defense; mandatory social insurance	1 753	2
Section P	Education	120 375	97 367
Section Q	Healthcare and social insurance	619 156	579 004
Section R	Activities related to culture, entertainment and recreation	358 481	107 681
Section S	Other service activities	100 285	67 723
Section U	Ex-territorial organizations and teams	3 349	0
<b>Total</b>		<b>34 163 439</b>	<b>23 130 110</b>

The above exposures contain:

- the principal amount (balance-sheet and off-balance sheet exposure without interest and fees, and without impairment allowances), reduced by the cash deposits received;
- unauthorized negative balances on current accounts;
- treasury limits reduced by received cash deposits, taking into account debt securities in the Bank's books, whose issuer is an entity from the given section.

At the end of 2016 exposure value aggravating internal concentration limits is PLN 61 908 393 thousand, of which PLN 34 163 439 thousand is exposure to business customers, while 27 744 954 thousand - individual clients. While at the end of 2015 exposure value aggravating internal concentration limits of PLN 40 378 914 thousand, of which PLN 23 130 110 thousand is exposure to business customers, while PLN 17 248 804 thousand - to individual clients.

Country	As at 31.12.2016
Poland	60 987 815
United Kingdom	298 043
Luxembourg	228 971
Cyprus	118 813
Sweden	87 117
Hungary	78 068
Switzerland	27 013
Germany	19 948
Ireland	18 806
Netherlands	13 884
Other country	29 915
<b>Total</b>	<b>61 908 393</b>

Country	As at 31.12.2015
Poland	39 758 626
United Kingdom	236 556
Sweden	88 341
Cyprus	76 841
Hungary	64 024
Luxembourg	60 787
Switzerland	24 612
Slovakia	21 494
Ireland	13 176
Germany	11 408
Other country	23 049
<b>Total</b>	<b>40 378 914</b>

The above exposures contain:

- the principal amount (balance-sheet and off-balance sheet exposure without interest and fees, and without impairment allowances), reduced by the cash deposits received;
- unauthorized negative balances on current accounts;
- treasury limits reduced by received cash deposits, taking into account debt securities in the Bank's books, whose issuer is an entity from the given country.

In the process of establishing and updating concentration limits, the Bank considers the following:

1. information on the credit risk levels pertaining to limited portfolio segments and their effect on the execution of risk appetite assumptions with respect to loan portfolio quality and the Bank's capital position;
2. sensitivity of limited portfolio segments to changes in the macroeconomic environment assessed by means of regular stress tests;

3. reliable economic and market information on all committed concentration areas, in particular macroeconomic and industry ratios, data on economic trends, projected interest rates, FX rates, political risk analyses, ratings of government and financial institutions;
4. reliable information on the economic standing of entities, industries, economic sectors; general economic data including information pertaining to the economic and political situation of countries, as well as other information required to assess concentration risk at the Bank;
5. interaction between different types of risk, such as credit risk, market risk, liquidity risk and operational risk.

### **Impairment write-downs and provisions**

The Bank assesses all balance sheet credit exposures (balance sheet groups of credit exposures) to identify objective premises for impairment, in accordance with the most current data as at the revaluation date. The Bank assesses off-balance sheet exposures in terms of the need to set up a provision.

Loan impairment is identified automatically in the Bank's central system, based on system information (repayment default) or data input by system users.

### **Catalogues of indicators of impairment**

Customer-related indicators of impairment:

- Significant repayment default/unauthorized overdraft – this evidence relates to business customers and retail customers alike and is recognized by the system if the customer is in default or has an unauthorized overdraft for more than 90 days, with a total amount of default for all customer accounts for which he is owner/ co-owner or borrower/co-borrower of at least PLN 500;
- Corporate recovery proceedings – this impairment indicator relates to business customers and is recognized on the basis of flagging a note in the system on the entrepreneur filing an application with the court for the commencement of corporate recovery proceedings;
- Bankruptcy/liquidation – this impairment indicator concerns business customers and is recognized on the basis of flagging a note in the system on filing a petition in bankruptcy;
- Consumer bankruptcy – this impairment indicator concerns individual customers and is recognized on the basis of flagging a note in the system about a consumer filing a petition in bankruptcy (so-called consumer bankruptcy);
- Undisclosed customer assets – this impairment indicator concerns business customers and retail customers alike and is recognized on the basis of flagging a note in the system about a customer submitting a false statement on property;
- Significant deterioration in the internal scoring/rating assessment – this impairment indicator concerns business customers and is recognized by the system when the assessment of customer borrowing drops by at least one class (compared to the original assessment) and at the same time is below the level acceptable by the Bank;
- Significant deterioration in the external rating assessment – this impairment indicator concerns business customers and is recognized on the basis of flagging a note in the system about reducing the external rating of the customer from the investment to speculative class;
- Significant deterioration in the economic and financial condition – this impairment indicator concerns business customers and is recognized on the basis of flagging a note in the system about a deterioration in the assessment of a customer's economic or financial condition (in line with the Resolution of the Ministry of Finance classification) by at least one category to the level of "below standard", "doubtful", or "lost";

- Customer demise – this impairment indicator refers to retail customers and is recognized upon flagging a note in the system about a customer's demise;
- No information on a customer's whereabouts – this impairment indicator refers to retail customers and is recognized by flagging a note in the system about the proven lack of the possibility of determining a customer's registered address;
- Job loss – this impairment indicator concerns retail customers and is recognized on the basis of flagging a note in the system about a customer's lack of ability to repay debt following the loss of a job;
- Financial difficulties of a customer – this impairment indicator concerns individual customers and is recognized on the basis of flagging a note in the system about the financial problems of a customer (in accordance with data from BIK – Credit Information Bureau).

Account-related indicators of impairment:

- Issuance of Bank enforcement title – this impairment indicator is recognized in the system based on input data on the issuance of a Bank Enforcement Title;
- Commencement of enforcement proceedings – this impairment indicator is recognized in the system based on input data on the Bank commencing internal enforcement proceedings;
- Effective loan agreement termination – this impairment indicator is recognized in the system based on input data on the effective date of termination of a loan agreement where the amount in default is at least PLN 500;
- Restructuring – this impairment indicator is recognized in the system based on input data on customer problems with timely debt repayment, changes in credit servicing principles made in the form of an annex to the loan agreement or signing an appropriate arrangement with the Bank;
- Debt submitted by the borrower to court – this impairment indicator is recognized in the system based on the input data on a customer submitting his debt to court;
- Identified fraud – this impairment indicator is recognized in the system based on the input data on identified fraud on the basis of a court sentence.

Indicators of impairment relating to exposures towards banks:

- Repayment default of more than 30 days – this impairment indicator is recognized based on repayment default of more than 30 days;
- Significant deterioration in the external rating by the contractor bank – this impairment indicator is recognized based on information about a deterioration in the external rating from the investment to speculative class;
- Significant deterioration in the external rating of the contractor bank's country of registration – this impairment indicator is recognized based on information about a deterioration in the external rating of the country of the contractor bank from investment to speculative class;
- Significant deterioration in the financial standing of the bank / insolvency of the bank – this impairment indicator is recognized based on information about customer risk assessed as unacceptable in the process of the periodical monitoring of limits.

Bond-related indicators of impairment:

- Lack of underlying bonds payments – this impairment indicator is recognized based on information about the lack of underlying bonds' payment at the dates set forth in the terms and conditions of the Bonds' issuance;

- Issuer's failure to fulfil other conditions set forth in the terms and conditions for the Bonds' issuance which enable the Bank to call for immediate payment.

Each account has the option of manually setting the default in the event of the occurrence of a potential impairment indicator not covered by the above listings. The default status is used where other important factors, not covered by the above listings, are identified that may constitute an indicator of impairment.

Premises for impairment of the carrying value of a credit exposure (balance sheet groups of credit exposures) are recorded in the system at customer or account level. Recorded impairment indicators at the account level result in flagging all the accounts of the given customer as impaired. Similarly, in the event of recording impairment indicators at customer level, the impairment is propagated to all the customer's accounts in the portfolio. The propagation each time applies to all accounts in respect of which the customer is the owner/co-owner or borrower/co-borrower. In respect of loan exposures in the balance sheet which became impaired, the Bank records impairment allowances in order to reduce their carrying amount to the present value of expected future cash flows.

The exposures in respect of which indicators of impairment have been identified are divided into those that are measured individually and those that are measured in groups. The individual assessment applies to exposures carrying the risk of impairment (calculated at customer level) which exceed the established thresholds set depending on the customer segment (see table).

Customer segment	Threshold	
	2016	2015
Individual customer: -loan	no threshold	no threshold
Individual customers -other products	no threshold	150 000
Business customers	500 000	500 000

Individual assessment is also applied to exposures threatened with impairment in respect of which the Bank is unable to identify a group of assets with similar credit risk characteristics or does not have a sufficient sample for estimating group parameters.

Individual assessment is based on an analysis of potential scenarios (business customers). Each scenario and tree branch are attributed the probability of finalization and the expected recoveries. The assumptions adopted for individual valuations are described in detail by the analysts. Recovery amounts expected under individual valuations are compared to the actual recoveries in quarterly cycles.

The group valuation is based on the time of a given exposure being in default and takes into account the specific nature of a given group in terms of the expected recoveries. Collateral is taken into consideration at the exposure level.

The exposures in respect of which no indications of impairment have been identified are grouped in accordance with the principle of maintaining a homogeneous risk profile and IBNR provisions are created for such groups of exposures. The amount of IBNR is determined based on PD, LGD and hedging parameters (taking into account the expected recovery rates).

PD parameters are determined on the basis of the migration matrix and the LIP (Loss Identification Period) levels applied. The period of historical data which is the basis for assessing PD was selected so as to achieve two goals: maximize the predictiveness of parameters and achieve stability of estimation. For this purpose, for most portfolios the Bank uses a 12-month observation period for migration between the delay and default baskets to determine PD. Portfolios of medium and large companies, for which the Bank uses a 24-month period due to the lower number of defaults, are an exception to this rule. The PD parameter is differentiated depending on particular delay portfolios and baskets. PD for particular delay baskets is divided into LIP periods in accordance with the table below:

Basket/Portfolio	Accounts/LOR KI	Mortgage loans KI	Credit cards KI	Loans KI	Other KI	MICRO KB	Other KB
<b>0 DPD</b>	5	6	5	5	5	5	4
<b>1-30 DPD</b>	3	3	3	3	3	3	3
<b>31-60 DPD</b>	2	2	2	2	2	2	2
<b>61-90 DPD</b>	1	1	1	1	1	1	1

The LIP parameter for individual basket overdue as of 31.12.2015 is presented in the following table:

Basket/Portfolio	Accounts/LOR KI	Mortgage loans KI	Credit cards KI	Loans KI	Other KI	MICRO KB	Other KB
<b>0 DPD</b>	5	6	5	5	5	5	4
<b>1-30 DPD</b>	4	3	3	3	4	4	3
<b>31-60 DPD</b>	3	2	2	2	2	2	2
<b>61-90 DPD</b>	2	1	1	1	1	1	1

The LIP periods were determined on the basis of a quantitative analysis and account for the period from the initial reason for the loss of ability to service debt.

### **Collateral**

Collateral is set up in an appropriate manner with reference to the credit risk incurred by the Bank and is flexible towards the customer's capabilities. Setting up the collateral does not exonerate the Bank from the duty to assess a customer's credit rating.

A loan has to be secured to ensure the Bank that the loan with the accrued interest and respective costs will be repaid if the borrower defaults on the dates determined in the loan agreement, and restructuring does not bring about the expected effects.

The Bank accepts, in particular, the following legal forms of collateral:

1. Guarantees, re-guarantees and warranties;
2. Account blocking;
3. Registered pledges;
4. Re-possession;
5. Assignment of debts;
6. Loan insurance;
7. Bills of exchange;
8. Mortgages;
9. Power of attorney to bank account;
10. Security deposits (as a special form of collateral).

Collateral is verified in the crediting process in terms of the legal ability to secure the Bank's interests, and its market value is assessed as well as the possibility of recovering it in the potential enforcement proceedings.

Debt collateral enables:

- reducing the amounts of impairment write-downs and allowances in accordance with IAS 39;
- applying more favourable risk weights for the purpose of calculating the capital requirement pursuant to Resolution No. 76/2010 of the Polish Financial Supervision Authority.

The value of collateral is taken into consideration when determining impairment write-downs of retail and business loans; in 2016 it amounted to PLN 1 277 million, and in 2015 to PLN 994 million. The value of collateral considered when IBNR allowances are calculated for loans that are not impaired in 2016 amounted to PLN 15 456 million and PLN 13 600 million in 2015. The impact of not considering the value of collateral for the level of impairment allowances would amount to, respectively, PLN 183 million in relation to impairment losses and PLN 78 million in relation to IBNR allowances as at 31 December 2016. The impact of not considering the value of collateral for the level of impairment allowances would amount to, respectively, PLN 124 million in relation to impairment losses and PLN 97 million in relation to IBNR allowances as at 31 December 2015.

### **Managing repossessed assets**

In justified cases the Bank repossesses assets put up as collateral to satisfy matured dues. Such transactions are conducted on the basis of accepted plans for managing the repossessed asset.

In 2016 Alior Bank SA only repossessed chattels classified to the widely meant group of vehicles in debt collection and restructuring processes. Assets repossessed in this manner were earmarked exclusively for sale and were not used for internal purposes.

The assets referred to above are repossessed both by internal services and using specialist external cooperating agents accepted by the Bank. Each repossessed chattel is valued to determine the selling price and to settle the repossession transaction with the collateralized loan by independent external experts operating under contracts concluded with the Bank.

In terms of individual customers in 2016, assets with a total value of PLN 79 100 thousand were repossessed and assets with a total value of PLN 69,500 thousand were sold. As at 31 December 2016, the value of chattels repossessed and not sold amounted to PLN 0.

In terms of business customers in 2016, assets with a total value of PLN 1 032 300 thousand were repossessed and assets with a total value of PLN 926 900 thousand were sold. As at 31 December 2016, the value of chattels repossessed and not sold amounted to PLN 132 700.

### **Scoring/rating**

Credit scoring is an instrument used to make individual loan decisions for individual customers and micro-companies, while credit rating is an instrument to support borrowing decisions in the segment of small, medium and large enterprises.

The scoring and rating models have been implemented to:

1. Control credit risk by acquiring reliable forecasts of a customer's creditworthiness;

2. Standardize lending criteria in an objective and unbiased manner;
3. Shorten the periods of credit decision taking, and boost the effectiveness of a credit application assessment (increase work capacity and reduce service costs);
4. Simplify the process of credit application assessment (automation);
5. Implement customer classification in terms of the degree of risk related to them;
6. Monitor and forecast the quality of the credit portfolio;
7. Simplify the assessment of binding credit policies and speed up change implementation in the decision making processes designated to assess the credit risks of business and individual customers.

The way the scoring and rating models operate is regularly monitored by the Bank. The objective of models validation is to assess whether the models applied properly differentiate risks, and whether the assessed risk parameters properly reflect the relevant risk aspects. In addition, functional controls verify whether credit process models have been applied in accordance with their designation.

The scoring models currently used were built internally in the Bank. To reinforce the risk management models operating in the Bank, a special team was appointed which plays the role of an independent validation unit.

The scoring models enable obtaining:

1. A decisive score value for a given customer/application;
2. A scoring class with a theoretical PD value ascribed;
3. A scoring recommendation for credit application, in the form of: "Approval" or "Rejection".

The type of model used to assess individual customers depends on the type and nature of the credit product for which the customer has applied, the credit history and the history of cooperation with the Bank. The type of model used to assess business customers depends on the segment in which a given customers is classified in terms of the sales revenues generated. The score achieved has an impact on the amount of standard costs of risk charged on the transaction.

As of 1 September 2015, the Bank introduced a single common rating scale with respect to PD, consisting of 25 classes (Q01-Q25). It replaced the previous scoring scale used for micro-enterprises that maintain simplified accounting (classes B1-B10) and five rating scales used for enterprises that carry out full financial reporting (classes A-J). In order to achieve uniform results, all scores/ratings in the business customers segment were presented in accordance with the new scale.

Due to the different scoring model occurring in the acquired separated part of Bank BPH data were presented separately.

The following table shows the data Alior Bank acquired without a separate part of BPH S.A.

Financial assets not overdue	Risk class	As at 31.12.2016	As at 31.12.2015
<b>Receivables not overdue and not impaired</b>			
<b>Retail segment</b>			
<b>Mortgage loans, cash loans, credit cards, current account overdraft</b>			
(1 – best class, 6 – worst class)	1	601 987	700 449
	2	603 978	691 423
	3	736 933	808 399
	4	828 111	887 246
	5	47 857	6 851

6 6 424 51 867

**Loans, credit cards, current account overdraft – standard process**

(K1 - best class, K10 - worst class)

K1	662 345	341 778
K2	641 286	426 684
K3	1 170 940	795 538
K4	1 466 667	1 084 859
K5	1 570 465	1 227 531
K6	1 456 033	1 034 654
K7	676 328	561 920
K8	218 700	201 861
K9	33 041	40 719
K10	3 206	3 809

**Mortgage loans**

(M1 – best class, M10 – worst class)

M1	3 586	2 818
M2	28 188	21 767
M3	138 149	103 571
M4	510 387	381 809
M5	1 287 607	935 591
M6	1 720 101	1 254 284
M7	1 323 442	940 449
M8	865 187	613 014
M9	346 980	233 637
M10	81 616	54 473

Without scoring

1 942 735

2 151 619

**Total retail segment**

**18 972 279**

**15 558 620**

**Business segment**

**Non-current products, car loans, current account overdraft limits**

(1 – best class, 6 – worst class)

1	1 048	7 785
2	7 029	11 784
3	2 573	16 478
4	3 474	6 172
5	0	0

(Q01 – best class, Q25 – worst class)

(Q01 – best class, Q25 – worst class)	Q01	0	21
	Q02	896	13 370
	Q03	20 147	195 015
	Q04	104 890	190 236
	Q05	212 485	17 095
	Q06	402 232	1 074 832
	Q07	575 500	402 377
	Q08	1 058 323	161 978
	Q09	509 064	1 038 925
	Q10	497 794	262 246
	Q11	1 035 165	1 293 114
	Q12	1 706 950	709 894
	Q13	1 148 374	521 595
	Q14	1 955 724	992 276
	Q15	900 742	355 544

Q16	990 141	694 126
Q17	657 114	674 844
Q18	517 857	288 928
Q19	417 234	626 156
Q20	248 403	163 146
Q21	214 957	89 767
Q22	252 574	51 762
Q23	55 150	71 686
Q24	85 344	2 108
Q25	36 340	44 906
No rating	1 108 199	641 028
<b>Total business segment</b>	<b>14 725 722</b>	<b>10 619 194</b>
<b>Receivables not overdue, not impaired</b>	<b>33 698 001</b>	<b>26 177 814</b>
Receivables not overdue, impaired	320 148	152 849
Retail segment	59 976	37 337
Business segment	260 172	115 512
<b>Total loans and advances to customers, not overdue</b>	<b>34 018 149</b>	<b>26 330 663</b>
<b>Available-for-sale financial assets:</b>		
issued by non-financial institutions	No scoring	219 735
issued by other financial institutions	No scoring	96 868
<b>Available-for-sale financial assets not overdue, not impaired</b>	<b>316 603</b>	<b>216 094</b>
Available-for-sale financial assets not overdue, impaired	No scoring	73 415
<b>Total available-for-sale financial assets not overdue</b>	<b>390 018</b>	<b>302 744</b>
<b>Financial assets held for trading</b>		
<b>Derivative instruments</b>		
(Q01 – best class, Q25 – worst class)		
Q02	5 802	0
Q03	29	7 622
Q04	8 075	4 710
Q05	1 400	1
Q06	8 585	7 910
Q07	4 107	5 721
Q08	24 995	1 939
Q09	11 283	17 424
Q10	8 375	7 970
Q11	13 611	16 638
Q12	13 858	9 399
Q13	9 510	8 111
Q14	23 737	18 598
Q15	8 860	5 334
Q16	12 287	12 280
Q17	8 605	10 970
Q18	4 416	4 910
Q19	4 655	6 148
Q20	3 204	2 766
Q21	4 320	1 741
Q22	1 277	54
Q23	516	4 962
Q24	8 830	0
Q25	309	681
No scoring	15 451	47 341
<b>Shares</b>	<b>6 312</b>	<b>1 335</b>
<b>Bonds</b>	<b>294</b>	<b>311</b>
<b>Certificates</b>	<b>557</b>	<b>1 610</b>
<b>Total financial assets held for trading</b>	<b>213 260</b>	<b>206 486</b>

The following table contains information regarding the acquired separated part of Bank BPH.

Receivables not overdue and not impaired	Risk class	average PD	As at 31.12.2016
<b>Retail segment</b>			
1-3	0.10%	4 648	
4 (4+, 4, 4-)	0.50%	145 292	
5 (5+, 5, 5-)	1.30%	736 766	
6 (6+, 6, 6-)	3.20%	2 497 289	
7 (7+, 7, 7-)	8.20%	501 771	
8 (8+, 8)	above 20%	149 013	
Receivables with impaired(8-, 9, 10)		4	
No rating		19 029	
<b>Total retail segment</b>			<b>4 053 812</b>
1-3	0.10%	184 068	
4 (4+, 4, 4-)	0.50%	903 654	
5 (5+, 5, 5-)	1.30%	1 349 918	
6 (6+, 6, 6-)	3.20%	695 052	
7 (7+, 7, 7-)	8.20%	159 273	
8 (8+, 8)	above 20%	18 556	
Receivables with impaired (8-, 9, 10)		96 116	
No rating		63 627	
<b>Total business segment</b>			<b>3 470 264</b>
<b>Receivables not overdue, not impaired</b>			<b>7 524 076</b>
<b>Receivables not overdue, impaired</b>			<b>200 186</b>
Retail segment			47 044
business segment			153 142
<b>Total loans and advances to customers, not overdue</b>			<b>7 724 262</b>
<b>Available-for-sale financial assets:</b>			
1-3	0.1%	1 409	
4 (4+, 4, 4-)	0.5%	4 418	
5 (5+, 5, 5-)	1.3%	12 728	
6 (6+, 6, 6-)	32%	6 846	
7 (7+, 7, 7-)	8.2%	150	
8 (8+, 8)	above 20%	1 464	
No rating		88	
<b>Total available-for-sale financial assets:</b>			<b>27 103</b>

### Overdue loans and advances to customers

As at 31.12.2016	Up to 1 month	From 1 month to 3 months	from 3 months to 1 year	from 1 year to 5 years	from 5 years	Total
---------------------	------------------	-----------------------------	----------------------------	---------------------------	-----------------	-------

<b>Amounts due, not impaired</b>	<b>2 184 687</b>	<b>536 694</b>	<b>119 184</b>	<b>130 302</b>	<b>3 250</b>	<b>2 974 116</b>
Retail segment	1 519 443	404 861	12 907	33 458	539	1 971 208
Business segment	665 244	131 832	106 276	96 844	2 711	1 002 908
<b>Amounts due, impaired</b>	<b>172 862</b>	<b>137 040</b>	<b>521 440</b>	<b>718 336</b>	<b>13 644</b>	<b>1 563 321</b>
Retail segment	51 155	81 415	289 363	360 680	4 289	786 903
Business segment	121 707	55 625	232 076	357 656	9 355	776 419
<b>Total amount due</b>	<b>2 357 549</b>	<b>673 734</b>	<b>640 624</b>	<b>848 638</b>	<b>16 894</b>	<b>4 537 438</b>

<b>As at 31.12.2015</b>	<b>Up to 1 month</b>	<b>From 1 month to 3 months</b>	<b>from 3 months to 1 year</b>	<b>from 1 year to 5 years</b>	<b>from 5 years</b>	<b>Total</b>
<b>Amounts due, not impaired</b>	<b>2 807 250</b>	<b>412 737</b>	<b>137 026</b>	<b>100 720</b>	<b>3 372</b>	<b>3 461 105</b>
Retail segment	1 047 724	257 776	49 819	20 449	2 745	1 378 513
Business segment	1 759 526	154 961	87 207	80 271	627	2 082 592
<b>Amounts due, impaired</b>	<b>145 409</b>	<b>121 262</b>	<b>329 481</b>	<b>523 603</b>	<b>2 467</b>	<b>1 122 222</b>
Retail segment	55 540	76 767	204 451	282 620	1 466	620 844
Business segment	89 869	44 495	125 030	240 983	1 001	501 378
<b>Total amount due</b>	<b>2 952 659</b>	<b>533 999</b>	<b>466 507</b>	<b>624 323</b>	<b>5 839</b>	<b>4 583 327</b>

## External rating classes

The structure of debt securities and amounts due from banks by external rating class is presented below.

The Bank does not assess other trade receivables by rating class.

<b>Portfolio/Rating</b>	<b>AAA</b>	<b>AA- do AA+</b>	<b>A- do A+</b>	<b>BBB- do BBB+</b>	<b>BB- do BB+</b>	<b>B- do B+</b>	<b>without rating</b>	<b>31.12.2016</b>
<b>Amounts due from banks</b>	<b>0</b>	<b>88 791</b>	<b>1 124 622</b>	<b>84 655</b>	<b>3 394</b>	<b>0</b>	<b>62 764</b>	<b>1 364 226</b>
<b>Available-for-sale debt instruments</b>	<b>0</b>	<b>0</b>	<b>8 889 109</b>	<b>0</b>	<b>0</b>	<b>0</b>	<b>78 607</b>	<b>8 967 716</b>
<b>Available-for-sale debt instruments</b>	<b>0</b>	<b>0</b>	<b>8 889 109</b>	<b>0</b>	<b>0</b>	<b>0</b>	<b>59 880</b>	<b>8 948 989</b>
including:								
issued by the Central Bank	0	0	2 599 538	0	0	0	0	2 599 538
issued by the State Treasury	0	0	6 197 981	0	0	0	0	6 197 981
issued by banks	0	0	91 590	0	0	0	0	91 590
issued by other financial institutions	0	0	0	0	0	0	59 880	59 880
<b>Investment securities held to maturity</b>	<b>0</b>	<b>0</b>	<b>1 954</b>	<b>0</b>	<b>0</b>	<b>0</b>	<b>0</b>	<b>1 954</b>
<b>Assets pledged as collateral</b>	<b>0</b>	<b>0</b>	<b>365 732</b>	<b>0</b>	<b>0</b>	<b>0</b>	<b>1 252</b>	<b>366 984</b>
<b>Derivative financial instruments</b>	<b>0</b>	<b>33</b>	<b>143 001</b>	<b>15 288</b>	<b>0</b>	<b>0</b>	<b>20 866</b>	<b>179 188</b>
<b>Total</b>	<b>0</b>	<b>88 824</b>	<b>10 524 418</b>	<b>99 943</b>	<b>3 394</b>	<b>0</b>	<b>163 489</b>	<b>10 880 068</b>

<b>Portfolio/Rating</b>	<b>AAA</b>	<b>AA- do AA+</b>	<b>A- do A+</b>	<b>BBB- do BBB+</b>	<b>BB- do BB+</b>	<b>B- do B+</b>	<b>without rating</b>	<b>31.12.2015</b>
-------------------------	------------	-----------------------	-----------------	-------------------------	-----------------------	---------------------	---------------------------	-------------------

<b>Amounts due from banks</b>	<b>0</b>	<b>113 751</b>	<b>425 474</b>	<b>19 519</b>	<b>58 713</b>	<b>0</b>	<b>25 083</b>	<b>642 540</b>
<b>Available-for-sale debt instruments</b>	<b>0</b>	<b>0</b>	<b>3 853 838</b>	<b>11 440</b>	<b>24 611</b>	<b>60 486</b>	<b>0</b>	<b>3 950 375</b>
including:								
issued by the Central Bank	0	0	0	0	0	0	0	0
issued by the State Treasury	0	0	3 773 380	0	0	0	0	3 773 380
issued by banks	0	0	0	0	0	0	0	0
issued by other financial institutions	0	0	80 458	11 440	24 611	60 486	00	176 995
<b>Assets pledged as collateral</b>	<b>0</b>	<b>0</b>	<b>628 332</b>	<b>0</b>	<b>0</b>	<b>0</b>	<b>0</b>	<b>628 332</b>
<b>Derivative financial instruments</b>	<b>0</b>	<b>8 719</b>	<b>275 301</b>	<b>37 667</b>	<b>29</b>	<b>0</b>	<b>1 945</b>	<b>323 661</b>
<b>Total</b>	<b>0</b>	<b>122 470</b>	<b>5 182 945</b>	<b>68 626</b>	<b>83 353</b>	<b>60 486</b>	<b>27 028</b>	<b>5 544 908</b>

### Monitoring credit risks related to retail and business customers

Continuous credit portfolio quality protection is ensured by:

- daily monitoring of timely loan repayments;
- periodic reviews – relating mainly to a customer's economic standing and the value of approved collaterals.

The monitoring of the individual customer segment includes the following areas:

- customers;
- credit products granted to debtors;
- agreements from which the credit exposure originated;
- collaterals approved;
- amount of impairment write-downs and provisions recorded.

Monitoring of the business customer segment mainly includes the following areas:

- customers and their related entities;
- business segment;
- credit products granted to debtors;
- verification of the customer's compliance with the provisions of the agreement which is the basis for the customer's credit exposure;
- collaterals approved (verification of their setting up and value);
- market conditions with affect the customer's credit capacity;
- amount of impairment write-downs and provisions recorded.

All credit exposures in the business customer segment are additionally covered by portfolio monitoring, i.e.:

- assessment on the basis of a dedicated behavioural assessment model; and
- an early warning flags identification process.

All credit exposures of retail and business customers are subject to monitoring and ongoing classification to appropriate process paths. To improve the monitoring process and controls of potential operating risks, adequate solutions have been implemented in the Bank's credit systems. System tools have been consolidated to effectively conduct the monitoring procedures (soon to be applicable to all the accounts).

Commitments classified as standard and dangerous, which may intensify the activity during pre-enforcement and debt collection proceedings, are regularly monitored. Accounts are evaluated with regard to transformation of debt under the restructuring procedure in order to minimize the Bank's default losses.

### The Bank's maximum exposure to credit risk

Items in the statement of financial position	As at 31.12.2016	As at 31.12.2015
Current account at the central bank	532 566	1 559 981
Financial assets held for trading	413 239	389 234
Bonds	294	311
Certificates	557	1 610
Interest rate transactions	189 703	198 578
Foreign exchange transactions	174 953	132 012
Other options	28 736	34 555
Other instruments	18 996	22 168
Available-for-sale financial assets	9 339 005	4 239 445
Debt instruments	9 339 005	4 239 445
issued by the State Treasury	6 197 981	3 773 380
issued by other governmental institutions	0	0
issued by monetary institutions	2 691 128	0
issued by other financial institutions	156 746	176 995
issued by companies	293 150	289 070
Hedging derivatives financial instruments	71 684	139 578
Amounts due from banks	1 364 226	642 540
Loans and advances to customers	46 279 849	30 913 990
Retail segment	25 891 222	17 595 314
Working capital facility	293 951	167 635
Consumer loans	13 956 654	8 699 017
Consumer finance loans	1 253 001	748 948
Loans for purchase of securities	125 117	119 069
Credit card loans	970 319	225 629
Loans for residential real estate	8 407 632	6 717 911
Other mortgage loans	833 485	896 008
Other receivables	51 063	21 097
Corporate segment	20 388 627	13 318 676
Working capital facility	11 114 177	7 361 826
Car loans	131 971	70 394
Investment loans	7 517 095	5 487 618
Acquired receivables (factoring)	794 087	376 403
Reverse Repo/BSB	680 780	0
Other receivables	150 517	22 435
Assets pledged as collateral	366 984	628 332
Other financial assets	690 338	363 771
<b>Total</b>	<b>59 057 891</b>	<b>38 876 871</b>

Off-balance sheet items	As at 31.12.2016	As at 31.12.2015
Off-balance sheet liabilities granted	14 157 110	8 552 647
Relating to financing	13 054 317	7 371 753
Finance Guarantees	1 102 793	1 180 894

In the Bank's opinion, the carrying amount best reflects maximum risk exposure.

## Applying forbearance practices

In the restructuring process of the Retail Customer the Bank uses the following tools:

- Extending the lending period. Extending the lending period leads to a reduction in monthly principal and interest instalments, and cannot exceed 120 months (for unsecured products), irrespective of the initial lending period. If under the restructuring process the lending period is extended on a one-off basis for the maximum period, the tool cannot be used again in the future. When the lending period is extended, restrictions following from the product statement, such as the age of the borrower, are taken into account.
- Granting a payment grace period (the whole or part of the instalment). In the grace period for the payment of capital and interest instalments the borrower is not obliged to make any payments in respect of the contract concluded. The loan repayment period may be extended by the number of months of the grace period granted (this is not identical to applying the tool which extends the lending period). A grace period for a full instalment is applied for up to 3 months, the grace period for the principal part of the instalment cannot exceed 6 months. The maximum total grace period may amount to 6 months during 2 consecutive years (24 months), as of the date of signing the restructuring annex;
- Consolidation of several liabilities to Alior Bank, including change in the LOR debit limit /unauthorized ROR debit/consumer loan, to an instalment loan. The effect of consolidation is the transformation of several dues resulting from different contracts into one due. The product initiated as a result of the consolidation is paid back in monthly instalments on the basis of a predefined time schedule. The parameters of the product initiated as a result of applying the given tool have to be compliant with the Product Statement: cash loan/consolidation loan.

In particularly justified situations other tools may be used.

In the restructuring process of a Business Customer no restrictions were introduced relating to the forms of forbearance practices applied. Due to the specific nature of the customers, the most frequently used tools are:

- Arrangement through a change in the time schedule for matured exposures (after maturity or termination notice). This consists of transferring the debt from one or more exposures to a non-renewable account with potential options for the time schedule: settlement of the whole debt on an accruals basis, or settling part of the debt on an accruals basis, and part as a payment at the end of the period.
- An annex reducing the limit in respect of renewable loans. This consists of systematic reduction in the credit limit (most often on a monthly basis) by the amount specified in the annex.
- The annex changing the terms and conditions relating to the deadline for payment /amount of instalment or grace period for the principal /interest.

## Monitoring of the risk relating to forbearance practices

Reporting the quality of restructured loan portfolio covers reporting at the level of particular overdue period brackets at which the restructuring decision was taken, and at the aggregate level. The base reporting period is a calendar month. In such breakdown the following sub-processes may be identified to which the presented amounts refer:

- The application process (number of applications, number of decisions issued, types of decisions);
- Quality of the loan portfolio (break-down into particular overdue levels, forms of restructuring, application of overrides);

- Measure of overdue period exceeding 90 days on restructured accounts in consecutive quarters, according to the balances as at the end of consecutive quarters after restructuring.

The results of the above monitoring of the restructured portfolio are shown in the monthly presentations for the Management Board.

The following risks relate to the application of forbearance tools by the Bank:

- Risk of lack/discontinuation of payments;
- Risk of loss of collateral (in particular chattels) or a significant reduction of its value;
- Risk of bankruptcy.

The Bank mitigates the above risks mainly through the Customer analysis, both in terms of financial possibilities and the history of cooperation with the Customer, information from site visits and other sources. Collateral may be used and exposure may thus be reduced before the forbearance tools are used. Using forbearance tools the Bank makes efforts to additionally insure the exposure to the largest possible extent (mortgage, warranties, pledges). Each Customer in respect of whom forbearance tools are used has an allocated care person from the Debt Collection Team who monitors the customer on an on-going basis in respect of delays, so as to react dynamically to any negative premises as they appear. Customers are obliged to cyclically update inventory balances in the event of pledges on inventories or to update their policies. In justified cases the Bank uses On-Site Collection – one of its functions is verification of the collateral.

#### **Assessment of impairment for exposures subject to forbearance practices**

In respect of forbearance practices the Bank adopts more stringent criteria for impairment identification. Apart from the standard catalogue of premises, additional criteria are used in respect of these exposures, defined as forbearance granted to a customer upon one of the following situations arising:

- A delay exceeding 30 days;
- Another indicator of impairment;
- An analyst's assessment of the timeliness of debt servicing being at risk (in respect of Retail Customers);
- Assessment of the economic and financial position as Substandard or worse (in respect of Business Customers).

In 2014 the Bank implemented a mechanism for marking entry to the forbearance status and exiting it in accordance with the provisions of the "EBA FINAL draft Implementing Technical Standards on Supervisory reporting on forbearance and non-performing exposures under article 99(4) of Regulation (EU) No 575/2013". The changes introduced had no impact on the manner of identifying impairment or the terms and conditions for reversing losses. Having identified premises for impairment subject to forbearance practices, the Bank acts according to the principle that three consecutive timely payments compliant with the new time schedule are the basis for determining the absence of impairment premises.

The Bank does not differentiate its approach to recognizing impairment depending on the type of facilitation granted to the customer. All types of facilitation are subject to additional, more stringent criteria for identifying impairment.

<b>Loans and advances to customers subject to forbearance practices</b>	<b>As at 31.12.2016</b>	<b>As at 31.12.2015</b>
Retail segment	183 788	100 422
not impaired	66 287	50 279
impaired	293 305	79 575
IBNR	- 655	-212
impairment allowances	-175 149	-29 220
individually assessed	-	-16 672
collectively assessed	- 175 149	-12 548
Corporate segment	615 948	255 597
not impaired	188 735	131 887
impaired	635 651	230 518
IBNR	-1 856	-26
impairment allowances	- 206 582	-106 782
individually assessed	-156 462	-90487
collectively assessed	-50 120	-16 295
<b>Total</b>	<b>799 736</b>	<b>356 019</b>

<b>Loans and advances to customers subject to forbearance practices</b>	<b>As at 31.12.2016</b>	<b>As at 31.12.2015</b>
impaired	547 225	174 091
including the amount of collateral	339 707	124 648
not impaired	252 511	181 928
including the amount of collateral	143 256	97 742
not overdue	109 180	85 305
overdue	143 331	96 623
<b>Total</b>	<b>799 736</b>	<b>356 019</b>

<b>Loans and advances to customers subject to forbearance practices by region</b>	<b>As at 31.12.2016</b>	<b>As at 31.12.2015</b>
dolnośląski	20 609	25 783
kujawsko-pomorski	16 068	19 444
lubelski	25 208	14 492
lubuski	24 605	13 802
Łódzki	38 465	26 478
małopolski	135 912	72 535
mazowiecki	125 188	67 946
opolski	12 924	1 975
podkarpacki	14 014	2 452
podlaski	7 041	2 276
pomorski	272 732	22 953
śląski	45 803	26 345
świętokrzyski	3 836	785
warmińsko-mazurski	10 888	13 693
wielkopolski	39 828	37 240
zachodniopomorski	6 615	7 820
<b>Total</b>	<b>799 736</b>	<b>356 019</b>

Change in the carrying amount of loans and advances to customers subject to forbearance practices	As at 31.12.2016	As at 31.12.2015
net carrying amount at the beginning of the period	356 019	392 951
change from the purchase of a separate part of the company BPH	307 878	0
impairment allowance	-34 609	-37 535
gross carrying amount of loans and advances excluded during the period	-46 103	-206 515
gross carrying amount of loans and advances included during the period	235 434	208 271
other changes	-18 883	-1 153
<b>Net carrying amount at the end of the period</b>	<b>799 736</b>	<b>356 019</b>

In the years 2016 and 2015, interest income on loans that were subject to forbearance amounted to PLN 30,114 thousand and PLN 20,307 thousand, respectively.

## 47. Operational risk

The purpose of managing the Bank's operational risk is to minimize its operational risk exposure, which is understood as the possibility of incurring losses resulting from failure to deploy internal processes, staff, systems or to external threats.

The Bank has a formalized operational risk management system in place, which is used to prevent the occurrence of operational events and incidents and limit losses in the event that the risk materializes. The principles and the structure of operational risk management in Alior Bank are based on the provisions of the Banking Law, the provisions of resolutions and recommendations of the Polish Financial Supervision Authority, and the Operational Risk Management Policy approved by the Bank's Management Board and Supervisory Board.

The Operational Risk Management Policy specifies, among other things, the operational risk management strategy, including the Bank's risk appetite, and the operational risk management system and principles, which comprise:

- Identification;
- assessment and measurement;
- counteracting;
- controlling;
- monitoring, and
- reporting of operational risk.

The Bank applies the standardized approach to calculating the capital adequacy in respect of operational risk.

The operational risk management structure at the Bank consists of: the Supervisory Board, the Bank's Management Board and the Operational Risk Committee (ORC).

The Management Board, which participates in Alior Bank's risk operational management process, is responsible for the correct functioning of the operational risk management and control processes, and specifically supports the process:

- by accepting the Bank's policy in this respect;
- by determining competencies and segregation of duties in the operational risk management process;
- by appointing and approving the composition of the Operational Risk Committee;

- by approving the level of internal operational risk limits and risk appetite;
- by conducting regular assessments of the operational risk management process and the level of use of internal operational risk limits and risk appetite;
- by creating and developing an organizational structure in the area of effective operational risk management.

Execution of the adopted operational risk strategy is supervised by the Supervisory Board, which, among other things:

- approves the Management Board's competencies which are necessary to manage operational risk;
- approves the Policy specifying the overall operational risk management strategies;
- approves and assesses the pursuit of strategies and – if necessary – orders that it be revised;
- periodically assesses the level of risk on the basis of information submitted by the Bank's Management Board and Operational Risk Committee;
- recommends actions to be taken to mitigate risk or change the Bank's operational risk profile.

The Operational Risk Committee advises and supports the Management Board in effective risk management. The Operational Risk Committee monitors the level of exposure to operational risk on an ongoing basis and assesses the current operational risk position at Bank level. It also participates in the operational risk management process, among other things, by:

- assessing the operational risk of the Bank's projects;
- approving or recommending changes in business continuity plans;
- determining the scope of self-assessment of the operational risk by the Bank;
- approving assumptions for conducting stress tests in respect of operational risk and their results.

It also issues the necessary recommendations and decisions to counteract operational issues, and if such are identified, mitigates their effects.

The process of mitigating operational risk is one of the most important elements of operational risk management as the decisions regarding the mitigation of this risk have a direct impact on its profile. Based on the recommendations of the Operational Risk Committee regarding the Bank's operating areas which are particularly exposed to operational threats, the Bank's Management Board takes decisions on the Bank's further actions aimed at mitigating or accepting the operational risk, or on discontinuing operations which are exposed to operational risk. The Management Board may decide to insure the identified operational risk.

The Operational Risk Team is responsible for ongoing control and monitoring of operational risk. This entity is also responsible for:

- developing and implementing appropriate operational risk methodologies and controls;
- giving opinions on and consulting the assessment of operational risk of the Bank's projects, products and procedures (new and modified);
- monitoring the level of utilization of internal operational risk limits;
- accumulating high quality data on events and operational results;
- monitoring internal and external events;
- monitoring the level of the Bank's risk using the tools used by the Bank, such as the level of key risk indices (KRI) and self-assessment;
- preparing cyclic reports relating to the operational risk level at the Bank.

The duty to monitor and mitigate operational risk in day-to-day activities relates to all the Bank's employees and organizational entities. The Bank's employees control the operational risk level on an ongoing basis in respect of the processes they are responsible for, and actively manage the risk exposure, taking action to avoid/limit operating losses. They are responsible for ongoing registration of events and financial operating losses relating to their areas of operation, they define and report the Key Risk Indicator (KRI) levels and the level of tolerance for processes particularly exposed to operational risk; they also participate in the self-assessment process.

### **Recording events/incidents and operating losses**

The Bank records the events, incidents and operating losses, which enables it to effectively analyse and monitor operational risks in accordance with the internal instruction specifying the registration principles. The records are maintained using the OpRisk system, which supports operational risk management and enables registering, analysing, measuring and monitoring data.

Since the business combination of the Banks, work has been carried out to introduce uniform principles and practices relating to operational risk management. The first stage consisted of the migration of operational events and losses from the separated part of the Bank BPH SA to the Oprisk system and the identification of new limits and operational risk appetite reflecting the risk profile of the combined Bank.

The combined Banks recognized gross operating losses of PLN 31,194 thousand in 2016. The operating losses increased by PLN 18,168 thousand in 2016 in relation to the year 2015, when they amounted to PLN 13,026 thousand (this amount includes operating losses in respect of loans incurred by ex Meritum Bank). In 2016, the amount of recoveries/operating income in respect of operational risk amounted to PLN 13,923 thousand, compared to PLN 8,688 thousand in 2015.

## **48. Capital management**

The purpose of managing capital by the Bank is to maintain an appropriate amount of own funds and Tier 1 capital to cover risk at the required level, in accordance with the assumed risk appetite, at each moment of operation.

Under its risk appetite the Bank determines the expected levels of coverage – by own funds and Tier 1 capital – of potential unexpected losses due to particular types of risk specified in the Regulation of the European Parliament and Council (EU) No. 575/2013 dated 26 June 2013 on prudential requirements for credit institutions and investment firms (CRR Regulation) and particular types of risk identified under the internal capital adequacy assessment process (ICAAP). Potential unexpected losses are determined using regulatory capital according to the methodology specified in the CRR Regulation and using internal capital determined using the methodology described below.

### **Capital management responsibility**

The Bank's Supervisory Board, Management Board, the Risk Management Committee and ICAAP take an active part in capital management.

Competencies of the Supervisory Board

- Approving the principles for estimating internal capital, capital management and capital planning

Competencies of the Management Board

- Preparation and implementation of the internal capital estimation processes

- Preparation and implementation of capital management processes
- Preparation and implementation of capital planning processes
- Regular ICAAP reviews
- Analysis of ICAAP reports (monitoring of capital targets and risk profile)
- Supervision over the ICAAP process

Competencies of the Risk Management Committee and ICAAP:

- Supervising the ICAAP process in the Bank, including the process of risk review and assessing the internal capital to cover material risks
- Monitoring capital goals, limits of capital allocation and limits for the solvency ratio and Tier 1 ratio
- Giving opinions on ICAAP process reviews

### **Capital adequacy measures**

The basic tools used by Alior Bank for capital management include:

1. The total capital ratio and Tier 1 ratio
2. Analysis of the regulatory capital requirement

Internal capital (ICAAP) and the ratio of covering internal capital with own funds.

### **48.1 Capital adequacy ratio**

As at 31 December 2016, the capital adequacy ratio and Tier 1 ratio were calculated in accordance with the Regulation of the European Parliament and of Council (EU) No. 575/2013 dated 26 June 2013 on prudential requirements for credit institutions and investment firms, amending Regulation (EU) No 648/2012 ("CRR Regulation"). Until the date of these financial statements, a part of the regulations relating to determining own funds and capital requirements (the so-called "national options") were not addressed or published by a Polish authority or public body authorized to supervise credit institutions and investment firms. A conservative approach was adopted to calculating the capital adequacy ratio in the non-regulated area; this related, among other things, to percentage amounts in the transition period and the risk weights in respect of foreign currency exposures secured with mortgages, for which this approach was indicated by the PFSA as potential "national options". It should be noted that if "national options" were determined and published, the Bank's capital adequacy could differ from that published in these financial statements.

Calculation of funds and capital adequacy ratio	As at 31.12.2016	As at 31.12.2015
<b>Total own funds for the</b>	<b>6 354 996</b>	<b>3 854 619</b>
<b>Share capital Tier I (CET1)</b>	<b>5 261 611</b>	<b>2 977 213</b>
<b>Additional capital Tier II</b>	<b>1 093 385</b>	<b>877 406</b>
Paid-up share capital	1 292 578	727 075
Supplementary capital	4 184 953	2 280 668
Other Capital	184 894	187 544
Profit verified by statutory auditor	168 419	178 463
Revaluation reserve - unrealized loss	-80 043	-12 901
Intangible assets measured at carrying amount	-480 913	-379 820
Revaluation reserve - unrealized profits	1 867	1 790
Subordinated liabilities	1 093 385	877 406
Additional valuation adjustments	-10 144	-5 606
<b>Capital requirements</b>	<b>3 717 843</b>	<b>2 459 640</b>
Capital requirements for the following risks: credit, counterparty, credit valuation adjustment, dilution and delivery of instruments to be settled at a later date	3 234 976	2 216 262
Total capital requirements for the following risks: equity instrument price risk, debt instrument price risk, commodity prices and FX risk	2 687	2 520
Capital requirement for general interest rate risks	65 760	32 637

Capital requirements for operating risk	414 420	208 221
<b>Tier 1</b>	<b>11.32%</b>	<b>9.68%</b>
<b>Capital adequacy ratio</b>	<b>13.67%</b>	<b>12.54%</b>

Following the recommendation of the PFSA for the sector in 2016, the Bank is obliged to keep the capital requirement ratio CET1 of at least 10,25% and a total of at least 13,25% of the TCR. Respectively in 2015 CET1 – 9% and TCR – 12%.

### Balance sheet and off-balance sheet exposures in credit risk by classes

	31.12.2016	31.12.2015		
Exposure class in the standard method	Exposure value	Risk weighted exposure value	Exposure value	Risk weighted exposure value
Governments and central banks	10 045 408	1 317 479	6 221 473	693 721
Institutions	1 751 428	657 698	1 349 818	563 649
Enterprises	13 458 697	7 088 938	7 636 196	4 894 565
Retail	25 159 847	14 297 952	16 209 459	8 736 945
Secured on real estates	19 017 656	11 872 068	14 569 557	9 415 917
Other	7 705 293	5 101 728	4 200 228	3 293 317
<b>Total</b>	<b>77 138 329</b>	<b>40 335 863</b>	<b>50 186 731</b>	<b>27 598 114</b>

### Primary balance sheet exposure value in credit risk, by exposure types

Exposure type	31.12.2016	31.12.2015
Cash in hand and equivalent items	206 416	192 824
Securities	9 702 042	4 863 185
Loans	47 719 677	33 810 060
Property, plant and equipment	246 290	227 633
Intangible assets	480 913	379 820
Other	3 190 409	966 039
<b>Total</b>	<b>61 545 747</b>	<b>40 439 561</b>

According to the Delegated Commission Regulation (EU) No. 183/2014 of 20.12.2013 the exposure includes adjustments for general and specific credit risk included in the Tier 1 capital.

### 48.2. Analysis of the regulatory capital requirement

In calculating its capital adequacy ratios, the Bank analyses the regulatory capital requirement level and the relation of its own funds to internal capital. The analysis consists in comparing actual values to budgeted values and explaining the possible differences: whether they are caused other than by the planned scale of the Bank's activity (especially the loan portfolio size) or other than the planned asset risk profile. During 2016, the Bank's equity exceeded the total capital requirement.

### Accounting for risk in the assessment of the goals to be met by business units

The Bank's business model defines the goal to be met by individual business units as profitability with elements of risk assessment (expected losses) and costs of capital. Costs of capital are understood as the product of the Bank's assumed RoE and the amount of regulatory capital which arose as a result of the operations of the given unit.

### 48.3. Internal capital

Under the ICAAP process, the Bank identifies and assesses the materiality of all types of risks to which it is exposed in connection with its operations.

Material types of risk as at 31 December 2016:

1. Credit risk – insolvency

2. Credit risk – industry concentration
3. Credit risk – customer concentration
4. Credit risk – currency concentration
5. Operational risk
6. Liquidity risk
7. Interest rate risk in the banking book
8. Market risk
9. Model risk
10. Reputation risk
11. Business risk

The Bank allocates internal capital using internal risk assessment models to particular risks identified as material for the Bank. Internal capital is assessed in respect of:

- credit risk based on the CreditRisk+ methodology as 99.95 quantile of the distribution of losses on the loan portfolio;
- market risk and interest rate risk in respect of the banking book, based on the VaR methodology;
- liquidity risk based on the liquidity gap model under the stress scenario;
- operational risk based on the model accounting for the rate of return on assets in the banking sector.

The total designated internal capital is secured by the value of available capital in consideration of appropriate safety buffers, in accordance with the assumed risk appetite.

#### **48.4 CRD IV/CRR package**

As at 31 December 2016, the Bank fully implemented the provisions of the CRR Regulation in respect of capital management, including own fund accounts and calculating capital requirements relating to particular risks.

#### **49. Registered audit company**

By a resolution dated 4 April 2014, the Supervisory Board elected PricewaterhouseCoopers Spółka z ograniczoną odpowiedzialnością with its registered office in Warsaw as the registered auditor to audit the financial statements. The contract for the review of the condensed interim financial statements and audit of the annual financial statements was signed on 6 June 2014. The contract was concluded for the period of performing the services related to the audit of the financial statements for 2014, 2015 and 2016.