Financial statements
of mBank Hipoteczny S.A.
according to International Financial Reporting Standards (IFRS)
for the year 2013

Selected financial data

The following selected financial data constitute supplementary information to the financial statements of mBank Hipoteczny S.A. for 2013.

Selected financial data		in PLN '000		in EUR '000	
		2013	2012 restated data	2013	2012 restated data
I.	Interest income	227,065	275,292	53,922	65,960
II.	Fee and commission income	5,277	5,432	1,253	1,302
III.	Net trading income	3,185	3,114	756	746
IV.	Profit before income tax	4,897	14,099	1,163	3,378
V.	Net profit attributable to the Company's equity shareholders	2,154	9,287	512	2,225
VI.	Net cash flows from operating activities	(64,914)	711,444	(15,415)	170,463
VII.	Net cash flows from investing activities	(6,154)	(3,262)	(1,461)	(782)
VIII.	Net cash flows from financing activities	118,072	(381,622)	28,039	(91,437)
IX.	Total net cash flows	47,004	326,560	11,162	78,244
X.	Total assets	4,782,443	4,809,712	1,153,174	1,176,486
XI.	Amounts due to other banks	1,203,488	1,172,467	290,193	286,793
XII.	Amounts due to customers	295,167	179,033	71,173	43,793
XIII.	Equity attributable to shareholders of the Company	501,963	500,705	121,037	122,476
XIV.	Share capital	275,000	275,000	66,310	67,267
XV.	Number of shares in '000	2,750	2,750	2,750	2,750
XVI.	Book value per share / Diluted book value per share (in PLN/EUR)	182.53	182.07	44.01	44.54
XVII.	Capital adequacy ratio (%)	14.92	11.97	14.92	11.97
XVIII.	Earnings per ordinary share / Diluted earnings per ordinary share (in PLN/EUR)	0.78	5.00	0.19	1.20

The following exchange rates were applied to calculate the selected financial data in EUR:

- for the items of the financial position statement — the NBP exchange rate as at 31 December 2013 — EUR 1 = PLN 4.1472 and the NBP exchange rate as at 31 December 2012 — EUR 1 = PLN 4.0882,
- for the items of the income statement and the cash flow statement — the rate calculated as the average NBP rate applicable as at the last day of each month in 2013 and 2012: EUR 1 = PLN 4.2110 and EUR 1 = PLN 4.1736, respectively.

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Income statement

		Year ended 31 December	
	Note	2013	2012 restated data
Interest income		227,065	275,292
Interest expense		(152,286)	(198,134)
Net interest income	7	**74,779**	**77,158**
Fee and commission income		5,277	5,432
Fee and commission expenses		(1,584)	(1,647)
Net fee and commission income	8	**3,693**	**3,785**
Net trading income, including:	9	3,185	3,114
Foreign exchange result		*4,186*	*2,278*
Other net trading income		*(1,001)*	*836*
Net income on investments in subsidiaries	23	63	-
Other operating income	10	7,297	674
Net impairment write-downs on loans and advances	11	(34,866)	(26,260)
Overhead costs	12	(39,189)	(36,867)
Amortisation and depreciation	24.25	(4,162)	(3,748)
Other operating expenses	13	(5,903)	(3,757)
Profit before income tax		**4,897**	**14,099**
Income tax expense	14	(2,743)	(4,812)
Net profit		**2,154**	**9,287**

Net profit		**2,154**	**9,287**
Weighted average number of ordinary shares / Diluted weighted average number of ordinary shares (in '000)	15	**2,750**	**1,857**
Earnings per ordinary share / Diluted earnings per ordinary share (in PLN)	15	**0.78**	**5.00**

Total profit of mBank Hipoteczny S.A. for 2013 and 2012 relates to the result of continued operations.

Explanatory notes presented on pages 9 to 85 constitute an integral part of these financial statements.

for the year 2013 (in PLN '000)

Statement of comprehensive income

		Year ended 31 December	
	Note	2013	2012
Net profit		**2,154**	**9,287**
Other comprehensive income net of tax		**(896)**	**2,232**
Items that may be reclassified to the income statement		**(931)**	**2,232**
Available-for-sale financial assets (gross)	16	(1,149)	2,755
Deferred tax on available-for-sale financial assets	16	218	(523)
Available-for-sale financial assets (net)	17	(931)	2,232
Items that will not be reclassified to the income statement		**35**	**-**
Actuarial gains and losses on post-employment benefits (gross)	16	43	-
Deferred tax on actuarial gains and losses on post-employment benefits	16	(8)	-
Actuarial gains and losses on post-employment benefits (net)	17	35	-
Total comprehensive income net of tax		**1,258**	**11,519**

Explanatory notes presented on pages 9 to 85 constitute an integral part of these financial statements.

for the year 2013 (in PLN '000)

Statement of financial position

ASSETS	Note	31.12.2013	31.12.2012
Cash and balances with the Central Bank	18	7,378	3,069
Amounts due from other banks	19	22,377	10,282
Derivative financial instruments	20	12,913	11,128
Loans and advances to customers	21	4,045,000	4,108,155
Investment securities available for sale	22	605,824	566,258
Investments in subsidiaries	23	-	65
Intangible assets	24	3,548	1,384
Tangible fixed assets	25	9,110	9,171
Deferred tax assets	32	13,058	9,960
Current income tax assets		620	-
Other assets, including:	26	62,615	90,240
- inventories	3.2.7	8,192	89,073
Total assets		**4,782,443**	**4,809,712**

LIABILITIES AND EQUITY	Note	31.12.2013	31.12.2012
Amounts due to other banks	27	1,203,488	1,172,467
Derivative financial instruments	20	278	461
Amounts due to customers	28	295,167	179,033
Debt securities in issue	29	2,661,407	2,852,445
Subordinated liabilities	30	100,268	100,316
Other liabilities and provisions	31	19,872	4,122
Current income tax liabilities		-	163
Total liabilities		**4,280,480**	**4,309,007**

Equity	Note	31.12.2013	31.12.2012
Equity		**501,963**	**500,705**
Share capital:	36	**275,000**	**275,000**
- Registered share capital		275,000	175,000
- Paid unregistered share capital		-	100,000
Retained earnings	37	**225,469**	**223,315**
- Profit for the previous year		223,315	214,028
- Profit for the current year		2,154	9,287
Other components of equity		**1,494**	**2,390**
Total equity		**501,963**	**500,705**
Total equity and liabilities		**4,782,443**	**4,809,712**

Explanatory notes presented on pages 9 to 85 constitute an integral part of these financial statements.

for the year 2013 (in PLN '000)

Statement of changes in equity

Changes in the period from 1 January 2013 to 31 December 2013

	Note	Share capital		Retained earnings				Other components of equity		Total
		Registered share capital	Paid unregistered share capital	Other Supplementary capital	General Risk Fund	Profit from the previous year	Profit for the current year	Valuation of available-for-sale financial assets	Actuarial gains and losses on post-employment benefits	
As at 1 January 2013		**175,000**	**100,000**	**186,800**	**27,000**	**9,515**	**-**	**2,390**	**-**	**500,705**
Net profit	37	-	-	-	-	-	2,154	-	-	2,154
Other comprehensive income (gross)	16	-	-	-	-	-	-	(1,149)	43	(1,106)
Deferred tax on other comprehensive income	16	-	-	-	-	-	-	218	(8)	210
Total comprehensive income	17	**-**	**-**	**-**	**-**	**-**	**2,154**	**(931)**	**35**	**1,258**
Transfer to General Risk Fund		-	-	-	4,000	(4,000)	-	-	-	-
Transfer to supplementary capital		-	-	5,515	-	(5,515)	-	-	-	-
Issue of shares		-	-	-	-	-	-	-	-	-
Transfer to registered share capital		100,000	(100,000)	-	-	-	-	-	-	-
As at 31 December 2013		**275,000**	**-**	**192,315**	**31,000**	**-**	**2,154**	**1,459**	**35**	**501,963**

Changes in the period from 1 January 2012 to 31 December 2012

	Note	Share capital		Retained earnings				Other components of equity	Total
		Registered share capital	Paid unregistered share capital	Other Supplementary capital	General Risk Fund	Profit from the previous year	Profit for the current year	Valuation of available-for-sale financial assets	
As at 1 January 2012		**175,000**	**-**	**170,150**	**23,000**	**20,878**	**-**	**158**	**389,186**
Net profit	37	-	-	-	-	-	9,287	-	9,287
Other comprehensive income (gross)	16	-	-	-	-	-	-	2,755	2,755
Deferred tax on other comprehensive income	16	-	-	-	-	-	-	(523)	(523)
Total comprehensive income	17	**-**	**-**	**-**	**-**	**-**	**9,287**	**2,232**	**11,519**
Transfer to General Risk Fund		-	-	-	4,000	(4,000)	-	-	-
Transfer to supplementary capital		-	-	16,650	-	(16,650)	-	-	-
Issue of shares		-	100,000	-	-	-	-	-	100,000
As at 31 December 2012		**175,000**	**100,000**	**186,800**	**27,000**	**228**	**9,287**	**2,390**	**500,705**

Explanatory notes presented on pages 9 to 85 constitute an integral part of these financial statements.

Financial Statements according to International Financial Reporting Standards (IFRS) for the year 2013 (in PLN '000)

Statement of cash flows

		Year ended 31 December	
	Note	2013	2012
A. Cash flows from operating activities		**(64,914)**	**711,444**
Profit before income tax		**4,897**	**14,099**
Adjustments:		***(69,811)***	***697,345***
Income tax paid (negative amount)		(6,414)	(7,013)
Amortisation	24, 25	4,162	3,748
Interest income	7	(227,065)	(275,292)
Interest expense	7	152,286	198,134
Interest received		236,059	264,210
Interest paid		(166,729)	(200,548)
Change in cash and balances with the Central Bank		-	-
Change in amounts due from other banks		-	1
Change in derivative financial instruments		(5,656)	(9,445)
Change in loans and advances to customers		58,041	50,805
Change in investment securities		(10,310)	62,019
Change in other assets		27,625	(69,783)
Change in amounts due to other banks		(260,440)	671,901
Change in amounts due to customers		116,091	3,783
Change in debt securities in issue		(3,210)	4,044
Change in subordinated liabilities		-	-
Change in other liabilities and provisions		15,793	691
Result on disposal of intangible assets and tangible fixed assets	13	19	90
Net income on investments in subsidiaries	23	(63)	-
Net cash from operating activities		**(64,914)**	**711,444**
B. Cash flows from investing activities		**(6,154)**	**(3,262)**
Cash inflows from investing activities		**798**	**90**
Disposal of intangible assets and tangible fixed assets		20	90
Disposal of shares	23	778	-
Cash outflows on investing activities		**6,952**	**3,352**
Purchase of intangible assets and tangible fixed assets	24, 25	6,302	3,352
Purchase of shares	23	650	-
Net cash from investing activities		**(6,154)**	**(3,262)**
C. Cash flows from financing activities		**118,072**	**(381,622)**
Cash inflows from financing activities		**1,198,014**	**1,756,034**
Loans and advances from banks		421,188	-
Issue of debt securities	29	776,826	1,556,034
Issue of shares		-	100,000
Subordinated loan	30	-	100,000
Cash outflows on financing activities		**1,079,942**	**2,137,656**
Repayment of loans and advances from banks		129,942	838,656
Redemption of debt securities in issue	29	950,000	1,199,000
Subordinated loan repayment	30	-	100,000
Net cash from financing activities		**118,072**	**(381,622)**
Net increase in cash and cash equivalents (A+B+C)		**47,004**	**326,560**
Cash and cash equivalents as at the beginning of the reporting period, including:		**498,179**	**171,619**
Cash and balances with the Central Bank		3,069	6,218
Amounts due from other banks		10,282	484
Investment securities with a maturity of up to 3 months from the date of purchase		484,828	164,917
Cash and cash equivalents as at the end of the reporting period, including:	**39**	**545,183**	**498,179**
Cash and balances with the Central Bank	18	7,378	3,069
Amounts due from other banks	19	22,377	10,282
Investment securities with a maturity of up to 3 months from the date of purchase		515,428	484,828

Explanatory notes presented on pages 9 to 85 constitute an integral part of these financial statements.

Notes to the statement of cash flows

Differences between the balance-sheet changes in items and changes in such items recognised under operating activities.

in PLN '000	Year ended 31 December	
	2013	2012 restated data
Amounts due from other banks, change resulting from balance-sheet values	(12,095)	(9,798)
Interest accrued and not yet received in the current year	-	1
Exclusion of change in cash and cash equivalents	12,095	9,798
Change in amounts due from other banks, in total	**-**	**1**
Derivative financial instruments, change resulting from balance-sheet values	(1,968)	(13,274)
Interest accrued and not received / not paid in the current year	3,587	7,273
Interest accrued in the previous year, and received / paid in the current year	(7,275)	(3,444)
Change in assets in respect of derivative financial instruments, in total	**(5,656)**	**(9,445)**
Loans and advances to customers, change resulting from balance-sheet values	63,155	42,158
Interest accrued and not yet received in the current year	17,713	25,207
Interest accrued in the previous year and received in the current year	(22,827)	(16,560)
Change in loans and advances to customers	**58,041**	**50,805**
Investment securities available for sale, change resulting from balance-sheet values	(39,566)	(259,510)
Interest accrued and not yet received in the current year	2,875	2,777
Interest accrued in the previous year and received in the current year	(3,070)	(3,914)
Exclusion of change in cash and cash equivalents	30,600	319,910
Valuation recognised in other comprehensive income	(1,149)	2,756
Change in investment securities, in total	**(10,310)**	**62,019**
Amounts due to other banks, change resulting from balance-sheet values	31,021	(168,874)
Interest accrued and not paid in the current year	(3,684)	(3,577)
Interest accrued in the previous year and paid in the current year	3,469	5,696
Exclusion of change in cash from financing activities	(291,246)	838,656
Change in amounts due to other banks, in total	**(260,440)**	**671,901**
Amounts due to customers, change resulting from balance-sheet values	116,134	803
Interest accrued and not paid in the current year	(186)	(144)
Interest accrued in the previous year and paid in the current year	143	3,124
Change in amounts due to customers, in total	**116,091**	**3,783**
Debt securities in issue, change resulting from balance-sheet values	(191,038)	364,005
Interest accrued and not paid in the current year	(21,462)	(34,312)
Interest accrued in the previous year and paid in the current year	36,116	31,385
Exclusion of change in cash from financing activities	173,174	(357,034)
Change in debt securities in issue, in total	**(3,210)**	**4,044**
Subordinated liabilities, change resulting from balance-sheet values	(48)	16
Interest accrued and not paid in the current year	(270)	(318)
Interest accrued in the previous year and paid in the current year	318	302
Change in subordinated liabilities, in total	**-**	**-**
Other liabilities and provisions, change resulting from balance-sheet values	15,750	691
Actuarial valuation of provisions for post-employment benefits recognised in other comprehensive income	43	-
Change in other liabilities and provisions, in total	**15,793**	**691**

Explanatory notes to the separate financial statements

1. Information on mBank Hipoteczny S.A.

In accordance with the decision of the District Court for the capital city of Warsaw, 16th Commercial Division, dated 16 April 1999, the Bank was entered in the Commercial Register, with the reference number 56623.

On 27 March 2001, the District Court in Warsaw decided to enter the Bank in the National Court Register, with the reference number KRS 0000003753.

According to the Polish Classification of Business Activities, the Bank's business comes under No 64.19.Z "Other forms of monetary intermediation".

On 29 November 2013, the District Court for the Capital City of Warsaw, 12th Commercial Division of the National Court Register, registered an amendment to the Bank's Memorandum of Association under Resolution No 1 of the Extraordinary General Shareholders' Meeting of BRE Bank Hipoteczny S.A. of 30 October 2013. In parallel to the registration of the amendment to the Memorandum of Association, the Bank's name was changed from BRE Bank Hipoteczny Spółka Akcyjna to mBank Hipoteczny Spółka Akcyjna. The Bank may use its abbreviated name: mBank Hipoteczny S.A.

The Bank's name was changed as part of the re-branding of BRE Bank Group which covered all entities within the Group. BRE Bank S.A. changed its name to mBank Spółka Akcyjna (abbreviated form: mBank S.A.).

In accordance with the Bank's Memorandum of Association, the Bank is engaged in providing banking services to individuals and legal entities, as well as organizational units without a legal personality, both in PLN and in foreign currencies.

The Bank operates within the territory of the Republic of Poland.

The Bank's registered office is located in Warsaw, at Al. Armii Ludowej 26.

The Bank's duration is not limited.

mBank Hipoteczny S.A. is a specialised mortgage bank, operating in the market for the financing of commercial properties and issuing of covered bonds.

The Bank's offer is addressed to business entities and institutional customers investing in purchasing, constructing or renovating commercial properties, such as offices, shopping centres, hotels, warehouses, as well as apartments and houses, carried out by housing developers. Another important operating area of the Bank is the crediting of local governments through the financing of investments such as the construction of the municipal buildings, maintenance and construction of roads, sewage treatment plants, educational establishments or other objects, as well as the refinancing of local governments' properties — the seats of local governments, utility and office premises. In 2013, the Bank extended the scope of its business to include retail loans. The Bank's credit offer is complemented with consulting services, addressed to investors and companies operating on the commercial property market. The Bank is also a leader in the issue of covered bonds, debt securities which refinance its credit activity.

Activities of mBank Hipoteczny S.A. are carried out in the operating segments described in detail in Note 6.

On average, the Bank had 144 employees in 2013 and 128 employees in 2012.

The financial statements were signed by the Management Board of mBank Hipoteczny S.A. on 3 March 2014.

2. Summary of significant accounting policies

The principal accounting policies applied in the preparation of these financial statements are set out below. Those principles were applied in all of the presented periods in a continuous way, unless stated otherwise.

2.1. Basis of preparation

The financial statements of mBank Hipoteczny S.A. have been prepared for the 12-month period ended 31 December 2013. These statements are standalone financial statements.

As at 31 December 2013, mBank Hipoteczny S.A. did not have any subsidiaries. On 28 November 2013, pursuant to a share purchase agreement, mBank Hipoteczny S.A. sold all the shares in the share capital of BDH Development Spółka z o.o. (former name: Bankowy Dom Hipoteczny Sp. z o.o.), in which the Bank held a 100% stake and 100% of the total number of votes at the general shareholders' meeting, to mBank S.A. (mBank Hipoteczny S.A. is a subsidiary of mBank S.A.).

The financial statements of mBank Hipoteczny S.A. have been prepared in accordance with the International Financial Reporting Standards ("IFRS") as adopted for use in the European Union, on the historical cost basis, taking into account the policies for measuring available-for-sale financial assets, financial assets and liabilities carried at fair value through profit or loss, including all derivative contracts.

The preparation of financial statements in accordance with IFRS requires the use of certain accounting estimates. It also requires the Management Board to present its own judgement in the process of applying the Bank's accounting policies. Areas involving a higher degree of judgement or complexity, or areas where assumptions and estimates are significant to the financial statements are disclosed in Note 5.

The financial statements were prepared under the going concern assumption. There are no circumstances indicating risks associated with the going concern in the foreseeable future.

2.2. Interest income and expenses

Income statement recognises all the interest earnings and costs regarding financial instruments measured at amortised/depreciated cost using the effective interest rate method.

The effective interest rate method is a method of calculating the amortised initial value of financial assets or liabilities and allocation of the interest income or expenses to the relevant period. The effective interest rate is a rate for which discounted future cash payments or proceeds are equal to the current net carrying amount of the given financial asset or liability. In the calculation of effective interest rate, the Bank assesses cash flows taking into account all the contractual provisions of a given financial instrument; however, it does not take into account the potential future losses related to the uncollectibility of loans. This calculation considers all payments executed or received between the parties to the agreement, which constitute an integral part of the effective interest rate, as well as costs of transaction and all other bonuses or discounts.

Interest income comprises interest and commissions received or receivable on loans, interbank deposits placed, bank accounts balances and investment securities recognised in the calculation of the effective interest rate.

Revenues and costs related to the interest element of the result on interest rate derivatives, as well as those resulting from the current calculation of swap points of foreign currency derivatives classified in the Bank book are recognised in the net interest result under the Revenues/interest costs on derivatives classified in the Bank book. The Bank is not engaged in trading; all derivative transactions are included in the banking book.

Interest expense include interest paid and accrued, as well as commissions settled through the effective interest rate in respect of deposits accepted from customers, interbank deposits, received credits, subordinated loans, the customers' bank account balances, as well as own issued debt securities.

Interest accrued on impaired receivables is recognised as interest income at the interest rate used for discounting future cash flows for the purpose of impairment measurement. Interest is recognised in the income statement in the recoverable amount, i.e. upon the recognition of adjustment to the impairment of exposure.

2.3. Fee and commission income and expense

Fee and commission income is generally recognised on an accrual basis, upon the service provision. Commission on granted loans is included in the effective interest rate calculations. Commissions on agreements regarding loans which have not been drawn down as at the date of collection or payment of the commissions adjust the effective interest rate as at the date of the funds being drawn down. Commission on credit agreements regarding loans which have not been drawn down is recognised in the income statement on a one-off basis, on the date of expiry of the said credit agreement. Commission on loan tranches placed at the customers' disposal (exposure commissions) is calculated by spreading it over the period of service provision. Commission is deferred over the period of the transaction to which the commission relates. Fee and commission income and costs which are not accounted for using the effective interest rate method are, in principle, recognised on an accrual basis at the time a given service is provided.

The commission costs relating to amounts paid on received loans and issued debt securities adjust the effective interest rate on the date of launching a loan or on the date of payment if it occurs later than the date of launching the loan, and are presented under interest income.

Commission costs relating to other transactions are charged to the income statement on a one-off basis.

2.4. Segment reporting

An operating segment is a component of the entity:

a) which engages in business activities and in connection with which revenues may be earned and costs incurred (including revenues and costs relating to transactions with other components of the same entity),
b) whose operating results are regularly reviewed by the chief operating decision maker in the entity and using those results to make decisions on resources allocated to a given segment and assessing the results of operations of the segment, and
c) in respect of which separate financial information is available.

2.5. Financial assets / Financial liabilities

2.5.1. Financial assets

The Bank classifies its financial assets into the following categories:

- loans and receivables,
- available-for-sale financial assets,
- financial assets at fair value through profit or loss,
- financial assets held to maturity.

The classification of investments is decided by the Management Board upon initial recognition.

Standardised purchase and sales transactions regarding financial assets carried at fair value through profit or loss, held to maturity and available for sale, are recognised and derecognised from the statement of financial position as at the date of settlement of the transaction. Loans are recognised when cash is advanced to the borrower. Financial assets are initially recognised at fair value plus transaction costs, except for financial assets carried at fair value through profit or loss. Financial assets are derecognised when the rights to receive cash flows from these assets have expired or been transferred, and the Bank has transferred substantially all risks and rewards of ownership.

Loans and receivables

Loans and receivables are non-derivative financial assets with fixed or determinable payments which are not quoted on the active market. They arise when the Bank advances cash, goods or services directly to the debtor, without the intention to introduce its receivable to trading.

Loans and receivables are stated at the adjusted purchase price (amortised/depreciated cost), using the effective interest rate.

Available-for-sale financial assets

Available-for-sale financial assets constitute investments which the Bank intends to hold for an indefinite period of time. They can be sold, for example, in order to improve the Bank's liquidity, in response to fluctuations of interest rates, exchange rates or equity prices.

Interest income/expense on available-for-sale financial assets is recognised in net interest income. Gain/(loss) on fair value valuation of available-for-sale financial assets is recognised in other comprehensive income.

Available-for-sale financial assets and financial assets measured at fair value through profit or loss are measured at fair value at the end of the reporting period. Loans and receivables and held-to-maturity investments are carried at amortised cost using the effective interest rate method.

Gains and losses arising from changes in the fair value of available-for-sale financial assets are recognised directly in other comprehensive income, until the financial asset is derecognised or impaired, at which time the total gains and losses previously recognised as other total income are recognised in the income statement. However, interest calculated using the effective interest method is recognised in the income statement. If, in a subsequent period, the fair value of a debt instrument classified as available for sale increases and the increase can be objectively related to an event occurring after the impairment loss was recognised in the income statement, the write-down is reversed, with the amount of the reversal recognised in the income statement.
Dividends on available-for-sale equity instruments are recognised in the income statement, once the entity's right to receive payment is established. Fair values of investments quoted on the active market are based on their current market values.

Financial assets at fair value through profit or loss

This category comprises financial assets held for trading.

The Bank classifies derivative instruments as financial assets valued at fair value through profit or loss. Rules for the valuation of derivative instruments are described in Note 2.9.

The measurement and the earning or losses on the sales of financial assets measured at fair value through profit or loss are recognised in net trading income.

Upon initial recognition, financial assets classified into this category are measured at fair value.

As at the end of the reporting period, financial assets measured at fair value through profit or loss are measured at fair value. Gains and losses arising from changes in the fair value of financial assets measured at fair value through profit or loss are demonstrated in the income statement, in the period in which they arose as net trading income. The Bank's investments in subsidiaries are demonstrated in the financial position statement according to the purchase price reduced by impairment write-downs.

Financial assets held to maturity

Investments held to maturity ("UDTZ") constitute financial assets not included among derivative instruments, with determined or determinable payments and determined maturity, which the Bank of the entity intends to hold and is capable of holding to maturity.

In the case of sales by the Bank, prior to maturity, of assets held to maturity, which cannot be recognised as insignificant, the so called "UDTZ portfolio Infection" occurs and thus all assets in this category are reclassified as available for sale.

In the reporting periods presented in these financial statements, the Bank had no assets held to maturity.

2.5.2. Financial liabilities

The Bank classifies its financial liabilities into the following categories:

- liabilities at fair value through profit or loss,
- other financial liabilities.

Financial liabilities measured at fair value through profit or loss shall be understood as:

- held-for-trading liabilities incurred to earn economic gains resulting from short-term price fluctuations and fluctuations in other market factors,
- other financial liabilities irrespective of intentions of the contract, if they constitute a component of a portfolio of similar financial liabilities which are very likely to earn the planned economic benefits in the short term,
- derivative financial instruments,
- liabilities measured at fair value through profit or loss at the Bank's option.

Apart from derivative financial instruments, the Bank did not classify any other financial liability as carried at fair value through profit or loss.

Other financial liabilities comprise specifically:

- bank accounts balances,
- customer deposits,
- subordinated borrowings received,
- loans and advances received,
- debt securities issued by the Bank (covered bonds and bonds),
- trade payables.

Other financial liabilities are stated at amortised cost using the effective interest rate method.

2.6. Offsetting financial instruments

Financial assets and liabilities are offset and reported in the statement of financial position as a net amount, when there is a legally enforceable right to offset the recognised amounts and the intention to settle them at the net amount, or realise a given asset and simultaneously settle the liability.

2.7. Impairment of financial assets

Assets carried at amortised cost

At the end of each reporting period, the Bank assesses whether there is objective evidence that a financial asset or a group of financial assets has been impaired. A financial asset or a group of financial assets has been impaired and impairment losses have been incurred only if there is objective evidence of impairment as a result of one or more events that occurred after the initial recognition of a given asset (a 'loss event') and when that loss event (or events) has had an impact on the future cash flows relating to that financial asset or group of financial assets that can be reliably estimated.

Rules for impairment measurement and calculation of impairment write-downs on loans and advances are presented in Note 3.2.3.

Uncollectible loans are written down to the related provisions for loan impairment. Such loans are written down after all the necessary procedures have been completed and the amount of loss has been determined.

Subsequent recoveries of amounts previously written down decrease the amount of impairment write-downs of loans in the income statement accordingly (in accordance with IAS 39). If, in a subsequent period, the amount of the impairment loss should decrease as a result of an event which occurred after the impairment was recognised (such as an improvement in the debtor's credit rating), the previously recognised impairment write-down is reversed by adjusting the impairment write-down account accordingly. The amount of reversal is disclosed in the income statement.

Receivables written-off but not remitted are recorded on off-balance sheet accounts. In the case of receivables written off without remitting, the Department responsible for such a receivable takes debt collection measures until the moment of full recovery or remission of the account receivable. Such activities may be discontinued if they are ineffective or not viable economically or if all the possibilities for recovery have been exhausted. Receivables written off are subject to derecognition from off-balance sheet accounts when:

- the account receivable has been recovered,
- the account receivable has been remitted.

Financial assets available for sale

At the end of each reporting period, the Bank assesses whether there is objective evidence that a financial asset or a group of financial assets has been impaired. In the case of instruments classified as available for sale, when assessing whether impairment took place, a significant or long-term decline in the fair value of the security below its purchase price is taken into account. If there is evidence of this type regarding financial assets that are available for sale, the total loss determined as the difference between the purchase price and the present fair value, less impairment of the given asset that was previously stated in the income statement is derecognised from equity and recognised in the income statement. Impairment of the equity instruments recognised in the profit and loss is not reversed through profit or loss, but through other comprehensive income. If, in a subsequent period, the fair value of a debt instrument classified as available for sale increases and this increase can be objectively related to an event occurring after the impairment recognition in the income statement, the impairment write-down is reversed in the income statement.

Renegotiated agreements

The Bank considers renegotiating the contractual terms and conditions for loans and advances as a premise of impairment, unless the renegotiation of the contractual terms was not enforced by the debtor's position, but was performed on normal business terms. Subsequently, the Bank assesses whether the impairment of such loans and advances should be recognised on an individual or group basis.

The general principle of the restructuring policy pursued by the Bank is to diagnose, as early as possible, the causes that give rise to the risk of default on the contractual terms of repayment of a loan and to determine whether such risks are attributable to the market or a given entrepreneur.

In the case of risks arising from market conditions, the Bank's policy provides for restructuring the loan towards the implementation of a "stay" strategy, which involves maintaining the relationship with the borrower and amending the terms of the loan in such a way, as to enable the entrepreneur to continue to operate and develop its business in the event of a favourable change in market conditions.

In the case of risks attributable to the entrepreneur, the Bank's policy is to restructure the loan towards the implementation of an "exit" strategy, in order to terminate the relationship with the borrower as soon as possible and, to the extent possible, without losses.

The most important factor taken into account in the restructuring of loans is the assumed period of repayment of the loan, but the Bank prefers restructuring to debt collection, unless restructuring fails to generate tangible results.

In the event of restructuring, the repayment terms of a loan, the Bank is flexible with regard to applicable margins, commissions and fees, provided that the full repayment of the loan is guaranteed.

Due to the nature of the loan product offered by the Bank (mortgage loan), in the case of impairment calculation, the Bank prefers to operate on the assumption of future cash receipts from the sale of assets on which the Bank has established mortgages within standard periods resulting from the liquidation of such assets, rather than to rely on proceeds from the borrower's own contributions or the realisation of other forms of collateral, unless such proceeds are almost certain.

2.8. Cash and cash equivalents

Cash and cash equivalents comprise items which mature within three months of the date of acquisition, including: unrestricted cash and balances in the Central Bank, Treasury bills and other eligible bills, loans and advances granted to other banks, amounts due from other banks and short-term State Treasury securities.

2.9. Derivative financial instruments

Derivative financial instruments are stated at fair value starting from the transaction date. Fair value is determined on the basis of the instruments' quotations on active markets, including on the basis of prices applied in recent transactions, and on the basis of valuation techniques, including models based on discounted cash flows and option valuation models, depending on which of the methods is appropriate in given circumstances. All derivative instruments with positive fair value are shown as assets in the statement of financial position, and those with a negative fair value are shown as liabilities. The fair value of derivative instruments consists of an increase or decrease in value, as well as the accrued interest stream. Accrued interest on derivatives is recognised after compensation.

The transaction price (i.e. the fair value of consideration paid or received) is the best indicator of a derivative's fair value on initial recognition, unless the instrument's fair value can be determined by comparison with other current market transactions relating to the same instrument (not modified) or on the basis of valuation techniques based solely on observable market data. If such a price is known, the Bank shows gains or losses on the first day.

The method for recognition of changes in the fair value is dependent on whether a given derivative instrument is designated as a hedging instrument, as well as the type of the hedged item. Changes in the fair value of derivative instruments which do not meet the criteria for applying hedge accounting policies are recognised in the income statement for the current period. The Bank does not apply hedge accounting. The Bank uses derivative instruments only as hedging transactions.

<u>Rules for calculating write-downs (valuation adjustments) due to counterparty risk on the valuation of market-risk derivatives</u>

Credit risk write-downs (valuation adjustments) for derivatives are created for clients in the financial sector who have not been classified into the *default* or *technical default* category, the latter signifying default resulting from a breach of contractual provisions (e.g. failure to cover the costs arising from the transaction, despite the principal amount being settled in a timely manner). The amount of the write-down is the sum of the credit losses on individual transactions entered into with a given counterparty due to the counterparty's default, which are expected to arise before the maturity dates of individual derivatives. The expected loss due to counterparty risk is calculated as the product of the expected exposure at the time of default, the cumulative probability of default for exposures arising from transactions concluded during the period up until their effective maturity and the estimated loss on the occurrence of default.

The cumulative probability of default (CPD) is expertly estimated for the individual counterparties of the Bank, broken down by individual tenors associated with the effective maturity of a given transaction. CPD values are determined on an annual basis between the available tenors of the CPD curve for individual counterparties, using binomial distribution. It is assumed for such annual periods that the probabilities of default in each of the annual periods are constant and independent of each other. If the duration of a contract corresponds to non-standard periods within a given annual period, linear interpolation between the cumulative PD for neighbouring tenors is applied. For the purposes of calculation of CPD for a given contractor, calculations are carried out for a period corresponding to the average residual period to maturity of a given transaction, weighted by a mark-to-market (MTM) valuation, in the context of a particular counterparty.

The LGD parameter is expertly estimated at the level of 37.5% for all counterparties. As at the reporting date, the Bank had no collateral in respect of changes in the valuation of contracts with individual counterparties.

<u>The Bank has the following derivative instruments in its portfolio:</u>

Interest rate risk instruments:

- IRS (Interest Rate Swap) contracts.

Currency risk instruments (which constitute future commitments to purchase foreign or domestic currencies):

- FX contracts,
- FX SWAP contracts.

2.10. Gains and losses on initial recognition

The best evidence of fair value of a financial instrument at initial recognition is the transaction price (i.e. the fair value of the payment executed or received), unless the fair value of that instrument is evidenced by comparison with other observable current market transactions in the same instrument (without modification) or based on a valuation technique whose variables include only data from observable markets.

2.11. Intangible assets

Intangible assets are stated according to purchase prices adjusted for the costs of improvements (rebuilding, extension, reconstruction, adaptation or modernization) and accumulated amortisation and impairment write-downs. Accumulated amortisation is calculated on the straight line basis, taking account of the economic useful lives of the intangible assets. If the expected economic useful life of a given intangible asset is different from that specified below, the period of accumulated amortisation of a given asset may be determined taking that difference into account. Expenditures on intangible assets are recognised as costs upon being incurred unless they form part of the cost of purchase or the cost of manufacture of an intangible asset which meets the recognition criteria.

<u>Computer software</u>

Purchased licenses for computer software are capitalised in the amount of costs incurred for purchasing and preparing specific software for use. The capitalised costs are written down over the expected economic useful life of the software (2–10 years). Expenditures related to developing or maintaining computer software are recognised as costs upon being incurred. Costs directly associated with the manufacture of identifiable and unique computer software by the Bank, which will probably generate economic benefits exceeding these costs and that will be earned for more than one year, are recognised as intangible assets.

Capitalised software development costs are amortised/depreciated over the expected economic useful lives.

<u>Costs of completed development projects</u>

The Bank identifies the costs of development projects as intangible assets in connection with obtaining future economic benefits and meeting the conditions specified in IAS 38, i.e. the Bank is able to and intends to complete and use the asset being generated, it has appropriate technical and financial resources for completing the project and using the asset being generated, and it may reliably determine the amount of the expenditure incurred during the development projects which may be attributed to the intangible asset generated.

The economic useful life of "Costs of completed development projects" is determined and does not exceed 5 years. Amortisation rates are tailored to the economic useful lives.

Expenditure on development projects comprises all expenditure which may be directly attributed to development activities.

Intangible assets are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount may be irrecoverable as well as at the end of each reporting period.

<u>Significant intangible assets as at 31 December 2013:</u>

- Def3000/CL System with a net value of PLN 396 thousand,
- vPlex license with a net value of PLN 208 thousand.

2.12. Tangible fixed assets

The carrying amount is the value at which a given asset is recognised in the statement of financial position, net of accumulated depreciation and accumulated impairment write-downs.

The cost of purchase or manufacture of tangible fixed assets is the amount of cash or cash equivalents paid or the fair value of other goods transferred upon the purchase of an asset at the time of purchase or manufacture. The cost of purchase or manufacture also includes all directly attributable costs incurred in order to adapt an asset to the location and conditions necessary for its operation, including the disassembly, scrapping and renovation costs which the Bank is obliged to incur. The cost of purchase or manufacture also includes the expenditure incurred at a later date in order to make the asset more useful, replace its parts or renovate it.

The depreciable value is the cost of purchase or manufacture of a given asset or its fair value determined otherwise, net of its residual value.

Depreciation is a systematic subtraction of the depreciable amount over the period of economic useful life of an asset. An impairment write-down is the excess of the carrying amount of a given asset over its recoverable amount.

The recoverable amount is the higher of the net realisable value of the asset and its value in use.

The residual value of an asset is the amount which the entity might expect to obtain for the asset at present, taking into account its age and condition as at the end of its economic useful life, net of estimated sales costs.

While determining the depreciation period and an annual depreciation rate, the economic useful life of a given fixed asset is taken into account. The depreciation periods and rates are reviewed periodically — no later than as at the beginning of each financial year.

The Bank depreciates its fixed assets on a straight line basis, by systematically subtracting the initial value or the revalued amount net of the residual value over the estimated useful life of the asset. The residual value and the useful life of an asset are reviewed as at the end of each financial year, and if the expectations differ from the earlier estimates, the difference is recognised as a change in estimates.

Useful life of an asset is the period in which it is expected to be used.

<u>Useful lives of the individual groups of fixed assets are as follows:</u>

- Technical equipment and machinery	5–10 years
- IT equipment	3 years
- Equipment and vehicles	5–10 years
- Office equipment and furniture	5–7 years

If the expected economic useful life of tangible fixed assets is different from that specified above, the depreciation period for a given asset may be determined taking that difference into account.

Depreciable fixed assets are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount may be irrecoverable and at the end of each reporting period. The carrying amount of a fixed asset is reduced to the level of its recoverable value if the carrying amount exceeds the estimated recoverable value. The recoverable amount is the higher of the two amounts: fair value of a fixed asset reduced by costs of its sales and the utility value.

The carrying amount of a component of tangible fixed assets is derecognised when the said asset is sold or if no further economic benefits are expected from the use or disposal of the asset.

The Bank does not increase the carrying amount of its tangible fixed assets by the costs of their current maintenance. Repair and maintenance costs are recognised in the income statement upon being incurred.

If a component part of tangible fixed assets is replaced, the Bank includes the cost of replacing the said part in the carrying amount of the asset upon the cost being incurred. The carrying amount of the replaced components is written down in accordance with the derecognition policies.

After the initial recognition of tangible fixed assets as a component of assets, the Bank reports them at the cost of purchase or manufacture, net of accumulated depreciation and accumulated impairment write-downs.

Gains and losses on the derecognition of tangible fixed assets are the difference between net proceeds from disposal and the carrying amount of a given asset and are recognised in the income statement in the period in which the item was derecognised.

2.13. Deferred income tax

Tax base differs from the profit/loss before tax recorded in the Bank's accounting records due to the difference in recognition of income as earned and costs as incurred in accordance with the balance sheet law and tax regulations.

The deferred income tax provision and assets are calculated using the tax rates and regulations in force as at the end of the reporting period, which are expected to apply when the deferred tax assets are realised or the tax liability is paid. Temporary differences are differences between the carrying value of a given asset or liability and its tax base.

A deferred income tax liability is recognised in respect of temporary differences, in the full amount, in accordance with the liability method.

The carrying amount of the deferred tax asset is reviewed at each balance sheet date and reduced to the extent that it is no longer probable that a sufficient taxable income will be generated to realise the deferred tax asset in part or in full. An unrecognised deferred income tax asset is reassessed at each balance sheet date and is recognised to the extent of the likelihood of achieving future taxable income that will allow the asset to be recovered.

Deferred tax assets and provisions are presented on a net basis in the Bank's statement of financial position, if the Bank has a legally enforceable right to account for them simultaneously when calculating the tax liability.

Deferred income tax relating to the fair value measurement of available-for-sale investments is recognised in the same way as the effect of fair value measurement, directly in other comprehensive income.

To determine foreign exchange rate differences, the Bank applies tax method.

2.14. Inventories

The Bank classifies non-financial assets taken over for debts as inventories. Assets taken over for debts are measured at the moment of initial recognition at the amount corresponding to their fair value, and then they are measured at the lower one of the two values: purchase/cost and net realisable value. Net realisable value is the estimated selling price in the ordinary course of business activity, less the applicable variable selling costs. The amount of any inventory write-downs to the net realisable value and any inventory losses are recorded as costs of the period in which a write-down or a loss occurred. Reversals of inventory write-downs resulting from increases in their net realisable value are recorded as a reduction in the amount of costs of inventories recognised as costs of the period in which the reversals took place.

2.15. Prepayments, accruals and deferred income

The Bank recognises prepayments if the expenses relate to future reporting periods. Prepayments are recognised in "Other assets" in the statement of financial position.

Accruals constitute liabilities payable for goods or services that have been received or supplied but have not been paid, invoiced or formally agreed with the supplier, including amounts due to employees. Deferred income comprises, amongst other things, income received but not yet earned. Accruals and deferred income are presented in "Other liabilities and provisions" in the statement of financial position.

2.16. Provisions

Pursuant to IAS 37, provisions are created when the Bank has an existing liability (legal or customarily expected) arising from past events, and when it is probable that the fulfilment of this liability will result in the necessity of an outflow of cash, and when the amount of the liability may be reliably estimated.

2.17. Pension benefits and other employee benefits

Pension benefits

The Bank creates provisions for future liabilities in respect of retirement, disability and post-mortem benefits, determined on the basis of estimations of such liabilities, using an actuarial model. Current service cost and net interest are recognised in profit or loss, while actuarial gains and losses are recognised in other comprehensive income.

Phantom share-based benefits

The Bank runs a remuneration program for the Management Board and employees having a significant impact on the risk profile of the Bank based on phantom shares settled in cash. These benefits are accounted for in accordance with IAS 19 "Employee Benefits". Measurement value of phantom shares increases costs incurred in a given period in correspondence with the commitments. Phantom shares are granted in quantity based on the valuation of these shares for the appraisal period. The phantom share valuation is calculated each time at the end of the reporting period as the Bank book value divided by the number of ordinary shares. The payout under phantom shares depends on the valuation of these shares in a given reporting period in which they are redeemed, adjusted with the capital increase above the par value during the entire appraisal period.

1) 50% of the bonus for a given period shall be granted in the non-cash form in phantom shares;
2) 20% of the portion referred to in item 1 is granted in a year following the appraisal period for which the bonus is granted, within 30 calendar days of approval by the General Meeting of Shareholders of the financial statements of mBank Hipoteczny S.A.;
3) and 80% of the portion referred to in item 1 is realised in three equal annual tranches ("Deferred tranches").

Eligible employees of the Bank are entitled to deferred tranches, provided that:

1) they received a positive assessment of their work from the Supervisory Board;
2) they fulfilled the conditions of employment at mBank Hipoteczny S.A.; and
3) the Bank's performance as at the end of the first, second and third calendar year after the end of the appraisal period is not lower than the result adopted for a given year in the financial plan lessen by 10%.

Each of the deferred tranches shall be granted within 30 calendar days upon the approval by the General Meeting of Shareholders of the financial statements for a given year.

The Supervisory Board may modify the level of the planned Bank performance in respect of the market situation.

2.18. Issuance of securities

The Bank's liabilities arising from the issue of securities (covered bonds and bonds) upon initial recognition are measured at fair value, including transaction costs that are directly attributable to the issue, and subsequently, throughout the duration of a given transaction, they are measured at the amortised cost using the effective interest rate.

2.19. Loans and advances received and deposits accepted

Loans and advances received and deposits accepted are initially recognised at fair value, less the incurred transaction costs. Upon initial recognition, loans and advances received and deposits accepted are stated at adjusted purchase price, using the effective interest rate. All differences between the amount received (less transaction costs) and the redemption value are recognised in the income statement over the period of validity of the relevant agreements, using the effective interest rate method.

2.20. Equity

The Bank's equity comprises capitals and reserves set up by the Bank in accordance with the Memorandum of Association and the Banking Law.

Registered share capital

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

Paid unregistered share capital

Paid-up capital not entered into the court register, but formally submitted for registration.

Retained earnings

Retained earnings include:

- other supplementary capital created from profit appropriation,
- General Risk Fund created through the profit appropriation and intended for the purposes specified in the Bank's Memorandum of Association or in other legal regulations;
- retained profit from the previous year,
- net profit/loss for the current year.

Other components of equity

Other components of equity comprise the result of the revaluation of financial instruments classified as "available for sale" and the actuarial valuation of post-employment benefits.

2.21. Leases

The Bank acts as a lessee. Lease agreements concluded by the Bank constitute operating lease agreements. All the lease payments made under operating lease agreements are charged to costs on a straight line basis over the lease period. The Bank has no financial leases.

2.22. Measurement of foreign currency items

Functional currency and presentational currency

The financial statements are presented in thousands of PLN, which is the Bank's functional and presentational currency.

Transactions and balances

Transactions denominated in foreign currencies are translated into the functional currency at the NBP mid exchange rate in force as at the end of reporting period. Foreign exchange gains and losses on the settlement of these transactions and the valuation of monetary assets and liabilities denominated in foreign currencies as at the end of reporting period are recognised in the income statement.

2.23. New standards, interpretations and amendments to the published standards

These financial statements include all the requirements of the European Union, approved by the International Accounting Standards, International Financial Reporting Standards and the related interpretations, except for the following standards and interpretations, which are awaiting approval by the European Union or have been approved by the European Union and will take effect only after the balance sheet date.

The Bank did not use the possibility of earlier adoption of standards.

Published standards and interpretations that have been issued and are applicable in the Bank for the annual periods beginning on 1 January 2013:

- IFRS 10, Consolidated Financial Statements (replaces the consolidation requirements of IAS 27), binding for annual periods beginning on or after 1 January 2013.
- IFRS 11, Joint Arrangements, binding for annual periods beginning on or after 1 January 2013.
- IFRS 12, Disclosure of Interests in Other Entities, binding for annual periods beginning on or after 1 January 2013.
- IFRS 13, Fair Value Measurement, binding for annual periods beginning on or after 1 January 2013.
- IAS 19 (Amended), Employee Benefits, binding for annual periods beginning on or after 1 January 2013.
- IAS 27, Separate Financial Statements (together with IFRS 10 replaces IAS 27 Consolidated Financial Statements), binding for annual periods beginning on or after 1 January 2013.
- IAS 28, Investments in Associates and Joint Ventures (replacing IAS 28, Investments in Associates), binding for annual periods beginning on or after 1 January 2013.
- Amendments to IAS 1, Presentation of Items of Other Comprehensive Income, binding for annual periods beginning on or after 1 July 2012.
- Amendments to IFRS 7, Disclosures — Offsetting Financial Assets and Financial Liabilities, binding for annual periods beginning on or after 1 January 2013.
- Amendments to IFRS 10, IFRS 11 and IFRS 12, i.e. Consolidated Financial Statements, Joint Arrangements and Disclosure of Interests in Other Entities: Guidance for the application, binding for annual periods beginning on or after 1 January 2013.
- Amendments to IFRS 2009–2011, the majority of which are binding for annual periods beginning on or after 1 January 2013.
- Government Loans (amendments to IFRS 1), binding for annual periods beginning on or after 1 January 2013.

The Bank believes that the application of the said standards and interpretations did not have a significant impact on the financial statements in the period of their initial application. The Bank does not hold any shares in other companies. The Bank has no control over any company which is a borrower of the Bank.

Published Standards and Interpretations which have been issued but are not yet binding or have not been adopted earlier

Standards and Interpretations approved by the European Union:

- Amendments to IAS 32, Offsetting Financial Assets and Financial Liabilities, binding for annual periods beginning on or after 1 January 2014.
- Amendments to IAS 36, Recoverable Amount Disclosures for Non-Financial Assets, binding for annual periods beginning on or after 1 January 2014.
- Amendments to IAS 39, Novation of Derivatives and Continuation of Hedge Accounting, binding for annual periods beginning on or after 1 January 2014.
- Amendments to IFRS 10, IFRS 12 and IAS 27, Investment Entities, binding for annual periods beginning on or after 1 January 2014.

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

Standards and interpretations not yet approved by the European Union:

- IFRS 9, Financial Instruments, Phase 1: Classification and Measurement, binding for annual periods beginning on or after 1 January 2015.
- IFRS 14, Regulatory Deferral Accounts, binding for annual periods beginning on or after 1 January 2016.
- IAS 19 (Amended), Defined Benefit Plans: Employee Contributions, binding for annual periods beginning on or after 1 July 2014.
- IFRIC 21, Fees, binding for annual periods beginning on or after 1 January 2014.
- Amendments to IAS 36, Recoverable Amount Disclosures for Non-Financial Assets, binding for annual periods beginning on or after 1 January 2014.
- Amendments to IFRS 2010–2012 were published by the International Accounting Standards Committee on 12 December 2013, and the majority of them are binding for annual periods beginning on or after 1 July 2014.
- Amendments to IFRS 2011–2013 were published by the International Accounting Standards Committee on 16 December 2013, and are mostly binding for annual periods beginning on or after 1 July 2014.

The Bank considers the impact and the point at which the IFRS 9 standard will apply. The Bank believes that the application of the remaining standards and interpretations will not have a significant impact on the financial statements in the period of their initial application.

2.24. Comparative data

Comparative data has been converted taking into account presentational changes introduced in the current financial year.

As at the beginning of 2013, changes occurred in the presentation of FX swaps result, and in the IRS transactions result. Pursuant to the provisions of IFRS 7 Appendix B item 5(e), the Bank decomposed the result on derivatives classified in the Bank book, and distinguished the interest component resulting from the current estimation of swap points and interest on IRS transactions.

After these changes, the component of valuation of derivatives classified in the Bank book, resulting from the current estimation of the interest component, including swap points, is presented in the income result as the Interest income/expense.

In the Bank's opinion, the above presentation of the interest component of the valuation of result on derivatives classified in the Bank book better reflects the economic nature of transactions concluded solely in order to manage the Bank's liquidity as well as to mitigate the foreign exchange risk and the interest rate risk.

In addition, in the current reporting period, the Bank changed the presentation of receipts from the reimbursement by customers of the annual contribution to the Bank Guarantee Fund. In the current period, the Bank has presented them under "Fee and commission income". In previous periods, such receipts were recognised as part of interest income. Expenses due to the annual contribution to the Bank Guarantee Fund are presented under "Fee and commission expense" — their presentation has not changed.

for the year 2013 (in PLN '000)

In the current reporting period, the Bank ceased to demonstrate collateralised assets in a separate item of the statement of financial position. Debt securities with collaterals are presented in the statement of financial position in accordance with their classification prior to establishing the collateral in "Available-for-sale investment securities".

Information on debt securities with collaterals is available in Note 22.

Transformation of the comparative data had no impact on the result and the amount of capital in the presented comparative data as at 31 December 2012.

Other data prepared as at 31 December 2012 is fully comparable with data from the current reporting period and, therefore, did not require transformations.

The impact of transformations on the comparative figures presented in the financial statements is demonstrated below.

Transformations in the Bank's statement of financial position as at 31 December 2012

	Period from 01.01.2012 to 31.12.2012 before transformation	presentational adjustments	Period from 01.01.2012 to 31.12.2012 after transformation
Investment securities available for sale	564,960	1,298	566,258
Pledged assets	1,298	(1,298)	-

Transformations in the income statement for the period from 1 January 2012 to 31 December 2012

	Period from 01.01.2012 to 31.12.2012 before transformation	presentational adjustments	Period from 01.01.2012 to 31.12.2012 after transformation
Interest income	245,624	29,668	275,292
Other net trading income	33,910	(33,074)	836
Fee and commission income	2,026	3,406	5,432

3. Financial risk management

3.1. Strategy for the use of financial instruments

In its operations, the Bank uses financial instruments, including derivatives. The Bank accepts deposits from customers and issues covered bonds and bonds. The Bank's liabilities bear both fixed and floating interest rates. The Bank invests the funds it raises in assets with an acceptable risk level in order to increase its interest margin. In order to hedge the currency risk and the interest rate risk, the Bank concludes transactions in derivatives.

In concluding the above transactions, the Bank maintains its liquidity at a level sufficient for settling all the arising liabilities.

The Bank does not apply hedge accounting.

<u>Derivative instruments</u>

The Bank exercises strict control over net open derivative positions, i.e. the difference between purchase and sale contracts, both in terms of nominal contractual amounts and the period of validity. At any given time, the amount exposed to the credit risk is limited to the current fair value of the instruments whose valuation is positive (i.e. assets), which, with regard to derivatives, constitutes only a small fraction of the value of an agreement or the nominal values used for expressing the volume of the existing instruments.

Off-balance sheet credit liabilities

Off-balance sheet credit liabilities relate to the unused portion of granted loans. The Bank reserves the right not to advance the unused portion of a loan in the event of a customer's credit-worthiness deteriorating, therefore, the likely amount of the related loss is much lower than the total amount of unused loan liabilities.
The Bank has organizational solutions in place which ensure formal and actual separation of the credit risk assessment processes from the credit decision-making process. Credit decisions are made jointly, in accordance with decision-making responsibilities, after taking into account the recommendation put forward by the director of the department responsible for credit risk assessment.

3.2. Credit risk

The Bank is exposed to credit risk which is the risk of a counterparty failing to meet its liabilities towards the Bank in full, within the agreed deadline. In order to limit credit risk, the Bank conducts its lending activities in accordance with its internal procedures, as well as policies on making loan decisions and assessing credit risk.

3.2.1. Collateral

The Bank's policies on securing loans and valuating credit collateral are governed by the provisions of the following Acts: on covered bonds and mortgage banks, on banking law, on the registered pledge and the register of pledges, on land and mortgage registers and mortgages, provisions of the Code of Commercial Companies, provisions of the Civil Code and other acts. In addition, collateral-related issues are governed by the Recommendations of the Banking Supervision Commission — currently the Polish Financial Supervision Authority, including Recommendation S and J, and the provisions of internal banking regulations.
The Bank has and applies Rules for determining the bank and mortgage value of real estate, approved by the Banking Supervision Commission — currently the Polish Financial Supervision Authority, and issued based on the Act of 29 August 1997 consolidated text Journal of Laws of 2003, No 99, item 919 with amendments), taking into consideration the provisions of Recommendation F relating to the basic criteria used by the Banking Supervision Commission for approving the rules on determining the bank mortgage value of properties issued by mortgage banks. Thus, the Bank ensures that the value of collateral for a credit exposure backed with a mortgage is sufficient throughout the term of an agreement. This assurance is based on the analysis of return on a given property in the long term, ended in the determination of the amount of capitalised net inflows which may be earned on a given property in the long term.

The Bank may perform or commission a revaluation of collateral, including of a property which constitutes collateral for a mortgage loan if, in the period since the last valuation, events have taken place which might have a significant impact on the value of given collateral or in the case of real estate which constitutes collateral for impaired loans.

The Bank accepts the following as collateral for loans payments on a mandatory, legally required basis:

- a mortgage on a financed property, entered in the land register in the first place — for refinancing the commercial properties, financing the commercial real estate developers, financing the housing real estate developers, financing land purchase and loans for individual customers,
- the transfer of rights from an insurance contract certified by a fire and other accident insurance policy on the real estate to be credited, issued by an insurance company approved by the Bank or the transfer of rights from an insurance contract certified by a comprehensive construction risk insurance policy on the construction project, issued by an insurance company approved by the Bank (respectively for refinancing a finished property and financing real estate projects in progress) — for refinancing the commercial properties, financing the commercial real estate developers, financing the housing real estate developers and loans for individual customers,
- the transfer of rights or pledge on receivables under lease contracts — for refinancing commercial properties, financing commercial real estate developers,

- blank signed promissory note with the borrower's promissory note declaration — for loans granted to local government units,
- a guarantee or warranty from local authorities (pursuant to the Civil Law) — for the financing of health care centres (ZOZ) or SPVs established by local government units.

The dominant organisational form of the Bank's borrowers is the so-called special purpose vehicles (SPV). To the best of the Bank's knowledge, Members of the Management Board and employees of the Bank do not perform any functions in the corporate bodies of the companies that are the Bank's borrowers.

If the said companies are commercial companies, i.e. limited liability companies and joint stock companies, the Bank accepts a registered pledge on their shares as collateral for loan repayment. Consequently, there is also a significant concentration of registered pledges on shares as collateral for the repayment of loans. In the case of financing limited partnerships or limited joint stock partnerships, the Bank accepts a pledge on shares of the general partner — the entity authorized to run the affairs of a limited partnership or a limited joint stock partnership — as collateral for loan repayment.

Irrespective of the types of collateral referred to above, the Bank may accept additional legal forms of collateral for loans, in particular:

a) a bank guarantee,
b) a warranty under the Civil Law or the Bill-of-exchange Law,
c) a registered pledge on rights or receivables,
d) a pledge under the provisions of the Civil Code on rights or receivables,
e) a transfer of receivables other than those referred to above,
f) blocking of funds in a bank account,
g) an authorisation to use a bank account,
h) credit debt accession,
i) credit insurance,
j) the debtor's statement of submission to enforcement proceedings,
k) a security deposit,
l) liabilities of the borrower's shareholders,
m) other forms of collateral permitted by law.

The Bank determines the form and value of collateral, taking into consideration:

a) the type and amount of loan and the crediting period,
b) the legal status of the borrower,
c) the financial position of the borrower,
d) the history of cooperation with the borrower and the capital group of which the borrower is a member,
e) costs of collateral provision,
f) the ability to satisfy the Bank's claims against the accepted collateral in the shortest possible time.

As regards bank guarantees and the assignment of rights from insurance policies, the Bank selects its counterparties taking into consideration the results of operations and the rating of the providers of the collateral. It only accepts collateral from reliable banks and insurance companies.

The Bank does not use any derivative credit instruments.

3.2.2. Description of the rating system and the credit risk management system

The Bank uses a rating system to analyse the quality of the loan portfolio, which is updated on an annual basis. The system currently covers more than 84% of the sum total of risk weighted exposures. The Bank uses the rating-based assessment in the case of financing the construction/purchase/refinancing of office, services and commercial buildings, shopping, services and entertainment areas, warehouses, estates of single-family or multi-family buildings designated for rental or for sale, hotels and commercial premises designated for commercial activities, offices or warehouses.

On 14 August 2012, Bundesanstalt für Finanzdienstleistungsaufsicht (BaFin) in cooperation with the Polish Financial Supervision Authority (letter of 27 August 2012) gave its consent for the Bank to apply the internal ratings method with the application of the supervisory approach in terms of assigning specialised lending exposures to risk categories (IRB slotting approach) in the calculation of the capital requirement due to credit risk. All the conditions set out by the Polish Financial Supervision Authority were assigned low significance. Based on the aforementioned agreement, the Bank uses internal ratings for the measurement of credit risk, in accordance with Appendix 5 to Resolution No 76/2010 of the Polish Financial Supervision Authority dated 10 March 2010. Capital requirement for credit risk calculated using the IRB approach is presented in Note 42.

In line with the approved plan for gradual implementation, on 4 April 2013 the Bank submitted an application to the PFSA for extension of approval for the use by mBank Hipoteczny S.A. of the IRB approach to include credit exposures covered by models for the financing and refinancing of hotels as well as the refinancing commercial premises.

On 12 December 2013, the Bank notified the PFSA about the extension of the gradual implementation of the IRB approach at mBank Hipoteczny S.A. to include the class of retail exposures secured on residential properties.

In order to assess the credibility of customers requesting retail mortgage loan products and to monitor/report credit risk in this portfolio, the Bank uses group-wide credit risk models, of which the Bank is a local user. Detailed rules and the scope of cooperation between Banks in terms of group-wide risk models are set out in a separate agreement on cooperation in the area of risk management. The capital requirement for credit risk in this portion of the portfolio is calculated using the standard method, as it is covered by the gradual implementation plan as at 31 December 2013.

In the area of retail banking the following models function within the rating system:

- The Loss Given Default (LGD) model. Under this model, loss has been defined as a function dependent on the level of recovery from the customer's repayments and the possible value of property collateral realised as part of the execution process.
- The Credit Conversion Factor (CCF) model. This factor is an integral part of the EAD model (CCF as the extent to which the customer has met off-balance sheet liabilities as at the date of occurrence of default).
- The Probability of Default (PD) model, which in a module-based model integrating the application models, behavioural models and models based on external data from the Credit Information Bureau (BIK) that function in the area of retail banking.

The ratings assigned by external rating agencies have very limited significance to the assessment of the Bank's credit risk due to special purpose companies being the dominating organizational form of borrowers.

The quality of the Bank's loan portfolio is assessed on the basis of monitoring the timeliness of repayments and monitoring the financial position of the borrower. The Bank has three separate portfolios: a retail portfolio (loans to individuals), a commercial portfolio (loans to sole traders, development loans, commercial loans, and loans to legal entities), and a public sector portfolio (loans to local authorities and loans guaranteed by local authorities). Loans to individuals are monitored for the timeliness of repayment on a monthly basis. The commercial and the public sector portfolios are monitored on a monthly basis for timely repayment, while the economic and financial situation is monitored on a quarterly or semi-annual basis, depending on the risk assessment of transactions measured by the score obtained in the rating model.

As disclosed in Note 3.2.5., non-overdue, unimpaired loans account for 86.60% of the gross amount of loans and advances to customers. The remaining 13.40% of the amount of the loan portfolio represents overdue, unimpaired loans (8.09%) as well as impaired loans (5.31%).

3.2.3. Impairment measurement

Portfolio of commercial loans, loans to local government units (JST) and retail loans granted up until 2004

The Bank measures the impairment of credit exposures in accordance with the International Accounting Standard No 39. The process of identification of impaired customers and the calculation of impairment write-downs is as follows:

a) determining, on a case-by-case basis, the evidence for impairment arising and, when it does arise, classifying the customer as part of the "default" category,
b) determining the estimated future cash flows (repayments) both from the collateral and repayments made by borrowers,
c) calculation of impairment taking into account the future value of estimated recoveries discounted using the effective interest rate,
d) impairment write-down accounting records.

The Bank accepts the failure to meet the obligations (a default event) in respect of a given debtor, if at least one of the following three events has occurred:

a) deterioration in the counterparty/transaction credit quality. The Bank assumes that the debtor is not likely to fully meet its credit obligations towards the Bank, the parent company or the subsidiary of the Bank, without the Bank taking actions such as collateral realisation (if collateral exists);
b) delays in payments of more than 90 days. Any exposure representing a debt liability of a debtor to the Bank or its parent company or subsidiary shall be past due by over 90 days, provided that:
   - in the case of retail exposures, the amount past due exceeds PLN 500,
   - in the case of the remaining exposures, the amount past due exceeds PLN 3,000,
c) classification of the entity as "in default" by the Bank's parent company.

The Bank reports defaulting customers to mBank S.A. on a monthly basis. At the same time, on being notified by mBank S.A. that the Bank's parent entity has found a customer of the Bank to be in default, the Bank reclassifies such a customer to the "default" category.

Retail loan portfolio granted in an agency scenario in cooperation with mBank S.A.

In the case of the retail portfolio, where loans are granted in cooperation with mBank (the gross carrying value of the portfolio as at 31 December 2013 is PLN 6,097 thousand), the amount of impairment write-downs is determined using the IMPAIRMENT system (a computer system used to calculate provisions and impairment write-downs for credit exposures in accordance with the International Financial Reporting Standards). It is assumed that there is evidence of impairment of a retail exposure if:

a) the amount of exposure is greater than PLN 500 PLN and it is delayed by more than 90 days,
b) a transaction is fraudulent,
c) a transaction is subject to restructuring,
d) a loan receivable is sold at a substantial economic credit loss,
e) the Bank files a request to initiate enforcement proceedings, bankruptcy or reorganisation proceedings (resulting in a possible omission of or delay in repayment) against the debtor associated with a given loan liability,
f) a loan liability is disputed by the debtor in court.

All cases of identified impairment are designated automatically, except for restructured or sold contracts, frauds and operational cases that are recognised as part of a case-by-case analysis. The method of measuring impairment loss is based on the portfolio method, except for selected mortgage exposures where events have occurred which make it necessary to analyse such exposures on a case-by-case basis.

In the case of retail exposures, the Bank identifies evidence for impairment at the transaction level.

According to the Bank, the date of default is the date of taking the decision regarding the occurrence of default based on information about lenient and stringent premises, as well as the exposure assessment analysis.

<u>Stringent premises of default</u>

The following elements constitute "stringent" premises of a default event, as they correspond to the deterioration of credit quality of a customer/transaction in accordance with the adopted definition:

a) recognition of an impairment write-down or establishment of a specific provision due to a visible deterioration of creditworthiness after the liability to the Bank arose;
b) the Bank's disposal of an exposure at a significant economic loss associated with a change in its creditworthiness;
c) the Bank's consent to forced restructuring of a loan liability, provided that this may result in reducing financial liabilities as a result of redeeming a significant part of the liability or deferring repayment of the principal, interest or commission — if any;
d) the Bank's filing of a statement declaring the debtor bankrupt or of a similar motion in reference to debtor's loan liabilities to the Bank, Bank's parent entity or subsidiary;
e) the debtor being declared bankrupt or obtaining similar legal protection leading to avoidance or delay of loan liabilities repayment to the Bank, Bank's parent entity or subsidiary.

<u>Lenient premises of default</u>

Apart from the stringent premises determining the occurrence of a default event, the Bank also identifies lenient premises. Lenient premises do not have to trigger automatic classification of a given event as a default event. Such premises are of a supplementary nature. These are issues which the Bank should additionally consider while analysing the borrower's situation, and which can indicate the deterioration of such situation. If, in the Bank's opinion, the identified lenient premises are of high significance for a given case, the Bank should commence the assessment explaining, whether there occurred a default event, independent of the lack of stringent premises.
The materiality (significance) of default premises should be coherent with the Bank's rating system.

In the event of lack of premises of impairment in relation to credit exposure, based on default probability, the impairment write-down on the incurred, but not identified losses, is calculated.
If there are impairment premises and the individual analysis of a given credit exposure does not show any impairment, the impairment write-down is calculated based on portfolio analysis parameters.

Principles of calculation of impairment write-downs

<u>Portfolio of commercial loans, loans to local government units (JST) and retail loans granted up until 2004</u>

For the purposes of impairment analysis, four portfolios have been distinguished at the Bank: retail loans granted up until 2004, the commercial portfolio, the public sector portfolio and the portfolio of retail loans granted in an agency scenario in cooperation with mBank S.A. The commercial portfolio is divided into two sub-portfolios to distinguish between loans to sole traders and other commercial loans (development loans, commercial loans and loans to legal entities).
A case-by-case analysis phase and a portfolio analysis phase have been isolated for the retail portfolio and the commercial portfolio. Each case-by-case analysis covers all loans in respect of which premises of impairment have been identified. The portfolio analysis covers all of the remaining loans.
The case-by-case analysis for retail loans consists of assigning an individual LGD ratio to each loan depending on the value of the LTV coefficient and the time over which the loan has remained in default. The case-by-case analysis for commercial loans consists of calculation of the amount of loss measured as the difference between the carrying amount of a loan and the current value of estimated future cash flows (excluding future losses on non-repaid loans that

have not yet been incurred) discounted at the original effective interest rate of a loan if objective evidence of impairment is identified.

For the purposes of the said assignment, a relation in the following form has been adopted:

$$LGD = (1 - ZLGD) * [BD * 100\% + (1 - BD) * \max(1 - CRR / LTV, 0)]$$

where:

LGD — (*Loss Given Default*) stands for the relationship between the expected loss on a given loan and the amount of the balance sheet exposure for that loan, estimated as at the date of impairment being measured;
ZLGD — (*Zero Loss Given Default*) stands for the percentage of loans which have defaulted, and which have left that state without the Bank taking any debt collection measures (the LGD for such loans is 0%);
BD — (*Bad Debt*) stands for the portion of loans for which Bank is unable to execute from collateral (because the debtor's place of residence is unknown, the property is inhabited by a family with a child, etc.) in total impaired loans (that had never had their classification as default changed);
CRR — (*Collateral Recovery Rate*) specifies what portion of the value of collateral (net of costs and after taking into consideration the time value of money) the Bank is able to recover if needed;
LTV — (*Loan to Value*) specifies the relationship between the loan amount and the value of the collateral as at the date of the impairment write-down being estimated. Should the LTV be impossible to determine due to the bank mortgage value of the real estate being unavailable, the highest possible LTV should be assumed. When estimating recovery, loans in this situation are treated as non-secured.

The portfolio analysis covers all retail and commercial loans which are not subject to the case-by-case analysis. The portfolio analysis makes use of ZLGD, BD, CRR and LTV parameters which are used for calculating LGD in the case-by-case analysis and, in addition, PD and LIP parameters.
LIP Parameter (*Loss Identification Period*) is defined as an average period that is sufficient for the Bank to identify conditions indicating a loss in value of loan. The Bank assumes that current LIP is 6 months.

PD Parameter (*Probability of Default*) is the probability of default in the loss identification period. PD for a given six-month period is calculated as a number of retail customers in respect of whom evidence of impairment was identified during the period divided by the number of customers present in the Bank's portfolio both at the beginning and end of the six-month period. PD, determined this way, is used to calculate average PD for 18 months.
Each separate portfolio has its own set of ZLGD, BD, CRR and PD parameters.

The following formula is used for measuring impairment on a portfolio basis:

$$RP = \sum_{i \notin \{\text{ind. analysed loans}\}} BS_i LGD_i PD$$

where:

RP — (*Portfolio Reserve*) stands for impairment write-down for incurred, but not identified losses;
PD — stands for the probability of default in the LIP period;
BS_i — stands for the current balance sheet exposure of the loan, in keeping with measurement at amortised costs;
LGD_i — stands for the LGD parameter set as at the date of the write-down being estimated, in accordance with the method discussed in the section on the case-by-case analysis, for the i loan.

Both in the case of the case-by-case analysis based on LGD and the portfolio analysis, a full-scope analysis is performed every six months. Impairments are updated on a monthly basis in accordance with the following equation:

$$RP = LGD_p \sum_{i \notin \{\text{ind. analysed loans}\}} BS_i PD$$

$$RP = LGD_p \sum BS_i$$

where:

LGD_p — stands for the relationship between the aggregate level of impairments for a given portfolio, determined on the basis of a full-scope analysis as at the end of the last six-month period, and the value of the balance sheet exposure of the loans in a given portfolio. The retail portfolio, impaired retail portfolio, commercial loans for sole traders and other commercial loans have separate LGD_p parameters.

The standard system for monitoring the Bank's loan portfolio consists of:

a) monitoring the timeliness of repayments,
b) monitoring the real estate which is being financed,
c) monitoring the economic and financial position of the borrower to whom a loan for commercial real estate has been granted to verify liquidity ratios and the debt servicing coverage ratio,
d) monitoring compliance with all regulations on environmental protection, occupational health and safety, and public safety,
e) reviewing the validity of collateral.

In the case of assets for which permanent impairment has been identified, the Bank imposes stricter monitoring, e.g. it reassesses the bank mortgage value of the real estate which constitutes collateral for the loan.

For the purposes of impairment measurement the Bank does not use the rating model.

<u>Retail loan portfolio granted in an agency scenario in cooperation with mBank S.A.</u>

For the purposes of impairment calculation, retail exposures are grouped into homogeneous portfolios with similar risk characteristics. For each of these portfolios risk, risk parameters are determined (probability of loss — PD and the amount of potential loss where such an indicator is present — LGD). The values of these parameters are calculated using the historical data for each portfolio and depend on the length of the overdue period. As at 31 December 2013, in the absence of sufficient time series, the Bank applies to this portfolio parameters calculated for a corresponding portfolio of mBank S.A. Subsequently, risk parameters and the amortised value of credit exposure are used to calculate the portfolio write-down on retail receivables.
The indicator of impairment is used in the calculation of the write-down on retail receivables in respect of individual transactions, not debtors. Therefore, the occurrence of an indicator of impairment does not result in classifying the remaining liabilities of the debtor as affected by the same indicator.

3.2.4. Maximum credit risk exposure — prior to accounting for collateral accepted

As at the end of 2013 and 2012, the Bank did not have any assets with maximum credit risk exposure different from their carrying value.

The Bank has a system for controlling and keeping its credit risk exposure to a minimum. 86.60% of the portfolio of loans and advances to customers and 100% of amounts due from banks are serviced on a timely basis and no impairment has been identified in their case (as at 31 December 2012: 90.49% and 100%, respectively).

<u>Maximum exposure to credit risk — financial effect of collaterals</u>

The tables below present the financial effect of collaterals, that is to what extent collaterals mitigate credit risk.

As at 31 December 2013	Gross value	Established impairment write-down	Impairment write-down without the collateral cash flows	Financial effect of collaterals
Balance sheet data				
Amounts due from other banks	**22,377**	**-**	**-**	**-**
Loans and advances to customers, including:	**4,120,588**	**(75,588)**	**(240,753)**	**165,165**
Individual customers	95,754	(1,994)	(6,044)	4,050
Corporate customers	3,799,524	(73,527)	(234,642)	161,115
Public sector customers	225,302	(67)	(67)	-
Other receivables	8	-	-	-
Total balance sheet items	**4,142,965**	**(75,588)**	**(240,753)**	**165,165**
Off-balance sheet data				
Lending commitments	969,798	-	-	-
Total off-balance sheet items	**969,798**	**-**	**-**	**-**

As at 31 December 2012	Gross value	Established impairment write-down	Impairment write-downs without the collateral cash flows	Financial effect of collaterals
Balance sheet data				
Amounts due from other banks	**10,282**	**-**	**-**	**-**
Loans and advances to customers, including:	**4,154,401**	**(46,246)**	**(194,539)**	**148,293**
Individual customers	97,944	(1,213)	(5,749)	4,536
Corporate customers	3,733,408	(44,936)	(188,693)	143,757
Public sector customers	322,737	(97)	(97)	-
Other receivables	312	-	-	-
Total balance sheet items	**4,164,683**	**(46,246)**	**(194,539)**	**148,293**
Off-balance sheet data				
Lending commitments	788,433	-	-	-
Total off-balance sheet items	**788,433**	**-**	**-**	**-**

3.2.5. Loans and advances to customers and banks

Loans and advances to customers	31.12.2013		31.12.2012	
	exposure (PLN '000)	share/coverage (%)	exposure (PLN '000)	share/coverage (%)
Not overdue, without impairment recognised	3,568,460	86.60	3,759,439	90.49
Overdue, without impairment recognised	333,463	8.09	217,857	5.25
Items with impairment recognised	218,665	5.31	177,105	4.26
Total gross	**4,120,588**	**100.00**	**4,154,401**	**100.00**
Impairment write-down on items not overdue, without impairment recognised	(6,528)	0.16	(6,077)	0.14
Impairment write-down on items overdue, without impairment recognised	(678)	0.02	(378)	0.01
Impairment write-down on items with impairment recognised	(68,382)	1.66	(39,791)	0.96
Total impairment write-down	(75,588)	1.84	(46,246)	1.11
Total net	**4,045,000**	**98.16**	**4,108,155**	**98.89**

The table below presents amounts due from banks:

Amounts due from other banks	31.12.2013		31.12.2012	
	exposure (PLN '000)	share/coverage (%)	exposure (PLN '000)	share/coverage (%)
Not overdue, without impairment recognised	22,377	100.00	10,282	100.00
Total gross	**22,377**	**100.00**	**10,282**	**100.00**
Total net	**22,377**	**100.00**	**10,282**	**100.00**

The Bank does not have any past due or impaired amounts due from banks.

for the year 2013 (in PLN ‘000)

Loans and advances neither past due nor impaired

Gross amounts of loans and advances neither past due nor impaired, broken down by rating score, are presented below.

	31.12.2013	31.12.2012
Exposures permanently exempted from the IRB approach	664,702	800,397
Exposures temporarily exempted from the IRB approach — specialised lending, including:	473,361	486,248
- PFSA category 1	4,941	-
- PFSA category 2	461,080	457,098
- PFSA category 3	7,340	29,150
Exposures temporarily exempted from the IRB approach — retain portfolio sold on an agency basis	6,097	-
Exposures subject to the IRB approach, including:	2,424,292	2,472,482
- PFSA category 1	4,958	-
- PFSA category 2	2,243,279	2,386,473
- PFSA category 3	149,280	73,927
- PFSA category 5	26,775	12,082
Other receivables	8	312
Total	**3,568,460**	**3,759,439**

Gross amounts of loans and advances neither past due nor impaired, broken down by customer category, are presented below.

	31.12.2013	31.12.2012
Individual customers	84,388	86,960
Corporate customers	3,264,411	3,359,104
Public sector customers	219,653	313,063
Other receivables	8	312
Total customers	**3,568,460**	**3,759,439**
Banks	22,377	10,282
Total	**3,590,837**	**3,769,721**

Evaluation of the credit quality of loans and advances neither past due nor impaired

	31.12.2013	31.12.2012
Loans and advances with limited credit risk	473,994	552,377
Loans and advances with standard credit risk	3,057,654	3,183,120
Loans and advances with increased credit risk	36,812	23,942
Total	**3,568,460**	**3,759,439**

The portfolio of loans and advances with limited credit risk includes loans and advances granted to customers from the public sector and to corporate customers, with a guarantee or a pledge from a local government unit constituting the basic legal security. The portfolio of loans and advances with standard credit risk includes loans and advances granted to individuals and corporate customers, with mortgage set up on real estate constituting the basic collateral, and in their case there is no evidence of impairment.
The portfolio of loans and advances with increased credit risk includes loans and advances granted to corporate customers in the case of which there was evidence of impairment but impairment did not occur due to the expected full recovery of the exposures.

Evaluation of the credit quality of derivatives

	31.12.2013	31.12.2012
Derivatives with limited credit risk	12,913	11,128
Total	**12,913**	**11,128**

for the year 2013 (in PLN '000)

All derivative transaction as at 31 December 2013 were transactions concluded with mBank S.A., therefore the Bank assesses the amount of credit risk associated with such instruments as low.

Overdue loans and advances without impairment recognised

Overdue exposures are exposures to customers or banks for which at least one receivable is overdue by one or more days. In the case of the portfolio made available on an agency basis, overdue exposure means exposure associated with delayed contracts (by one day or more). For loans and advances overdue by less than 90 days, no impairment is recognised, unless other available information shows that impairment has taken place. In rare cases, for loans and advances overdue by more than 90 days, the Bank may decide not to recognize impairment if there is specific evidence that the said loans and advances have not been impaired.

Gross amounts of loans and advances which were overdue but not recognised as impaired, broken down by customer category, are presented below:

Overdue loans and advances without impairment recognised (31 December 2013)	Individual customers	Corporate customers	Public sector customers	Total customers
up to 30 days	5,114	261,742	5,649	272,505
from 31 to 60 days	300	56,352	-	56,652
from 61 to 90 days	133	404	-	537
more than 90 days	18	3,751	-	3,769
Total	**5,565**	**322,249**	**5,649**	**333,463**

Overdue loans and advances without impairment recognised (31 December 2012)	Individual customers	Corporate customers	Public sector customers	Total customers
up to 30 days	3,745	135,844	6,311	145,900
from 31 to 60 days	977	39,555	3,363	43,895
from 61 to 90 days	241	92	-	333
more than 90 days	16	27,713	-	27,729
Total	**4,979**	**203,204**	**9,674**	**217,857**

Loans and advances individually impaired

Gross amounts of loans and advances individually impaired (before taking account of cash flows in respect of the collateral held), broken down by asset category, are presented below.

Loans and advances individually impaired	Individual customers	Corporate customers	Total customers
31 December 2013			
Impaired loans and advances	5,801	212,864	218,665
Estimated credit support from contributions and collaterals	**3,713**	**146,365**	**150,078**
Impairment write-downs	**1,859**	**66,523**	**68,382**
Bank and mortgage value of real estate constituting collateral for loans	**15,446**	**247,295**	**262,741**
31 December 2012			
Impaired loans and advances	6,005	171,100	177,105
Estimated credit support from contributions and collaterals	**4,429**	**132,396**	**136,825**
Impairment write-downs	**1,064**	**38,727**	**39,791**
Bank and mortgage value of real estate constituting collateral for loans	**15,496**	**283,252**	**298,748**

In 2013, just as in 2012, the Bank did not recognise impairment on any exposures to banks.

The factors considered in determining the impairment of loans disclosed in table above comprise all impairment premises recognised by the Bank, including significant financial difficulties of the debtor and default in interest or principal repayment.

The basic form of collateral for loans granted by the Bank to its customers is mortgage established for the benefit of the Bank and entered as the first item in the land and mortgage register maintained for real estate.
The value of the real estate which constitutes collateral for a loan granted by the Bank is estimated on the basis of the concept of the so-called bank mortgage value which assumes that the real estate will retain its value over a longer period of time.

In the event of adverse changes in the value of collateral, the Bank verifies it by revaluing the real estate. Depending on the effects of the valuation, the Bank, as a rule, negotiates with the borrower, in accordance with the loan agreement concluded:

a) setting up additional collateral,
b) changing the collateral,
c) making a one-off repayment of the debt to the LTV level acceptable by the Bank,
d) renegotiating the terms of agreement.

As a result of the valuation analysis, the Bank revalues the estimated credit support from contributions and collaterals and creates an impairment write-down.

Failure to reach agreement may result in the loan agreement being terminated in part or in full if the economic and financial position of the borrower has deteriorated permanently.

The Bank has a contingency plan in the event of unexpected, radical changes in prices on the real estate market.

Additionally, in the above tables, in the item "Bank mortgage value of the real estate constituting collateral for loans", the Bank shows the present value of the collateral accepted, not adjusted to the decreasing value of the credit exposure. The bank and mortgage value of real estate constituting collateral for the loans granted by the Bank exceeds the value of the exposure. Therefore, in the event of any additional amounts due from exposure, e.g. additional enforcement costs, etc., the Bank will be able to satisfy its claims.

The bank and mortgage value of real estate is established for the purposes of the Bank and, in the Bank's opinion, reflects the level of the risk related to the real estate as collateral of loans granted. The bank and mortgage value of real estate takes particular account of only those characteristics of the real estate and the related revenues that, with the assumption of the rational use, are of permanent nature and may be obtained by any of the real estate holders.

3.2.6. Debt instruments: investment securities

The value of investment securities and amounted to PLN 605,824 thousand as at 31 December 2013, compared to PLN 566,258 thousand as at 31 December 2012. Both as at 31 December 2013 and as at 31 December 2012, debt instruments had a rating of A- to A+ on the scale of Fitch Rating agency. Certain investment securities serve as collateral for the guaranteed deposits protection fund, as referred to in Note 35.

Both as at 31 December 2013 and as at 31 December 2012, all investment securities were neither past due nor impaired.

3.2.7. Repossessed collateral

The Bank may directly repossess the real estate of a debtor of the Bank on which a mortgage has been established to secure the repayment of a loan, in exchange for cancelling all or a part of the loan liability under a given loan agreement.
Repossession applies to the properties of the Bank's debtor which constitute mortgage collateral for the repayment of liabilities under the loan agreement or other properties indicated by the Bank's debtor and accepted by the Bank as the object of repossession.

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The Bank is obliged to take measures to dispose of the repossessed property or a part thereof immediately after the purchase/repossession.

The decision as to the sale strategy for the property or a part thereof repossessed/purchased by the Bank and the mode of such a sale is taken by the Bank's Management Board.
As at 31 December 2013, the value of repossessed collateral amounted to PLN 8,192 thousand, as compared to PLN 89,073 thousand as at 31 December 2012.

Changes in repossessed collateral

	Period from 01.01.2013 to 31.12.2013	Period from 01.01.2012 to 31.12.2012
As at the beginning of the period	**89,073**	**18,772**
Increase (due to)	11,314	75,494
- repossessed real estate	8,172	74,708
- activated transaction costs	20	786
- reversal of impairment write-downs on sold properties	3,122	-
Decrease (due to)	(92,195)	(5,193)
- sale of real estate	(92,066)	(3,460)
- establishment of impairment write-downs	(129)	(1,733)
As at the end of the period	**8,192**	**89,073**

In 2013, the Bank repossessed properties for a total amount of PLN 8,172 thousand. Based on:

- an agreement on the transfer of premises to release debtors (a Borrower and a Company assuming a part of the Borrower's debt) from a liability of 2 December 2013 for a total gross amount of PLN 3,391 thousand, i.e. PLN 2,757 thousand net. As a result of the repossession of the property, a part of the debtors' liability in the amount of PLN 2,757 thousand expired. The difference between the value of the properties covered by the agreement and transferred to the Bank and the amount of liability which expired, i.e. PLN 634 thousand, in accordance with the agreement, was repaid by the Bank on behalf of the debtors entirely to the account of the Tax Office. The value of the repossessed property totalling PLN 2,757 thousand was increased by the cost of a notarial deed, i.e. by PLN 20 thousand. The amount of PLN 2,777 thousand was posted to the inventories account under the agreement in question. The remainder of the Borrower's liability in the amount of PLN 2,013 thousand was sold under an agreement on the sale of receivables of 2 December 2013 for the price of PLN 2 thousand to the company which assumed a part of the Borrower's debt,
- an agreement on the transfer of the property to release the debtors from a liability dated 2 December 2013 for a total amount of PLN 6,660 thousand gross, i.e. PLN 5,415 thousand net. Consequently, the amount of PLN 5,415 thousand was posted to the inventories account. Following the repossession of the property, the obligation to repay a part of the loan principal and interest totalling PLN 4,574 thousand to the Bank expired. The difference between the value of the properties covered by the agreement and transferred to the Bank and the amount of liability which expired, i.e. PLN 2,086 thousand, in accordance with the agreement:
  - was repaid by the Bank on behalf of the debtors in the amount of PLN 1,245 thousand to the account of the Tax Office.
  - the remaining amount of PLN 841 thousand was set off against the claim of the Company which acquired the remainder of the Borrower's debt from the Bank in accordance with an agreement concluded on 2 December 2013.

In 2013, the Bank sold a part of premises in the properties repossessed in 2012 and 2011 properties with a total book value of PLN 4,933 thousand.

In 2013, the Bank sold four properties repossessed in 2012 and 2011 for a total gross amount of PLN 78,439 thousand, i.e. PLN 68,226 thousand net, with a total book value of PLN 87,133 thousand on the basis of agreements concluded with BDH Development Sp. z o.o. (Buyer):

- a sale agreement dated 12 December 2013 for a total gross amount of PLN 48,462 thousand, i.e. PLN 39,400 thousand net. As at 31 December 2013, the entire amount has been paid by the Buyer. The book value of the property is PLN 35,145 thousand. With the sale of the property in question, the Bank generated an accounting profit of PLN 4,255 thousand (Note 10), and a tax profit of PLN 6,503 thousand. The difference between the accounting profit and the tax profit in a non-deductible tax cost (Note 14),
- a sale agreement dated 23 December 2013, amended by a notarial deed of 3 January 2014 for a total amount of PLN 15,644 thousand net (which is also the gross price, as the transaction was exempted from value added tax (VAT)). In keeping with the agreement, the Buyer paid the amount to the Bank in January 2014. The book value of the property is PLN 18,500 thousand. In connection with the sale transaction, an impairment write-down on the property of PLN 1,093 thousand was reversed. With the sale of the property in question, the Bank generated an accounting loss of PLN (1,762) thousand (Note 13), and a tax loss of PLN (2,855) thousand,
- a sale agreement dated 23 December 2013 for a total gross amount of PLN 22,784 thousand, i.e. PLN 18,524 thousand net. Under the agreement, the amount will be paid by the Buyer as follows: PLN 18,779 thousand within 21 days from the date of conclusion of the agreement (the amount was paid in January 2014), the amount of PLN 4,005 thousand is to be repaid by 31 March 2014. The book value of the property is PLN 17,761 thousand. In connection with the sale transaction, an impairment write-down on the property of PLN 640 thousand was reversed. With the sale of the property in question, the Bank generated an accounting profit of PLN 1,403 thousand (Note 10), and a tax profit of PLN 763 thousand,
- a sale agreement dated 23 December 2013 for a total amount of PLN 14,333 thousand gross, i.e. PLN 13,182 thousand net. In keeping with the agreement, the Buyer paid the amount in January 2014. The book value of the property is PLN 15,727 thousand. In connection with the sale transaction, an impairment write-down on the property of PLN 1,389 thousand was reversed. With the sale of the property in question, the Bank generated an accounting loss of PLN (1,156) thousand (Note 13), and a tax loss of PLN (2,545) thousand.

The amount owed and not paid by the Buyer for the sale of inventories is presented in the statement of financial position under Other assets — receivables from the sale of inventories (Note 26). Due to the fact that the Buyer is a company associated with the Bank, the account receivable in respect of the sale of inventories is presented in Note 40.

The profit from the sales of inventories is presented in the income statement under "Other operating income" — "Profit from the sales of inventories" (Note 10). The loss on the sales of inventories is presented in "Other operating expenses" — "Loss on the sales of assets repossessed for debts (inventories) and costs of their maintenance" (Note 13). Due to the fact that the Buyer is a company associated with the Bank, both the gain and the loss in respect of the sale of inventories are presented in Note 40.

3.3. Concentration of assets, liabilities and off-balance-sheet items

Risk of geographical concentration

The Bank does not present its assets, liabilities or off-balance-sheet items by geographical area due to the geographical diversification of risks being immaterial. The Bank operates only within the territory of the Republic of Poland.

Risk of concentration of large exposures, risk of concentration of exposures

The concentration risk is a risk which may significantly affect the stability and safety of the Bank's operations through default on the part of a single entity, entities related in terms of equity or organization, or groups of entities in the case of which the probability of such default is dependent on common factors.

As part of managing the concentration risk, the Bank identifies the risk, measures, monitors, and reports it.

The Bank's concentration risk is measured by determining the amount of the exposure which generates the concentration risk and comparing this amount with the established limits specified in the legal regulations and internal limits.
The Bank mitigates the credit risk using the internal exposure concentration limits specified in the internal procedures.

While determining the proposed levels of the internal exposure concentration limits, the Bank takes the following issues into account:

a) the macroeconomic situation in Poland,
b) the situation of the real estate market in Poland,
c) the situation of the financial markets in Poland,
d) the implementation of the Bank's lending policies in the previous year,
e) the results of the Bank's restructuring and debt collection measures,
f) information on the financial position of entities, industries, branches, and sectors of the economy taken from reliable sources (academic centres), in accordance with the recommendations of Resolution No 384/2008 of the Polish Financial Supervision Authority,
g) economic and quality information on the process of management in the entities to which it has exposures that generate the concentration risk,
h) factors arising from other types of risk relating to the identified exposures which generate the concentration risk (including the interest rate risk, the liquidity risk, the operating risk, and the political risk) that might contribute to an increase in the concentration risk,
i) the results of stress tests.

The internal exposure limits are specified in relation to the amount of the Bank's own funds and in relation to the Bank's aggregate exposures.

The Bank reports on the concentration risk monitored on a monthly basis, with regard to:

a) monitoring holding companies,
b) monitoring the exposure concentration limit,
c) monitoring the limit on large exposures,
d) monitoring the limit on loans granted to the Bank's related entities,
e) monitoring internal limits.

<u>Risk of industry concentration</u>

The Bank concentrates its activities on granting loans secured with a mortgage on real estate to legal entities, loans to local authorities, and loans secured with a guarantee or a warranty of local authorities. Irrespective of the external loan concentration limits, the Bank's Management Board sets internal limits relating to, amongst others:

a) industry concentration by type of real estate being financed,
b) financing real estate under construction and land purchases,
c) the share of financing of the individual types of real estate in the loan portfolio.
d) geographic concentration, currency concentration,
e) the type of interest rates used in the Bank (fixed and floating),
f) the duration of the tenor.

In 2013, none of the above internal limits was exceeded.

The assessment of an individual credit risk in the case of financing commercial real estate is carried out based on the evaluation of the creditworthiness of borrowers, credit ratings, encompassing quantitative ratios, i.e. the debt service coverage ratio (DSCR), the interest service coverage ratio (ISCR), the level of own funds, and in the case of housing developers — the benchmarking price level, as well as qualitative measures, e.g. way of managing projects or default incident identification. The Bank's ratings include several segments of specialised financing defined in the Bank's procedures with regard to their diversification by the investment type and phase. The Banks assesses credit transaction risk by risk estimates. In particular, the Bank, whose operations are burdened with credit risk, prior to the conclusion and during the execution of a given transaction carries out a risk assessment — in the form of monitoring — based on individual rating systems which were developed based on expert approach.

Credit risk management in financing commercial real estate includes also: recognising impairment write-downs of balance sheet credit exposures and write-downs of off-balance-sheet credit exposures, write-down recognition and reversal ratios, the use of limits, stress tests, scenario analyses, monitoring the dues concentration limit, the use of collateral for loans, following conservative principles for determining the bank mortgage value of real estate, the use of statistical models for updating the value of real estate.

The structure of the concentration of the Bank's exposure to individual industries is presented in the table below.

Item	Industries	Net carrying amount (PLN '000) 31.12.2013	Share in the portfolio (%)	Net carrying amount (PLN '000) 31.12.2012	Share in the portfolio (%)
1.	Activity related to the real estate market	2,580,077	63.78	2,571,132	62.59
2.	Building industry	903,963	22.35	881,525	21.46
3.	Activity related to culture, entertainment and leisure	217,392	5.37	195,644	4.76
4.	Public administration and defence; compulsory social security	155,919	3.86	178,636	4.35
5.	Health protection and social welfare	71,786	1.78	146,775	3.57
6.	Activity related to accommodation and catering services	22,303	0.55	25,538	0.62
7.	Individuals	46,678	1.15	46,161	1.12
8.	Other	46,882	1.16	62,744	1.53
	Total	**4,045,000**	**100.00**	**4,108,155**	**100.00**

3.4. Market Risk

The Bank is exposed to the market risk understood as the risk of changes in the current valuation of the financial instruments which constitute the Bank's portfolios, which result from changes in prices and the values of market parameters. The Bank's exposure to the market risk is the result of there being open positions in interest rate and foreign exchange instruments which are exposed to market changes in the values of the relevant risk factors, in particular to changes in interest rates, exchange rates, and the volatility of these risk factors.

The risk profile results from the Bank's operating strategy. The Bank offers products based on variable and fixed interest rates, but products based on the variable interest rates are preferable. The Bank offers products in foreign currencies: EUR and USD. The Bank does not perform transactions on its own account for trading purposes; it only has the bank portfolio. The Bank's key method for managing the market risk is the use of natural hedges, i.e. obtaining funds in the currencies and with the interest rates that are directly tailored to the corresponding assets. Due to the nature of the Bank's operations, the exposure to the market risk should be maintained at a relatively low level. The Bank tries to limit its exposures to the market risk, following from the structure of its assets and liabilities, by concluding hedging transactions whose catalogue is approved by the Bank's Management Board. In the identification of market and liquidity risks, both internal and external factors are taken into account. The internal factors include: the specific nature of lending activities and the specific nature of the refinancing structure. The external factors comprise factors which constitute the Bank's environment: the interbank market, the behaviour of the financial markets, the shareholder's strategy and policies vis-à-vis the Bank. The market risk is identified in all types of products and activities. The identification process relies on universally applicable methodologies. The Bank determines the risk level by measuring the Value at Risk (VaR) and by conducting stress tests.

VaR is a statistical measure of the market risk level which illustrates the possible loss to which a portfolio is exposed during a specific period of time, for a given confidence level, in normal market conditions, due to changes in risk factors (exchange rates, interest rates, prices). The possibility of a loss means that with a high, previously determined degree of probability (the confidence level), with which the value at risk is determined, a loss smaller than the VaR determined may be expected over a given period of time.

The Bank determines the value at risk using the historical simulation method. In this method, the dispersion of changes in the value of a portfolio is determined on the basis of the historical dispersion of changes in risk factors, observed over a specific period of time. VaR is determined with a one-day time horizon, on the basis of 250 historical observations, and is monitored at the confidence level of 99%.

As at 31 December 2013, VaR amounted to PLN 115 thousand, with the confidence level amounting to 99%. As at 31 December 2012, VaR amounted to PLN 176 thousand, with the confidence level amounting to 99%.

The value of the Bank's average VaR in the period from 01.01.2013 to 31.12.2013 and in the period from 01.01.2012 to 31.12.20112 is presented in the table below.

in PLN '000	12 months until 31.12.2013		12 months until 31.12.2012	
	average	maximum	average	maximum
Interest rate risk	109	203	115	261
Currency risk	53	1,083	27	912
Total VaR	**162**	**1,073**	**142**	**1,173**

<u>Stress tests and scenario testing</u>

An additional market risk measure, which supplements the measurement of value at risk, is a stress test which shows a hypothetical change in the current valuation of the Bank's portfolio, which would result from the risk factors assuming specified extreme values in a one-day time horizon. The Bank uses, inter alia, the method of a scenario consisting of large, extremely correlated changes (identical in every group) in the values of risk factors. As at 31 December 2013, the risk amount resulting from this scenario was PLN 516 thousand, whereas the average risk amount for this scenario in the period from 01.01.2013 to 31.12.2013 was PLN 892 thousand.

The decomposition of the risk amount resulting from the said stress test into an amount allocated to the interest rate risk and the currency risk is presented below.

Stress tests	31.12.2013			31.12.2012		
	Total	Interest rate risk	Currency risk	Total	Interest rate risk	Currency risk
Amount of risk in PLN '000	516	(3,545)	4,061	1,494	(1,876)	3,370

The Bank measures the sensitivity of the current value of its portfolio to a parallel shift of the yield curve by 100 BP in a direction which is unfavourable from the perspective of the maturity profile of the remeasurement gap. The remeasurement gap presents the Bank's aggregate interest-capital exposures corresponding to the individual nodes of the yield curve. The 100 BP risk amount is determined as the difference between the current value of a portfolio, calculated on the basis of 100 BP-stressed risk factor values as at the reporting date, and the current value of the portfolio based on the risk factor values observed on the reporting date. The 100 BP risk amount ran at PLN 214 thousand as at 31 December 2013, whereas its average in the period from 1 January 2013 to 31 December 2013 was PLN 1,988 thousand, as at 31 December 2012 it was PLN 573 thousand, and the average in the period from 1 January 2012 to 31 December 2013 was PLN 593 thousand.

3.5. Currency risk

The currency risk is the result of the exposure of the current value of the Bank's exposures in assets, liabilities, and off-balance-sheet items denominated in PLN to the adverse effects of changes in market exchange rates.

The Bank is exposed to the currency risk to a small extent because it does not maintain a significant currency mismatch of its assets and liabilities (the foreign currency position), by adjusting the currency structure of conducted lending campaign and sources of refinancing and closing the balance sheet currency position with derivative contracts (Note 20). The risk of the effect of changes in exchange rates on the Bank's results of operations is limited, and the control and reporting procedures in place at the Bank eliminate the possibility of such risk arising to a considerable extent. As part of the currency risk management, the Bank evaluates the scale and structure of the currency risk exclusively on the basis of the Bank's current foreign currency position. The foreign currency position taking account of the expected loan repayments and loan advances affecting the currency risk is also subject to monitoring. The Bank manages its foreign currency position by conducting spot or forward currency purchase/sale transactions and by concluding SWAP transactions.

for the year 2013 (in PLN '000)

The table below shows the Bank's exposures exposed to currency risk as at 31.12.2013 and as at 31.12.2012. The table shows the Bank's assets and liabilities at carrying amounts, by currency.

31.12.2013	PLN	EUR	USD	Total
Assets				
Cash and balances with the Central Bank	7,378	-	-	**7,378**
Amounts due from other banks	22,114	161	102	**22,377**
Derivative financial instruments	12,573	340	-	**12,913**
Loans and advances to customers	1,815,097	2,132,499	97,404	**4,045,000**
Investment securities available for sale	605,824	-	-	**605,824**
Investments in subsidiaries	-	-	-	**-**
Intangible assets	3,548	-	-	**3,548**
Tangible fixed assets	9,110	-	-	**9,110**
Deferred tax assets	13,058	-	-	**13,058**
Current income tax assets	620	-	-	**620**
Other assets	62,428	187	-	**62,615**
Assets exposed to currency risk, in total	**2,551,750**	**2,133,187**	**97,506**	**4,782,443**
Liabilities				
Amounts due to other banks	30,053	1,128,115	45,320	**1,203,488**
Derivative financial instruments	1	277	-	**278**
Amounts due to customers	264,554	29,806	807	**295,167**
Debt securities in issue	2,286,169	375,238	-	**2,661,407**
Subordinated liabilities	100,268	-	-	**100,268**
Other liabilities and provisions	19,872	-	-	**19,872**
Liabilities exposed to currency risk, in total	**2,700,917**	**1,533,436**	**46,127**	**4,280,480**
Net balance-sheet currency gap	**(149,167)**	**599,751**	**51,379**	**501,963**
Derivative financial instruments (FX, FX SWAP) — purchase	**664,807**	**1,452**	**-**	**666,259**
Derivative financial instruments (FX, FX SWAP) — sale	**1,453**	**603,418**	**51,204**	**656,075**
Net currency gap	**514,187**	**(2,215)**	**175**	**512,147**

31.12.2012	PLN	EUR	USD	Total
Assets				
Cash and balances with the Central Bank	3,069	-	-	**3,069**
Amounts due from other banks	10,119	135	28	**10,282**
Derivative financial instruments	11,128	-	-	**11,128**
Loans and advances to customers	2,101,431	1,898,051	108,673	**4,108,155**
Investment securities	566,258	-	-	**566,258**
Investments in subsidiaries	65	-	-	**65**
Intangible assets	1,384	-	-	**1,384**
Tangible fixed assets	9,171	-	-	**9,171**
Deferred tax assets	9,960	-	-	**9,960**
Other assets	90,196	44	-	**90,240**
Assets exposed to currency risk, in total	**2,802,781**	**1,898,230**	**108,701**	**4,809,712**
Liabilities				
Amounts due to other banks	-	1,064,761	107,706	**1,172,467**
Derivative financial instruments	111	350	-	**461**
Amounts due to customers	154,221	23,977	835	**179,033**
Debt securities in issue	2,811,370	41,075	-	**2,852,445**
Subordinated liabilities	100,316	-	-	**100,316**
Other liabilities and provisions	4,122	-	-	**4,122**
Current income tax liabilities	163	-	-	**163**
Liabilities exposed to currency risk, in total	**3,070,303**	**1,130,163**	**108,541**	**4,309,007**
Net balance-sheet currency gap	**(267,522)**	**768,067**	**160**	**500,705**
Derivative financial instruments (FX, FX SWAP) — purchase	**788,097**	**-**	**-**	**788,097**
Derivative financial instruments (FX, FX SWAP) — sale	**-**	**784,934**	**-**	**784,934**
Net currency gap	**520,575**	**(16,867)**	**160**	**503,868**

3.6. Interest rate risk

Interest rate risk is a risk arising from the exposure of the current and future results of the Bank and its capital to the adverse effect of changes in interest rates. The Bank manages the interest rate gap by matching the revaluation dates of assets and liabilities. In the event of such mismatch arising, appropriate hedging instruments are used (derivative transactions IRS, Basis Swap). The interest rate derivative transactions are concluded exclusively for the purpose of hedging the items arising from the Bank's lending activities and its financing.

The mismatch gap on the revaluation dates and the interest income at risk ("EaR") determined on its basis are a measure of interest rate risk.

A sudden, permanent and adverse change in market interest rates of 100 BP for all the maturity dates would result in the annual interest income being reduced by:

EaR (in PLN '000)	31.12.2013	31.12.2012
for items expressed in PLN	5,228	4,687
for items expressed in USD	12	6
for items expressed in EUR	49	87

While calculating these values, it was assumed that the structure of assets and liabilities recognised in the financial statements as at 31 December 2013 and as at 31 December 2012 would not change within the following year and that the Bank would not take any actions to change the exposure to risk.

In 2013, the level of interest rate risk was maintained at a similar level to 2012 as a result of ongoing matching of the dates for revaluation of loans granted and their corresponding sources of financing. Additionally, in order to mitigate the interest rate risk the Bank concludes IRS hedging transactions.

The Bank's exposures to interest rate risk are presented below. The data in the table shows assets and liabilities at carrying amounts, in the order of reprising dates specified in the agreements or their maturity.

31.12.2013	Up to 1 month	From 1 to 3 months	From 3 to 12 months	From 1 to 5 years	Over 5 years	Total
Interest-bearing assets	1,820,182	1,265,877	1,545,468	49,044	-	**4,680,571**
Interest-bearing liabilities	1,546,689	942,987	1,643,137	-	123,533	**4,256,346**
Interest-bearing assets – interest-bearing liabilities	**273,493**	**322,890**	**(97,669)**	**49,044**	**(123,533)**	**424,225**
Derivative financial instruments assets	6,326	980	5,607	-	-	**12,913**
Derivative financial instruments liabilities	-	278	-	-	-	**278**
Derivative financial instruments assets – derivative financial instruments liabilities	**6,326**	**702**	**5,607**	**-**	**-**	**12,635**
Net gap	**279,819**	**323,592**	**(92,062)**	**49,044**	**(123,533)**	**436,860**

31.12.2012	Up to 1 month	From 1 to 3 months	From 3 to 12 month	From 1 to 5 years	Total
Interest-bearing assets	2,032,783	1,397,399	1,176,037	81,233	**4,687,452**
Interest-bearing liabilities	1,247,099	1,150,480	1,905,268	-	**4,302,847**
Interest-bearing assets – interest-bearing liabilities	**785,684**	**246,919**	**(729,231)**	**81,233**	**384,605**
Derivative financial instruments assets	6,881	1,935	2,312	-	**11,128**
Derivative financial instruments liabilities	-	111	350	-	**461**
Derivative financial instruments assets – derivative financial instruments liabilities	**6,881**	**1,824**	**1,962**	**-**	**10,667**
Net gap	**792,565**	**248,743**	**(727,269)**	**81,233**	**395,272**

In the breakdown, the item "Interest-bearing assets" comprises:

- cash and balances with the Central Bank,
- amounts due from other banks,
- investment securities,
- loans and advances to customers (excluding other amounts due).

In the breakdown, the item "Interest-bearing liabilities" comprises:

- amounts due to other banks,
- amounts due to customers (excluding other liabilities),
- debt securities in issue,
- subordinated liabilities.

In the breakdown, the items "assets in respect of derivative financial instruments" and "liabilities in respect of derivative financial instruments" comprise the fair value of receivables and liabilities in respect of derivatives:

- interest rate swaps (IRS),
- currency swaps (SWAP).

3.7. Liquidity risk

Liquidity risk is a risk of the Bank being unable to finance its assets and settle its liabilities on a timely basis in the ordinary course of its activities or in other circumstances that can be predicted, without having to incur losses.

A strategic objective in managing the liquidity risk is to ensure that the Bank is able to settle its liabilities on a timely basis and to finance its stably growing assets, and to minimise the effect of that risk on the Bank's results.

The Bank manages its liquidity risk in a manner ensuring the maintenance of current, short-term, mid-term and long-term liquidity. The Bank determines the rules for identification, measurement, assessment, monitoring and reporting of the risk. As part of managing the market liquidity risk, the Bank diversifies the sources of finance mainly as part of cooperation with mBank S.A. The Bank finances its long-term assets first of all with mortgage and public covered bonds with long maturities, and it satisfies its current demand for financing on the interbank market and by issuing short-term bonds, accepting deposits from customers and handling customer current accounts.

The Bank has a contingency plan in the event of a liquidity crisis arising. The plan determines cases of crisis situations resulting in risk of liquidity loss or a new risk for managing the currency and interest rate risk, identifies sources of reserve funding for the Bank and points a general scheme of conduct for Bank in case of crisis situation.

The Bank ensures its spot and current liquidity by maintaining a liquidity portfolio which is composed of instruments that can be liquidated fast.

The current and short-term liquidity is monitored using 1-week and 1-month liquidity ratios respectively. Moreover, the Bank limits the exposure level as part of the cumulative liquidity gap in the periods of up to 1 month, 3 months, 6 months, 1 year and 2 years.

In 2013 and 2012, the Bank met all the liquidity norms introduced by the PFSA Resolution No 386/2008 of 17 December 2008:

- M1 — short-term liquidity gap,
- M2 — short-term liquidity ratio,
- M3 — the ratio of equity to non-liquid assets,
- M4 — the ratio of equity and stable borrowings to non-liquid assets and assets with limited liquidity.

The table below shows the values of liquidity norms M1–M4 as at 31 December 2013 and 31 December 2012, as well as the average and extreme values of liquidity norms:

for the year 2013 (in PLN '000)

liquidity norm	value as at 31.12.2013	average	minimum	maximum
M1	PLN 427,979 thousand	PLN 507,415 thousand	PLN 308,219 thousand	PLN 627,110 thousand
M2	1.712	2.156	1.356	4.966
M3	29.347	5.641	4.281	29.483
M4	1.079	1.083	1.045	1.130

liquidity norm	value as at 31.12.2012	average	minimum	maximum
M1	PLN 624,871 thousand	PLN 389,472 thousand	PLN 267,157 thousand	PLN 664,791 thousand
M2	1.884	1.922	1.404	3.415
M3	4.284	7.990	3.790	16.698
M4	1.073	1.052	1.011	1.097

In 2013 and 2012, the Bank did not exceed the limit for liabilities nor any of the liquidity norms.

3.7.1 Cash flows from transactions in non-derivative financial instruments

The table below shows undiscounted cash flows to be paid or received by the Bank. The cash flows have been presented as at the balance sheet date, categorised by the remaining contractual maturities. The amounts denominated in foreign currencies were converted to PLN using the average NBP rate binding as at the balance sheet date.

Liabilities (by contractual dates of maturity) as at 31 December 2013

	Up to 1 month	From 1 to 3 months	From 3 months up to 1 year	From 1 to 5 years	Over 5 years	Total
Liabilities (by contractual dates of maturity)						
Amounts due to other banks	179,681	323,484	294,191	424,504	-	1,221,860
Amounts due to customers	272,313	14,316	5,907	-	2,706	295,242
Debt securities in issue	90,512	46,062	550,798	2,009,449	212,733	2,909,554
Subordinated liabilities	-	1,533	4,600	24,651	124,651	155,435
Total liabilities	**542,506**	**385,395**	**855,496**	**2,458,604**	**340,090**	**4,582,091**
Assets (by expected dates of maturity)						
Cash and balances with the Central Bank	7,378	-	-	-	-	7,378
Amounts due from other banks	22,379	-	-	-	-	22,379
Loans and advances to customers	67,412	70,174	378,530	1,757,923	2,955,210	5,229,249
Investment securities available for sale and pledged assets	515,500	-	44,681	48,382	-	608,563
Total assets	**612,669**	**70,174**	**423,211**	**1,806,305**	**2,955,210**	**5,867,569**
Net liquidity gap	**70,163**	**(315,221)**	**(432,285)**	**(652,299)**	**2,615,120**	**1,285,478**

for the year 2013 (in PLN '000)

Liabilities (by contractual dates of maturity) as at 31 December 2012

	Up to 1 month	From 1 to 3 months	From 3 months up to 1 year	From 1 to 5 years	Over 5 years	Total
Liabilities (by contractual dates of maturity)						
Amounts due to other banks	306,161	374,715	495,620	-	-	1,176,496
Amounts due to customers	170,467	775	7,068	-	864	179,174
Debt securities in issue	121,304	134,913	802,400	2,001,424	205,894	3,265,935
Subordinated liabilities	-	1,871	5,868	31,040	138,906	177,685
Total liabilities	**597,932**	**512,274**	**1,310,956**	**2,032,464**	**345,664**	**4,799,290**
Assets (by expected dates of maturity)						
Cash and balances with the Central Bank	3,069	-	-	-	-	3,069
Amounts due from other banks	10,283	-	-	-	-	10,283
Loans and advances to customers	46,548	97,422	417,844	2,029,836	3,156,981	5,748,631
Investment securities available for sale	485,000	300	6,975	86,086	-	578,361
Total assets	**544,900**	**97,722**	**424,819**	**2,115,922**	**3,156,981**	**6,340,344**
Net liquidity gap	**(53,032)**	**(414,552)**	**(886,137)**	**83,458**	**2,811,317**	**1,541,054**

The amounts disclosed in the analysis of maturities are non-discounted contractual cash flows.

3.7.2 Cash flows from transactions in derivative financial instruments

Derivative financial instruments settled on a net basis

Derivative financial instruments settled by the Bank on a net basis include interest rate swap contracts (IRS).

The table below shows the Bank's derivative financial liabilities which will be settled on a net basis, presented by their maturity as at the balance sheet date. The amounts denominated in foreign currencies were converted to PLN using the average NBP rate binding as at the balance sheet date. The amounts disclosed in the table are non-discounted contractual cash outflows.

31.12.2013

Derivative financial instruments to be settled on a net basis	within 1 month	from 3 months to 1 year	from 1 to 5 years	over 5 years	Total
Interest rates swap contracts (IRS)	325	(1,718)	(1,164)	3,063	**506**
Total net valuation	**325**	**(1,718)**	**(1,164)**	**3,063**	**506**

31.12.2012

Derivative financial instruments settled on a net basis	From 3 months up to 1 year	Total
Interest rates swap contracts (IRS)	350	**350**
Total net valuation	**350**	**350**

Derivative financial instruments settled in gross amounts

Derivatives settled by the Bank on a gross basis include currency derivatives: SPOT and FORWARD currency SWAP contracts.

The table below shows derivative financial assets of the Bank which will be settled on a gross basis, by maturity as at the balance sheet date. Amounts in foreign currencies have been converted to PLN using the NBP exchange rate as at the balance sheet date.

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31.12.2013

Derivative financial instruments to be settled on a gross basis	within 1 month	from 1 to 3 months	from 3 months to 1 year	Total
Currency SWAP contracts				
- outflows	243,254	39,572	373,248	**656,074**
- inflows	248,241	40,606	377,412	**666,259**

31.12.2012

Derivative financial instruments to be settled on a gross basis	within 1 month	from 1 to 3 months	from 3 months to 1 year	Total
Currency SWAP contracts				
- outflows	547,819	94,029	143,087	**784,935**
- inflows	550,755	94,013	143,329	**788,097**

4. Fair value of financial assets and liabilities

The fair value is the price that would be obtained for the sale of an asset or paid for the transfer of a liability in a transaction carried out on normal commercial terms between market participants as at the measurement date, i.e. the exit price as at the measurement date from the perspective of the market participant who holds the asset or has the liability.

In accordance with market practice, the Bank measures financial instruments in respect of which it maintains open positions, using market prices (mark-to-market valuation) or valuation models recognised in practice (model valuation) which rely on market parameters and, in a limited number of cases, on parameters estimated internally by the Bank. All open positions in derivative instruments (foreign exchange and interest rate-based) are measured using the relevant market models that rely on prices or parameters observable in the market.

The key assumptions and methods used by the Bank for estimating the fair values of financial instruments are presented below:

Amounts due from other banks

The Bank has assumed that the fair value of floating interest rate deposits and fixed interest rate deposits maturing within less than 1 year is equal to their carrying amount. The Bank does not have any deposits placed for more than 1 year.

Amounts due from other banks are presented at level 3 in the fair value hierarchy.

Loans and advances to customers

The fair value of receivables from loans and advances to customers was calculated as the current value of future cash flows, using current interest rates, taking into account the credit risk margin and realistic dates of repayment under loan agreements. The levels of credit margins have been determined on the basis of market quotations of median credit margins for Moody's rating system. Credit margins were assigned to individual credit exposures by mapping Moody's rating system with the Bank's internal rating system. In order to reflect the fact that most of the Bank's exposures are secured, while the median of market quotations is largely based on unsecured issues, the Bank has made adjustments in this respect.

Investment securities available for sale

On initial recognition, they are stated at fair value of the consideration paid. Transaction costs are included in the initial cost using the effective interest rate method.
Debt securities quoted on the stock exchange or for which there is an active market are measured by the Bank at the balance sheet date at fair value (the current market price); the valuation is based on quotations at the close of business.

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Any increases in value or impairment are booked as at the valuation date, i.e. as at the end of the month, separately for each type of securities.
The Bank sells the securities of the same issuer and the same series contained in the Bank's portfolio but purchased in various periods and at various prices, using the FIFO method, according to which securities are released in the order in which they were purchased.

Financial instruments on the liabilities side are:

- bank accounts balances,
- loans received,
- subordinated loans received,
- deposits,
- liabilities in respect of covered bonds and bonds issued by the Bank.

The Bank does not have any financial instruments on the liabilities side with fixed interest rates maturing in over 1 year, except for liabilities in respect of covered bonds issued by the Bank (the issue of 26 July 2013 with a total nominal value of EUR 30,000 thousand).

The Bank has assumed that the fair value of liabilities in current accounts, loans received, subordinated loans received and deposits with floating or fixed interest rates below 1 year is equal to their carrying amount. Such liabilities are presented at level 3 in the fair value hierarchy.

Debt securities in issue (covered bonds and bonds)

The Bank has estimated the fair value of issued covered bonds and unsecured corporate bonds with a high rating using the credit spread. In the case of issued tranches subject to secondary trading, it was assumed that the value of the credit spread is the same as the value of the issue on the primary market with the same period to maturity. The clean price of individual tranches of floating covered bonds was estimated taking into account the period to redemption, the expected value of the credit spread for the issue on the secondary market and quotations from the swap curve.
Liabilities in respect of debt securities in issue are presented at level 3 in the fair value hierarchy.

The table below summarises carrying amounts and fair values for each group of financial assets and liabilities which are not presented at their fair value in the Bank's statement of financial position.

Financial assets and liabilities	31.12.2013		31.12.2012	
	Carrying value	Fair Value	Carrying value	Fair Value
Financial assets				
Cash and balances with the Central Bank	**7,378**	**7,378**	**3,069**	**3,069**
Amounts due from other banks	**22,377**	**22,377**	**10,282**	**10,282**
Loans and advances to customers, including:	**4,045,000**	**4,057,222**	**4,108,155**	**3,976,415**
Corporate customers	3,725,996	3,746,120	3,688,472	3,572,721
Individual customers	93,761	84,473	96,731	80,983
Public sector customers	225,235	226,621	322,640	322,399
Other receivables	8	8	312	312
Total financial assets	**4,074,755**	**4,086,977**	**4,121,506**	**3,989,766**
Financial liabilities				
Amounts due to other banks	**1,203,488**	**1,203,488**	**1,172,467**	**1,172,467**
Amounts due to customers, including:	**295,167**	**295,167**	**179,033**	**179,033**
Corporate customers	294,978	294,978	178,854	178,854
Individual customers	174	174	150	150
Public sector customers	15	15	29	29
Debt securities in issue	**2,661,407**	**2,649,432**	**2,852,445**	**2,861,593**
Subordinated liabilities	**100,268**	**100,268**	**100,316**	**100,316**
Total financial liabilities	**4,260,330**	**4,248,355**	**4,304,261**	**4,313,409**

for the year 2013 (in PLN '000)

Disclosures concerning the fair value hierarchy

31.12.2013	including:	Level 1	Level 2	Level 3
		Prices quoted in active markets	Valuation techniques based on observable market data	Other valuation techniques
Financial assets				
Cash and balances with the Central Bank	7,378	-	-	7,378
Amounts due from other banks	22,377	-	-	22,377
Derivative financial instruments	12,913	-	12,913	-
Interest-bearing instruments	339	-	339	-
Foreign exchange instruments	12,574	-	12,574	-
Loans and advances to customers	4,057,222	-	-	4,057,222
Investment securities available for sale, including:	605,824	90,396	515,428	-
Treasury bonds	90,396	90,396	-	-
Central Bank's bills	515,428	-	515,428	-
Total financial assets	**4,705,714**	**90,396**	**528,341**	**4,086,977**
Financial liabilities				
Amounts due to other banks	1,203,488	-	-	1,203,488
Derivative financial instruments	278	-	278	-
Interest-bearing instruments	277	-	277	-
Foreign exchange instruments	1	-	1	-
Amounts due to customers	295,167	-	-	295,167
Debt securities in issue	2,649,432	-	-	2,649,432
Subordinated liabilities	100,268	-	-	100,268
Total financial liabilities	**4,248,633**	**-**	**278**	**4,248,355**

31.12.2012	including:	Level 1	Level 2	Level 3
		Prices quoted in active markets	Valuation techniques based on observable market data	Other valuation techniques
Financial assets				
Cash and balances with the Central Bank	3,069	-	-	3,069
Amounts due from other banks	10,282	-	-	10,282
Derivative financial instruments	11,128	-	11,128	-
Interest-bearing instruments	2,413	-	2,413	-
Foreign exchange instruments	8,715	-	8,715	-
Loans and advances to customers	3,976,415	-	-	3,976,415
Investment securities available for sale, including:	566,258	81,430	484,828	-
Treasury bonds	81,132	81,132	-	-
Central Bank's bills	484,828	-	484,828	-
Treasury bills	298	298	-	-
Total financial assets	**4,567,152**	**81,430**	**495,956**	**3,989,766**
Financial liabilities				
Amounts due to other banks	1,172,467	-	-	1,172,467
Derivative financial instruments	461	-	461	-
Interest-bearing instruments	350	-	350	-
Foreign exchange instruments	111	-	111	-
Amounts due to customers	179,033	-	-	179,033
Debt securities in issue	2,861,593	-	-	2,861,593
Subordinated liabilities	100,316	-	-	100,316
Total financial liabilities	**4,313,870**	**-**	**461**	**4,313,409**

In the reporting period, there were no changes in the classification of components of the statement of financial position with respect to fair value hierarchy.

5. Major estimates and judgements made in connection with the application of accounting policy principles

The Bank makes estimates and assumptions that affect the amounts of assets and liabilities reported in the next financial period. The estimates and assumptions, which are subject to continuous assessment, are based on historical experience and other factors, including the expectations as to future events which seem justified in a given situation.

Impairment of loans and advances

The Bank reviews its loan portfolio for impairment at least on a quarterly basis. In order to determine whether impairment should be recognised in the income statement, the Bank makes judgements as to whether there is any observable data indicating that there is a measurable decrease in the estimated future cash flows from any loans. If there is objective evidence of the impairment of a loan, the amount of the loss is measured as the difference between the carrying amount of a loan and the current value of estimated future cash flows (excluding future losses on non-repaid loans that have not yet been incurred) discounted at the original effective interest rate of a loan.

If the current amount of estimated cash flows for the portfolio of loans with recognised individual impairment changed by +/- 10%, the estimated amount of the impairment of loans would decrease by PLN 13,213 thousand or increase by PLN 15,028 thousand, respectively. This estimation was performed for the portfolio of loans in the case of which impairment is recognised on the basis of a case-by-case analysis of future cash flows in respect of repayments and recoveries from collateral.

Impairment of non-financial assets — inventories

Impairment write-downs on repossessed properties are calculated on a semi-annual and annual basis. The calculation of impairment involves comparing the selling prices of properties (apartments) in the last six months/year with the prices of such properties (apartments) as at the date of purchase. Loss on sale is a prerequisite for estimating the impairment of property values for the entire population.

Deferred income tax assets

The Bank capitalises the value of impairment write-downs on loans whose non-recoverability will be documented in deferred tax. The Bank capitalises impairments write-downs on loans in the event of estimating the most likely scenario will entail documenting non-recoverability in accordance with applicable tax laws as a result of undertaken debt collection activities.

Liabilities in respect of post-employment benefits

The expenses relating to post-employment benefits are determined using the actuarial valuation method. Actuarial valuation requires making assumptions about discount rates, future salary increases, mortality rates and other factors. Due to the long-term nature of these liabilities, such estimates are burdened with a high degree of uncertainty.

Phantom share-based benefits

The Bank runs a remuneration program for the Management Board and employees having a significant impact on the risk profile of the Bank based on phantom shares settled in cash.

The structure of the Programme is described in Note 2.17.

In accordance with IAS 19, the present value of liabilities under other long-term employee benefits has been determined using the projected unit credit method.

The basis for the calculation of the provision for the deferred portion of variable remuneration for eligible employees of the Bank, is the amount of the premium that the Bank is obligated to pay pursuant to the Regulations on the variable remuneration of the Management Board Members of mBank Hipoteczny S.A. and the Regulations on the variable remuneration of the employees with a material impact on the risk profile of the Bank, for the First, Second, Third and Fourth Assessment Period corresponding to 2012, 2012–2013, 2012–2014 and 2013–2015, respectively.

The final value of the premium, which is a product of the number of shares and their estimated value as at the balance sheet date preceding the realisation of each of the deferred tranches is subject to actuarial discounting at the reporting date. The discounted amount is reduced by amounts of allocations to the relevant provision, which are subject to actuarial discounting at the same date. The actuarial discount is the product of the financial discount and the probability of each of the participants individually reaching the moment of obtaining full entitlement to each of the deferred tranches.

Annual allocations are calculated according to the projected unit credit method.

The aforementioned probability was determined using the Multiple Decrement Model, where the following three risks were taken into account: the possibility of dismissal, the risk of total incapacity for work, the risk of death.

The value of the provision for the deferred portion of variable remuneration as at 31 December 2013 amounts to PLN 250 thousand, whereas as at 31 December 2012 it amounted to PLN 318 thousand.

The fair value of financial instruments

The fair value of financial instruments not quoted on active markets is determined using valuation techniques. All the models are approved prior to application and they are also calibrated in order to assure that the obtained results indeed reflect the actual data and comparable market prices. As far as possible, observable market data originating from an active market are used in the models.

6. Operating segments

Following the management approach, operating segments are reported in accordance with the internal reporting provided to the Bank's Management Board (the chief operating decision-maker), which is responsible for allocating resources to the reportable segments and assesses their performance.

mBank Hipoteczny S.A. is a specialist mortgage bank and it plays a leading role in the market of commercial real estate financing and issuing covered bonds. The Bank's offer is addressed to corporate and institutional clients investing in buying, building or renovating commercial properties, such as offices, malls, hotels, warehouses, as well as apartments and houses, carried out by housing developers. Another important area of activity of the Bank is lending money to local government units in the form of financing of investments such as municipal housing, road construction and repairs, construction of sewage treatment plants, educational facilities and other facilities, as well as the refinancing of municipal real estate — seats of local governments, utility premises, office buildings. In 2013, the Bank extended the scope of its business to include retail loans (loans to individuals — agency model). The Bank is also a leader in the issue of covered bonds, debt securities which refinance its credit activity.

Taking into consideration the specialist business profile of the Bank, the following operating segments were separated:

- loans for refinancing,
- loans to local government units (JST),
- loans to housing real estate developers,
- loans to commercial real estate developers,
- loans for land purchase,
- Loans to individual customers.
- Loans to individual customers — agency model.

The segments were identified taking into account specific customer and product groups on the basis of homogeneous transaction characteristics. The classification is consistent with sales management.

Loans for refinancing — this is a major segment of the Bank's activities, which comprises loans for refinancing or purchase of existing commercial properties (office buildings, warehouses, shopping centres, logistics centres, hotels, guest houses, commercial premises, etc.).

Loans to local government units (JST) — this segment comprises loans to local government units (municipalities, districts, provinces) as well as loans guaranteed by local government units (commercial companies established by local governments, public health care institutions).

Loans to housing real estate developers — this segment comprises loans for the financing of housing development projects (estates with single/multi-family houses for sale or rent).

Loans to commercial real estate developers — this segment comprises loans for the financing of commercial real estate projects that are consistent with the Bank's crediting policy.

Loans for land purchase — this segment comprises loans for financing and refinancing the purchase of land for housing real estate development projects.

Loans to individual customers — this segment comprises loans granted to individuals, mainly for housing purposes. The segment is in decline due to the discontinuation of sales in the segment since 2004.

Loans to individual customers — agency model — this segment comprises loans granted to individuals for housing purposes. Loans are offered in PLN and secured by a mortgage. Loans are sold under an agency agreement through the network of mBank S.A. branches. Loans are recognised in the books of mBank Hipoteczny S.A.

Non–allocated items — this position comprises all assets other than credits and loans.

On the basis of the above product segmentation, the profit before tax, including all profit and loss positions, is determined for each individual operating segment separately.

The main purpose of profit and loss segmentation is to present the profitability of each individual segment of Bank's operations as closely as possible. In order to achieve this, the Bank assigns all direct income such as interest income, fee and commission income as well as impairment write-downs at the loan agreement level. Due to the fact that the Bank cannot assign its liabilities to appropriate operating segments at the transaction level, the interest costs as well as fee and commission costs are attributed using a scheme described below.

The Bank's refinancing costs are divided into three categories: costs of public covered bonds, costs of mortgage covered bonds and average cost of other refinancing sources (mostly loans and deposits obtained from mBank S.A.). For each category an average refinancing cost is calculated on basis of margin of each liability in a given category.

The interest and fee and commission costs for loans to local government units segment is calculated on the basis of actual refinancing costs of public covered bonds and part of average cost of other refinancing sources that is attributable to this segment (proportionally to the liabilities refinancing the surplus of JST loans over the value of the covered bonds issued).

The interest and fee and commission expense for other segments is calculated on the basis of actual refinancing costs of mortgage covered bonds and average cost of other refinancing sources that are attributable to the segment, proportionally to the share of segment loans in all loans portfolio (excluding JST loans).

Remaining income statement items are divided between the segments on the basis of the share of segment loans in all loans portfolio, or share of risk weighted assets of segment in all risk weighted assets in case of depreciation and bank overheads. The Bank does not allocate the income tax charge to individual segments, accordingly the operating segments profit/loss data is presented on profit before income tax level. Data concerning operating segments is measured according to the same principles as those disclosed in the accounting policy.

The division into operating segments described above is the main and only segmentation of Bank's operations. Taking into consideration the fact that the Bank operates only within the territory of the Republic of Poland, the Bank does not use geographic segmentation.

There are no operations between the segments within the Bank.

The segmentation of assets and profit and loss has been made using the information that Bank uses for controlling and management purposes. Assets and income and costs attributable to these assets have been assigned to individual segments. The segment results include all profit and loss positions. Liabilities have not been allocated to individual segments, as it is not presented to the chief operating decision-maker on a regular basis.

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Period from 01.01.2013 to 31.12.2013	Loans for refinancing commercial real estates	Loans to local government units	Loans to housing real estate developers	Loans to commercial real estate developers	Loan for land purchase	Loans to individuals	Loans to individuals — agency model	Total	Income statement
Interest income	136,727	29,264	39,430	12,824	6,728	2,001	91	227,065	227,065
Interest expense	(78,365)	(29,630)	(27,938)	(9,668)	(3,938)	(2,401)	(346)	(152,286)	(152,286)
Net interest income	**58,362**	**(366)**	**11,492**	**3,156**	**2,790**	**(400)**	**(255)**	**74,779**	**74,779**
Fee and commission income	3,248	458	845	607	65	48	6	5,277	5,277
Fee and commission expense	(1,041)	(184)	(187)	(127)	(26)	(16)	(3)	(1,584)	(1,584)
Net impairment write-downs on loans and advances	(28,833)	25	(4,414)	(400)	(462)	(782)	-	(34,866)	(34,866)
Depreciation and bank overheads	(31,408)	(1,156)	(5,663)	(3,878)	(793)	(397)	(56)	(43,351)	(43,351)
Other income statement items	3,363	124	607	415	85	42	6	4,642	4,642
Segment result (before tax)	**3,691**	**(1,099)**	**2,680**	**(227)**	**1,659**	**(1,505)**	**(302)**	**4,897**	**4,897**

31.12.2013	Loans for refinancing commercial real estates	Loans to local government units	Loans to housing real estate developers	Loans to commercial real estate developers	Loan for land purchase	Loans to individuals	Loans to individuals — agency model	Non-allocated assets items	Total	Statement of financial position
Loans and advances to customers	**2,646,903**	**479,491**	**477,789**	**327,193**	**66,947**	**40,573**	**6,096**	**8**	**4,045,000**	**4,045,000**
Other assets	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**737,443**	**737,443**	**737,443**
Segment assets	**2,646,903**	**479,491**	**477,789**	**327,193**	**66,947**	**40,573**	**6,096**	**737,451**	**4,782,443**	**4,782,443**

Profit before tax for the Bank's operating segments has been presented in line with the income statement, prepared for the purpose of the audited financial statements.

for the year 2013 (in PLN '000)

Period from 01.01.2012 to 31.12.2012, restated data	Loans for refinancing commercial real estates	Loans to local government units	Loans to housing real estate developers	Loans to commercial real estate developers	Loan for land purchase	Loans to individuals	Total	Income statement
Interest income	153,233	40,394	48,543	18,734	11,821	2,567	275,292	275,292
Interest expense	(95,936)	(41,189)	(33,897)	(16,948)	(6,806)	(3,358)	(198,134)	(198,134)
Net interest income	**57,297**	**(795)**	**14,646**	**1,786**	**5,015**	**(791)**	**77,158**	**77,158**
Fee and commission income	3,070	592	896	721	100	53	5,432	5,432
Fee and commission expense	(1,037)	(223)	(186)	(146)	(37)	(18)	(1,647)	(1,647)
Net impairment write-downs on loans and advances	(24,321)	(3)	(444)	(473)	(1,275)	256	(26,260)	(26,260)
Depreciation and bank overheads	(28,587)	(1,340)	(5,151)	(4,042)	(1,076)	(419)	(40,615)	(40,615)
Other income statement items	22	1	4	3	1	-	31	31
Segment result (before tax)	**6,444**	**(1,768)**	**9,765**	**(2,151)**	**2,728**	**(919)**	**14,099**	**14,099**

31.12.2012	Loans for refinancing commercial real estates	Loans to local government units	Loans to housing real estate developers	Loans to commercial real estate developers	Loan for land purchase	Loans to individu als	Non-allocated assets items	Total	Statement of financial position
Loans and advances to customers	**2,575,103**	**561,883**	**463,978**	**364,101**	**96,929**	**45,849**	**312**	**4,108,155**	**4,108,155**
Other assets	**-**	**-**	**-**	**-**	**-**	**-**	**701,557**	**701,557**	**701,557**
Segment assets	**2,575,103**	**561,883**	**463,978**	**364,101**	**96,929**	**45,849**	**701,869**	**4,809,712**	**4,809,712**

Profit before tax for the Bank's operating segments has been presented in line with the income statement, prepared for the purpose of the audited financial statements.

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7. Net interest income

	Year ended 31 December	
	2013	**2012 restated data**
Interest income		
Loans and advances, including the unwind of discount relating to impairment write-down, of which:	182,677	224,261
- interest income on impaired loans and advances	10,426	11,025
Cash and short-term deposits	518	741
Investment securities	17,687	17,216
Interest income on derivatives classified into banking book	26,183	33,074
Total interest income	**227,065**	**275,292**

	Year ended 31 December	
	2013	**2012 restated data**
Interest expense		
Due to settlements with banks	(14,740)	(23,944)
Due to settlements with customers	(2,049)	(3,593)
Due to the issue of debt securities	(128,776)	(164,026)
Due to subordinated loan	(6,721)	(6,571)
Total interest expense	**(152,286)**	**(198,134)**
Total net interest income	**74,779**	**77,158**

Net interest income broken down into individual sectors is as follows:

	Year ended 31 December	
	2013	**2012 restated data**
Interest income		
From the banking sector	40,402	46,263
From other entities, including:	186,663	229,029
- from corporate customers	166,823	198,849
- from individual customers	3,902	5,107
- from the public sector	15,938	25,073
Total interest income	**227,065**	**275,292**

Interest income generated on monetary bills is presented in the item *Interest income from the banking sector*, whereas interest income from treasury bills and bonds in the item *Interest income from the public sector*.

	Year ended 31 December	
	2013	**2012 restated data**
Interest expense		
From the banking sector	(21,461)	(30,515)
From other entities, including:	(2,049)	(3,593)
- from corporate customers	(2,049)	(3,593)
From own issuances	(128,776)	(164,026)
Total interest expense	**(152,286)**	**(198,134)**

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8. Net fee and commission income and expense

	Year ended 31 December	
	2013	2012 restated data
Fee and commission income		
Credit-related fees and commissions	4,909	5,036
Commissions from bank accounts	330	352
Commissions from money transfers	38	44
Total fee and commission income	**5,277**	**5,432**
Fee and commission expense		
Costs related to the debt instrument's issue program (covered bonds and bonds)	(982)	(1,112)
Other	(602)	(535)
Total fee and commission expense	**(1,584)**	**(1,647)**
Total net fee and commission income	**3,693**	**3,785**

9. Net trading income

	Year ended 31 December	
	2013	2012 restated data
Foreign exchange result	**4,186**	**2,278**
Net exchange differences on translation	(2,471)	(6,331)
Valuation of foreign currency derivatives	6,657	8,609
Other net trading income	**(1,001)**	**836**
Interest rate risk instruments	(1,001)	836
Total net trading income	**3,185**	**3,114**

Foreign exchange result covers realised and unrealised, positive and negative exchange rate differences, as well as valuation of FX SWAP derivatives, whereas the result on other net trading activities includes the effects of changes in the fair value of IRS derivatives.

10. Other operating income

	Year ended 31 December	
	2013	2012
Profit from the sales of inventories	5,658	-
Revenue from sales of receivables	841	-
Income from sales of services	470	612
Income from the release of the provisions for bonuses and legal proceedings	170	-
Income from recovering receivables designated previously as prescribed, remitted or uncollectible	51	29
Other	107	33
Total other operating income	**7,297**	**674**

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On 2 December 2013, the Bank entered into an agreement for the sale of receivables which had been written off. A result of this transaction, the Bank recognised income in the amount of PLN 841 thousand, presented in other operating income.

The profit from the sales of inventories results from the conclusion of an agreement for the sale of properties repossessed in 2012:

- a sale agreement dated 12 December 2013, concluded with BDH Development Sp. z o.o. for a total gross amount of PLN 48,462 thousand, i.e. PLN 39,400 thousand net, with the value of the property in the Bank's books of PLN 35,145 thousand and an accounting profit on the transaction of PLN 4,255 thousand.
- a sale agreement dated 23 December 2013, concluded with BDH Development Sp. z o.o. for a total gross amount of PLN 22,784 thousand, i.e. PLN 18,524 thousand net, with the value of the property in the Bank's books of PLN 17,760 thousand, income from the reversal of an impairment write-down on the property of PLN 640 thousand and an accounting profit on the transaction of PLN 1,403 thousand.

11. Net impairment write-downs on loans and advances

	Year ended 31 December	
	2013	**2012**
Establishment of write-downs on loans and advances to customers (Note 21)	(45,974)	(39,695)
Reversal of write-downs on loans and advances to customers (Note 21)	11,108	13,435
Total net impairment write-downs on loans and advances	**(34,866)**	**(26,260)**

12. Overhead costs

	Year ended 31 December	
	2013	**2012**
Staff-related expenses	(22,832)	(21,652)
Material costs	(14,211)	(11,963)
Contribution and payments to the Bank Guarantee Fund	(1,726)	(1,849)
Taxes and fees	(267)	(1,034)
Contributions to the Social Benefits Fund	(153)	(369)
Total Bank overheads	**(39,189)**	**(36,867)**

The item "Material costs" comprises, inter alia, the cost of instalments related to the operating lease of premises and equipment (the lease of real estate).

Staff-related expenses

	Year ended 31 December	
	2013	**2012**
Wages and salaries	(18,870)	(17,941)
Social security expenses	(2,317)	(1,939)
Costs of pension benefits	(15)	(47)
Provision for unused employee leaves	(303)	(432)
Costs of long-term employee benefits	(127)	(318)
Other employee benefits	(1,200)	(975)
Total staff-related expenses	**(22,832)**	**(21,652)**

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In 2013, the average number of employees was 144 (in 2012: 128).

The long-term employee benefits are associated with the costs of the programme for variable remuneration for Bank's Management Board and employees having a material impact on the risk profile of the Bank. Long-term employee benefits are described in note 2.17.

13. Other operating expenses

	Year ended 31 December	
	2013	**2012**
Loss on the sales of assets repossessed for debts (inventories) and costs of their maintenance	(5,327)	(1,303)
Inventories revaluation write-downs	(129)	(1,733)
Costs of execution proceedings	(392)	(352)
Provision for legal proceedings	-	(189)
Loss on the sales or liquidation of fixed assets and intangible assets	(19)	(90)
Compensations for damages, penalties and fines paid	(1)	(13)
Donations made	(5)	(5)
Other	(30)	(72)
Total other operating expenses	**(5,903)**	**(3,757)**

The item "Loss on the sales of assets repossessed for debts (inventories) and costs of their maintenance" comprises:

- the result on the sale of properties repossessed in 2012 and 2011 and related maintenance costs until the date of sale of the entire property totalling PLN (2,409) thousand,
- loss on the sale of two properties referred to in Note 3.2.7 totalling PLN (2,918) thousand.

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14. Income tax expense

	Year ended 31 December	
	2013	**2012**
Current income tax	(5,631)	(7,171)
Deferred income tax (Note 32)	2,888	2,359
Total income tax	**(2,743)**	**(4,812)**

Profit before income tax	**4,897**	**14,099**
Income tax calculated at the rate applicable in a given fiscal year (19%)	(930)	(2,679)
Non-taxable income	607	2,110
Non-deductible tax costs	(2,443)	(4,243)
- the value of write-downs on receivables	(1,926)	(3,715)
- increase in the value of a repossessed property to fair value	(427)	-
- other	(90)	(528)
Adjustments in respect of current tax from prior years	23	-
Total income tax expense	**(2,743)**	**(4,812)**

Effective tax rate calculation		
Profit before income tax	4,897	14,099
Income tax expense	(2,743)	(4,812)
Effective tax rate	**56.01%**	**34.13%**
Nominal tax rate	**19.00%**	**19.00%**

The item "Non-taxable income" comprises mainly the value of written-off interest from previous years on loans written-off in the amount of PLN 567 thousand for 2013 and PLN 2,099 thousand for 2012.

Tax authorities may inspect the correctness of tax settlements over a period of 5 years from the end of the year in which the deadline for submitting a tax return had expired. Since the beginning of the Bank's operations, no tax inspections were carried out by the tax authorities with regards to corporate income tax.

In 2013, a tax inspection with regards to VAT for June 2013 was carried out by the Tax Office.

15. Profit per share

	Year ended 31 December	
	2013	**2012**
Net profit attributable to shareholders of mBank Hipoteczny S.A.	2,154	9,287
Weighted average number of ordinary shares	2,750	1,857
Basic net profit per share (in PLN per share)	**0.78**	**5.00**
Diluted:		
Net profit attributable to shareholders of mBank Hipoteczny S.A., applied during the estimation of diluted profit per share	2,154	9,287
Weighted average number of ordinary shares for diluted profit per share	2,750	1,857
Diluted net profit per share (in PLN per share)	**0.78**	**5.00**

Basic earnings per share are computed as the quotient of the profit attributable to the Bank's shareholders and the weighted average number of ordinary shares during the year.

Diluted earnings per share are equal to basic earnings per share, as there are no dilutive elements.

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The weighted average number of ordinary shares outstanding during the period is the number of ordinary shares at the beginning of the period, adjusted by the number of ordinary shares redeemed or issued during the period multiplied by a time-weighting factor. The time-weighting factor is the number of days that the shares are outstanding as a proportion of the total number of days in the period.

16. Disclosures concerning the tax effect of other comprehensive income components

	Year ended 31 December	
	2013	**2012**
Items that may be reclassified to the income statement	**(931)**	**2,232**
Available-for-sale financial assets:	(931)	2,232
- gross amount	(1,149)	2,755
- deferred tax	218	(523)
Items that will not be reclassified to the income statement	**35**	**-**
Actuarial gains and losses on post-employment benefits	35	-
- gross amount	43	-
- deferred tax	(8)	-
Other comprehensive income, net	**(896)**	**2,232**

17. Disclosures concerning the components of other comprehensive income

	Year ended 31 December	
	2013	**2012**
Items that may be reclassified to the income statement	**(931)**	**2,232**
Available-for-sale financial assets:	(931)	2,232
- unrealised gains on debt instruments recognised in the financial year (net)	-	2,232
- unrealised losses on debt instruments recognised in the financial year (net)	(931)	-
Items that will not be reclassified to the income statement	**35**	**-**
Actuarial gains and losses on post-employment benefits (net)	35	-
Other comprehensive income, net	**(896)**	**2,232**

18. Cash and transactions with the Central Bank

The Bank has a current account with the National Bank of Poland, with a balance amounting to PLN 7,378 thousand as at 31 December 2013. As at 31 December 2012, the Bank maintained PLN 3,069 thousand in the current account. On the basis of the National Bank of Poland Act dated 29 August 1997, mBank Hipoteczny S.A. maintains a mandatory reserve deposit. The arithmetic mean of daily balances of the mandatory reserve which the Bank is required to maintain during a given period in the current account with NBP amounted to:

- PLN 5,883 thousand for the period from 31 December 2013 to 30 January 2014,
- PLN 2,053 thousand for the period from 31 December 2012 to 30 January 2013.

As at 31 December 2013, the interest rate on the cash maintained as a mandatory reserve was 2.475%, as compared to 4.05% as at 31 December 2012.

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19. Amounts due from other banks

	31.12.2013	31.12.2012
Placements with other banks (overnight deposits)	22,001	10,001
Current accounts	376	281
Included in cash equivalents	**22,377**	**10,282**
Total (gross) amounts due from other banks	**22,377**	**10,282**
Total (net) amounts due from other banks	**22,377**	**10,282**
Short-term amounts due from other banks (up to 1 year)	22,377	10,282

All amounts due were due from Polish banks.

In 2013, the average amount-weighted interest rates on placements with other banks were as follows: EUR — 0.05%, PLN — 2.57%. In 2012: EUR — 0.20%, PLN — 4.40%.

20. Derivative financial instruments

	Base contract value	Fair value of asset	Fair value of liability
As at 31 December 2013			
Derivative financial instruments held for trading			
Foreign exchange derivatives			
- FX swap contracts	656,073	12,573	-
Total foreign exchange derivatives	**656,073**	**12,573**	-
Interest rate derivatives			
- IRS contracts	331,776	340	278
Total interest rate derivatives	**331,776**	**340**	**278**
Total derivative assets/liabilities recognised	**987,849**	**12,913**	**278**
Short-term (up to 1 year)	863,433	12,913	9
Long-term (more than 1 year)	124,416	-	269

	Base contract value	Fair value of asset	Fair value of liability
As at 31 December 2012			
Derivative financial instruments held for trading			
Foreign exchange derivatives			
- FX swap contracts	784,934	8,715	111
Total foreign exchange derivatives	**784,934**	**8,715**	111
Interest rate derivatives			
- IRS contracts	488,176	2,413	350
Total interest rate derivatives	**488,176**	**2,413**	**350**
Total derivative assets/liabilities recognised	**1,273,110**	**11,128**	**461**
Short-term (up to 1 year)	1,273,110	11,128	461
Long-term (more than 1 year)	-	-	-

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21. Loans and advances to customers

	31.12.2013	31.12.2012
Loans and advances to corporate customers	**3,799,524**	**3,733,408**
Loans and advances to individual customers	**95,754**	**97,944**
Loans and advances to the public sector	**225,302**	**322,737**
Other receivables	**8**	**312**
Loans and advances from customers (gross)	**4,120,588**	**4,154,401**
Impairment write-downs on loan and advances to customers (negative amount)	(75,588)	(46,246)
Loans and advances from customers (net)	**4,045,000**	**4,108,155**
Short-term (up to 1 year)	406,311	432,294
Long-term (more than 1 year)	3,638,689	3,675,861

As at 31 December 2013, the gross value of loans to individual customers, corporate customers and the public sector in the Bank's loan portfolio, carrying floating interest rates, amounted to PLN 4,119,463 thousand, and the gross value of loans carrying fixed interest rates amounted to PLN 1,117 thousand. As at 31 December 2012, the value of loans carrying floating interest rates amounted to PLN 4,141,448 thousand, and the value of loans carrying fixed interest rates amounted to PLN 12,641 thousand.

Impairment write-downs on loans and advances

	31.12.2013	31.12.2012
Incurred but not identified losses		
Gross balance sheet exposure	3,901,923	3,977,296
Impairment write-downs on exposures analysed on a portfolio basis	(7,205)	(6,455)
Net balance sheet exposure	**3,894,718**	**3,970,841**
Impaired receivables		
Corporate customers	212,864	171,100
Individual customers	5,801	6,005
Total gross balance sheet exposure	218,665	177,105
Impairment write-down on exposures analysed on a case-by-case basis	(68,383)	(39,791)
Net balance sheet exposure	**150,282**	**137,314**

Movements in impairment write-downs on loans and advances

	Impairment write-downs as at 01.01.2013	Write-downs created	Reversal of write-downs	Loans written-off	Impairment write-downs as at 31.12.2013
Individual customers	(1,213)	(1,620)	840	-	(1,993)
Corporate customers	(44,936)	(44,341)	10,225	5,524	(73,528)
Public sector customers	(97)	(13)	43	-	(67)
Total movements in impairment write-downs on loans and advances	(46,246)	(45,974)	11,108	5,524	(75,588)

	Impairment write-downs as at 01.01.2012	Write-downs created	Reversal of write-downs	Loans written-off	Impairment write-downs as at 31.12.2012
Individual customers	(1,442)	(563)	792	-	(1,213)
Corporate customers	(30,839)	(39,129)	12,627	12,405	(44,936)
Public sector customers	(110)	(3)	16	-	(97)
Total movements in impairment write-downs on loans and advances	(32,391)	(39,695)	13,435	12,405	(46,246)

Write-offs on receivables affect the Bank's results, if such receivables were previously included in deferred tax. Reversal of deferred tax liabilities results in a reduction of the tax expense.

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22. Investment securities

	31.12.2013	31.12.2012
Debt securities stated at fair value	**605,824**	**566,258**
Quoted, including:	605,824	566,258
- pledged Central Bank's bills (BFG)	1,500	1,000
- pledged treasury bills (BFG)	-	298
Total investment securities, including:	**605,824**	**566,258**
- Central Bank's bills	515,428	484,828
- treasury bills	-	298
- treasury bonds	90,396	81,132
Short-term (up to 1 year)	557,433	487,963
Long-term (more than 1 year)	48,391	78,295

The Bank had no debt securities based on floating interest rates.

Pledged assets are not subject to resale or further pledging.

Movements in investment securities and pledged assets

	31.12.2013	31.12.2012
Investment securities and pledged assets		
As at the beginning of the period	**566,258**	**306,748**
Increase	23,617,741	14,066,967
Decrease	(23,577,026)	(13,810,212)
Gains/losses on changes in fair value	(1,149)	2,755
As at the end of the period	**605,824**	**566,258**

23. Investments in subsidiaries

As at 31 December 2013, the Bank did not have any subsidiaries. Until 28 November 2013, mBank Hipoteczny S.A. had one subsidiary — Bankowy Dom Hipoteczny Spółka z ograniczoną odpowiedzialnością (BDH) — which was formed on 8 March 2005 as a special purpose vehicle of mBank Hipoteczny S.A. The Bank held 100% of shares in BDH and 100% of the total votes at the General Shareholders' Meeting.

As at 31 December 2012, the share capital of BDH amounted to PLN 65 thousand and consisted of 65 shares with a par value of PLN 1 thousand each. All of the Bank's shares in the share capital of BDH had been paid up.

Pursuant to Resolution No 13/2013 of the Management Board of mBank Hipoteczny S.A. dated 12 March 2013, a capital contribution was made to BDH in the amount of PLN 650 thousand. The capital contribution was recognised in the Bank's books as an increase in the number of shares in BDH. Until 28 November 2013, the value of BH shares in the Bank's books was PLN 715 thousand.

On 26 November 2013, the District Court for the Capital City of Warsaw, 12^{th} Commercial Division of the National Court Register, registered a new name of Bankowy Dom Hipoteczny Sp. z o.o. As of 26 November 2013, the company operates under the name of BDH Development Spółka z ograniczoną odpowiedzialnością.
On 28 November 2013, mBank Hipoteczny S.A. and mBank S.A. concluded an agreement, whereby all of the shares in the share capital BDH Development Spółka z ograniczoną odpowiedzialnością were sold. The shares were sold for PLN 778 thousand. The profit from the sale of shares in BDH Development Spółka z ograniczoną odpowiedzialnością, amounting to PLN 63 thousand, has been presented in the income statement under "Net income on investments in subsidiaries".

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24. Intangible assets

	31.12.2013	31.12.2012
Concessions, patents, licences and similar items, including:	1,970	1,384
- computer software	1,970	1,384
Costs of completed development projects	-	-
Intangible assets under development	1,578	-
Total intangible assets	**3,548**	**1,384**

Movements in intangible assets

Movements in the period from 01.01.2013 to 31.12.2013	Acquired computer software	Costs of completed development projects	Intangible assets under development	Total
Gross value of intangible assets as at the beginning of the period: 01.01.2013	**9,483**	**185**	**-**	**9,668**
Increase (due to)	**1,314**	**-**	**2,010**	**3,324**
- purchase	882	-	2,010	2,892
- transfer from intangible assets under development	432	-	-	432
Decrease (due to)	**-**	**-**	**(432)**	**(432)**
- transfer from intangible assets under development	-	-	(432)	(432)
Gross value of intangible assets as at the end of the period: 31.12.2013	**10,797**	**185**	**1,578**	**12,560**
Accumulated amortisation (depreciation) as at the beginning of the period: 01.01.2013	**(8,099)**	**(185)**	**-**	**(8,284)**
Amortisation for the period (due to):	**(728)**	**-**	**-**	**(728)**
- amortisation charges	(728)	-	-	(728)
Accumulated amortisation (depreciation) as at the end of the period: 31.12.2013	**(8,827)**	**(185)**	**-**	**(9,012)**
Net book value of intangible assets as at the end of the period: 31.12.2013	**1,970**	**-**	**1,578**	**3,548**

Movements in the period from 01.01.2012 to 31.12.2012	Acquired computer software	Costs of completed development projects	Intangible assets under development	Total
Gross value of intangible assets as at the beginning of the period: 01.01.2012	**9,344**	**185**	**-**	**9,529**
Increase (due to)	**139**	**-**	**103**	**242**
- purchase	36	-	103	139
- transfer from intangible assets under development	103	-	-	103
Decrease (due to)	**-**	**-**	**(103)**	**(103)**
- transfer from intangible assets under development	-	-	(103)	(103)
Gross value of intangible assets as at the end of the period: 31.12.2012	**9,483**	**185**	**-**	**9,668**
Accumulated amortisation (depreciation) as at the beginning of the period: 01.01.2012	**(7,327)**	**(154)**	**-**	**(7,481)**
Amortisation for the period (due to):	**(772)**	**(31)**	**-**	**(803)**
- amortisation charges	(772)	(31)	-	(803)
Accumulated amortisation (depreciation) as at the end of the period: 31.12.2012	**(8,099)**	**(185)**	**-**	**(8,284)**
Net book value of intangible assets as at the end of the period: 31.12.2012	**1,384**	**-**	**-**	**1,384**

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25. Tangible fixed assets

	31.12.2013	31.12.2012
Technical equipment and machinery	6,599	6,467
Vehicles	978	1,389
Fixed assets under construction	390	-
Other fixed assets	1,143	1,315
Total tangible fixed assets	**9,110**	**9,171**

Movements in tangible fixed assets

Movements in the period from 01.01.2013 to 31.12.2013	Equipment	Vehicles	Other fixed assets	Fixed assets under construction	Total
Gross value of tangible fixed assets as at the beginning of the period: 01.01.2013	**16,219**	**2,529**	**5,897**	**-**	**24,645**
Increase (due to)	**2,615**	**-**	**405**	**1,634**	**4,654**
- purchase	1,371	-	405	1,634	3,410
- transfer from fixed assets under construction	1,244	-	-	-	1,244
Decrease (due to)	**(716)**	**(72)**	**(1,135)**	**(1,244)**	**(3,167)**
- sale	-	(72)	-	-	(72)
- scrapping	(716)	-	(1,135)	-	(1,851)
- transfer from fixed assets under construction	-	-	-	(1,244)	(1,244)
Gross value of tangible fixed assets as at the end of the period: 31.12.2013	**18,118**	**2,457**	**5,167**	**390**	**26,132**
Accumulated amortisation (depreciation) as at the beginning of the period: 01.01.2013	**(9,752)**	**(1,140)**	**(4,582)**	**-**	**(15,474)**
Amortisation for the period (due to):	**(1,767)**	**(339)**	**558**	**-**	**(1,548)**
- amortisation charges	(2,466)	(392)	(576)	-	(3,434)
- sale	-	53	-	-	53
- scrapping	699	-	1,134	-	1,833
Accumulated amortisation (depreciation) as at the end of the period: 31.12.2013	**(11,519)**	**(1,479)**	**(4,024)**	**-**	**(17,022)**
Net value of tangible fixed assets as at the end of the period: 31.12.2013	**6,599**	**978**	**1,143**	**390**	**9,110**

Movements in the period from 01.01.2012 to 31.12.2012	Equipment	Vehicles	Other fixed assets	Fixed assets under construction	Total
Gross value of tangible fixed assets as at the beginning of the period: 01.01.2012	**14,555**	**2,381**	**5,684**	**-**	**22,620**
Increase (due to)	**2,444**	**377**	**392**	**1,935**	**5,148**
- purchase	509	377	392	1,935	3,213
- transfer from fixed assets under construction	1,935	-	-	-	1,935
Decrease (due to)	**(780)**	**(229)**	**(179)**	**(1,935)**	**(3,123)**
- sale	-	(229)	-	-	(229)
- scrapping	(780)	-	(179)	-	(959)
- transfer from fixed assets under construction	-	-	-	(1,935)	(1,935)
Gross value of tangible fixed assets as at the end of the period: 31.12.2012	**16,219**	**2,529**	**5,897**	**-**	**24,645**
Accumulated amortisation (depreciation) as at the beginning of the period: 01.01.2012	**(8,456)**	**(841)**	**(4,240)**	**-**	**(13,537)**
Amortisation for the period (due to):	**(1,296)**	**(299)**	**(342)**	**-**	**(1,937)**
- amortisation charges	(2,046)	(408)	(491)	-	(2,945)
- sale	-	109	-	-	109
- scrapping	750	-	149	-	899
Accumulated amortisation (depreciation) as at the end of the period: 31.12.2012	**(9,752)**	**(1,140)**	**(4,582)**	**-**	**(15,474)**
Net value of tangible fixed assets as at the end of the period: 31.12.2012	**6,467**	**1,389**	**1,315**	**-**	**9,171**

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26. Other assets

	31.12.2013	31.12.2012
Other, including:	**62,615**	**90,240**
- receivables from the sale of inventories	52,761	-
- inventories	8,192	89,073
- other prepayments	725	683
- income receivable	313	127
- other	624	357
Total other assets	**62,615**	**90,240**
Short-term (up to 1 year)	62,615	90,240
Long-term (more than 1 year)	-	-

Inventories consist of repossessed assets, as described in the note 3.2.7.

27. Amounts due to other banks

	31.12.2013	31.12.2012
Term deposits (including overnight deposits)	787,862	1,049,799
Loans received	415,626	122,668
Total amounts due to other banks	**1,203,488**	**1,172,467**
Short-term (up to 1 year)	788,768	1,172,467
Long-term (more than 1 year)	414,720	-
Fixed rate deposits	787,862	1,049,799

All loans received are based on floating interest rates.
In 2013, the average amount-weighted interest rates on term deposits were as follows: EUR — 0.37%, PLN — 2.73%, USD — 0.49%, In 2012: EUR — 0.89%, PLN — 4.52%, USD — 0.50%.

mBank Hipoteczny S.A. did not provide any collateral to its lenders. The Bank did not register any violations of contractual terms related to liabilities in respect of loans taken out.

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28. Amounts due to customers

	31.12.2013	31.12.2012
Corporate customers:	**294,978**	**178,854**
Cash in current accounts	226,551	123,265
Term deposits (including overnight deposits)	64,633	54,354
Other liabilities (in respect of):	3,794	1,235
- liabilities in respect of cash collateral	2,169	475
- other	1,625	760
Individual customers:	**174**	**150**
Other liabilities (in respect of):	174	150
- liabilities in respect of cash collateral	65	65
- other	109	85
Public sector customers:	**15**	**29**
Other liabilities (in respect of):	15	29
- other	15	29
Total amounts due to customers	**295,167**	**179,033**

Short-term (up to 1 year)	292,933	178,493
Long-term (more than 1 year)	2,234	540

29. Debt securities issued

Issued covered bonds bear floating interest rates with a semi-annual interest coupon, except for the covered bonds issued on 23 July 2013 with a nominal value of EUR 30,000 thousand. These bonds bear a fixed interest rate.

As at 31 December 2013, mortgage covered bonds issued in PLN and EUR, as well as public covered bonds issued in PLN, are assigned 'A' level by the Fitch Ratings Ltd. agency.

Receivables secured with mortgage entered as the first position in the land and mortgage register are set up as collateral for mortgage covered bonds. The collateral for public covered bonds are loans, including interest receivable, partly secured with a guarantee or pledge of local government units and loans granted to such local government units. In addition, the basis for the issue of mortgage covered bonds up to 10% of the amount of the Bank's debt claims secured by a mortgage may include:

- the Bank's funds invested in securities issued or guaranteed by the National Bank of Poland (NBP), the European Central Bank, governments or central banks of the Member States of the European Union, the Organization for Economic Co-operation and Development (OECD), except for countries which restructure or have restructured their foreign debt over the past 5 years, as well as the State Treasury,
- the Bank's funds deposited with the National Bank of Poland (NBP),
- the Bank's funds held in cash.

Total nominal value of mortgage covered bonds issued as at:

- 31 December 2013 amounted to PLN 1,978,248 thousand,
- 31 December 2012 amounted to PLN 1,790,882 thousand.

Total nominal value of public covered bonds issued as at:

- 31 December 2013 amounted to PLN 350,000 thousand,
- 31 December 2012 amounted to PLN 450,000 thousand.

The carrying amount of covered bonds issued as at 31 December 2013 and 31 December 2012 is presented in the tables below.

The non-overdue principal of loans registered in the register of covered bonds collateral that constitute the collateral for the issue of mortgage covered bonds as at:

- 31 December 2013 amounted to PLN 2,404,717 thousand,
- 31 December 2012 amounted to PLN 2,619,590 thousand.

According to the Act on covered bonds and mortgage banks, the Bank is eligible to refinance mortgage loans not exceeding 60% of the mortgage-banking value of the real estate with the proceeds from issue of covered bonds.

The value of loan receivables constituting collateral for the issue of mortgage covered bonds not exceeding 60% of the bank and mortgage value of real estate as at:

- 31 December 2013 amounted to PLN 2,019,926 thousand,
- 31 December 2012 amounted to PLN 2,162,039 thousand.

Both as at 31 December 2013 and 31 December 2012, mortgage covered bonds were backed by loan receivables secured by mortgages entered as the first item in the land register.

The non-overdue principal of loans registered in the register of covered bonds collateral that constitute the collateral for the issue of public covered bonds as at:

- 31 December 2013 amounted to PLN 480,604 thousand,
- 31 December 2012 amounted to PLN 561,481 thousand.

The minimum level of collateral for covered bonds in trading required by law is specified as the equivalent of the nominal amount of the issued mortgage covered bonds.

The nominal value of public covered bonds quoted on two markets as part of the CATALYST system: The Regulated Market of Securities maintained by BondSpot S.A. and the regulated parallel stock exchange market of GPW w Warszawie S.A. (Warsaw Stock Exchange) as at:

- 31 December 2013 amounted to PLN 350,000 thousand,
- 31 December 2012 amounted to PLN 450,000 thousand.

The nominal value of mortgage covered bonds quoted on two markets as part of the CATALYST system: The Regulated Market of Securities maintained by BondSpot S.A. and the regulated parallel stock exchange market of GPW w Warszawie S.A. (Warsaw Stock Exchange) as at:

- 31 December 2013 amounted to PLN 1,978,248 thousand,
- 31 December 2012 amounted to PLN 1,790,882 thousand.

The Bank did not register any violations of contractual terms related to liabilities in respect of debt securities issued.

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Movements in the balance of debt securities issued

	31.12.2013	31.12.2012
As at the beginning of the period	**2,852,445**	**2,488,440**
Increase (due to)	903,726	1,715,506
- issue	776,826	1,556,034
- accrued interest	126,900	159,472
Decrease (due to)	(1,094,764)	(1,351,501)
- redemption	(950,000)	(1,199,000)
- interest repayment	(140,304)	(152,348)
- currency translation differences	(4,460)	(153)
As at the end of the period	**2,661,407**	**2,852,445**
Short-term (up to 1 year)	608,159	936,563
Long-term (more than 1 year)	2,053,248	1,915,882
Fixed interest rate debt securities issued	133,481	49,388
Floating interest rate debt securities issued	2,527,926	2,803,057

As at 31.12.2013

Debt financial instruments by type	Nominal value	Interest rate as at 31.12.2013	Guarantee / collateral	Redemption date	Amount of liability
Long-term issues (with original maturity of over 1 year)					
Covered bonds (PLN)	25,000	4.05%	Mortgage bonds register	2014-04-28	25,174
Covered bonds (PLN)	200,000	4.11%	Mortgage bonds register	2014-07-28	203,435
Covered bonds (PLN)	100,000	4.07%	Mortgage bonds register	2015-09-28	100,921
Covered bonds (PLN)	100,000	3.94%	Mortgage bonds register	2014-11-28	100,307
Covered bonds (PLN)	100,000	3.88%	Mortgage bonds publicly registered	2015-11-30	100,238
Covered bonds (PLN)	200,000	3.85%	Mortgage bonds register	2016-04-20	201,194
Covered bonds (PLN)	100,000	3.70%	Mortgage bonds register	2015-05-15	100,366
Covered bonds (PLN)	200,000	3.68%	Mortgage bonds register	2017-06-16	199,855
Covered bonds (PLN)	100,000	3.59%	Mortgage bonds register	2015-07-07	101,613
Covered bonds (PLN)	200,000	4.00%	Mortgage bonds register	2017-04-20	201,127
Covered bonds (PLN)	200,000	4.39%	Mortgage bonds register	2018-06-15	199,796
Covered bonds (EUR)	10,000	2.24%	Mortgage bonds register	2017-10-19	41,580
Covered bonds (PLN)	100,000	4.40%	Mortgage bonds register	2016-11-15	100,391
Covered bonds (PLN)	100,000	4.01%	Mortgage bonds publicly registered	2015-07-28	101,576
Covered bonds (PLN)	150,000	4.50%	Mortgage bonds publicly registered	2016-09-28	151,421
Covered bonds (PLN)	80,000	3.70%	Mortgage bonds register	2019-06-21	79,973
Covered bonds (EUR)	30,000	2.75%	Mortgage bonds register	2020-07-28	123,533
Covered bonds (EUR)	50,000	1.35%	Mortgage bonds register	2018-22-10	207,085
Bonds (PLN)	30,000	3.60%	no collateral	2014-03-17	30,044
Bonds (PLN)	50,000	3.90%	no collateral	2015-03-16	50,054
Bonds (PLN)	30,000	3.63%	no collateral	2014-04-15	30,228
Bonds (PLN)	50,000	3.60%	no collateral	2014-10-06	50,417
Bonds (PLN)	20,000	3.57%	no collateral	2014-10-22	20,133
Short-term issues (with original maturity of up to 1 year)					
Bonds (PLN)	50,000	3.78%	no collateral	2014-01-07	50,445
Bonds (PLN)	30,000	3.73%	no collateral	2014-01-15	30,238
Bonds (PLN)	15,000	3.58%	no collateral	2014-07-15	15,111
Bonds (PLN)	35,000	3.51%	no collateral	2014-10-27	35,204
Bonds (PLN)	10,000	3.20%	no collateral	2014-02-28	9,948
Debt securities in issue (carrying value)					**2,661,407**

As at 31.12.2012

Debt financial instruments by	Nominal value	Interest rate as at 31.12.2012	Guarantee / collateral	Redemption date	Amount of liability
Long-term issues (with original maturity of over 1 year)					
Covered bonds (PLN)	25,000	6.05%	Mortgage bonds register	29.04.2013	25,257
Covered bonds (PLN)	100,000	5.46%	Mortgage bonds publicly registered	20.09.2013	101,508
Covered bonds (PLN)	200,000	5.79%	Mortgage bonds register	21.10.2013	202,074
Covered bonds (PLN)	25,000	6.10%	Mortgage bonds register	28.04.2014	25,244
Covered bonds (PLN)	200,000	6.55%	Mortgage bonds register	28.07.2014	205,353
Covered bonds (PLN)	100,000	5.79%	Mortgage bonds register	28.11.2014	100,416
Covered bonds (PLN)	100,000	5.64%	Mortgage bonds register	15.05.2015	100,538
Covered bonds (PLN)	100,000	4.92%	Mortgage bonds register	07.07.2015	102,710
Covered bonds (PLN)	100,000	6.45%	Mortgage bonds publicly registered	28.07.2015	102,569
Covered bonds (PLN)	100,000	6.31%	Mortgage bonds register	28.09.2015	101,460
Covered bonds (PLN)	100,000	5.73%	Mortgage bonds publicly registered	30.11.2015	100,348
Covered bonds (PLN)	200,000	5.92%	Mortgage bonds register	20.04.2016	201,839
Covered bonds (PLN)	150,000	6.74%	Mortgage bonds publicly registered	28.09.2016	152,225
Covered bonds (PLN)	100,000	6.20%	Mortgage bonds register	15.11.2016	100,311
Covered bonds (PLN)	200,000	6.07%	Mortgage bonds register	20.04.2017	201,778
Covered bonds (PLN)	200,000	5.20%	Mortgage bonds register	16.06.2017	199,836
Covered bonds (PLN)	200,000	5.91%	Mortgage bonds register	15.06.2018	199,780
Covered bonds (EUR)	10,000	2.31%	Mortgage bonds register	19.10.2017	40,959
Bonds (PLN)	50,000	6.00%	no collateral	07.01.2013	50,723
Bonds (PLN)	50,000	5.98%	no collateral	15.01.2013	50,637
Bonds (PLN)	10,000	5.71%	no collateral	26.08.2013	10,057
Bonds (PLN)	50,000	5.85%	no collateral	28.10.2013	50,515
Short-term issues (with original maturity of up to 1 year)					
Bonds (PLN)	5,000	5.73%	no collateral	15.01.2013	4,989
Bonds (PLN)	15,000	5.75%	no collateral	12.03.2013	14,833
Bonds (PLN)	30,000	5.61%	no collateral	05.04.2013	29,566
Bonds (PLN)	30,000	5.36%	no collateral	15.03.2013	30,063
Bonds (PLN)	75,000	5.11%	no collateral	18.03.2013	75,149
Bonds (PLN)	25,000	5.70%	no collateral	24.05.2013	25,135
Bonds (PLN)	75,000	5.31%	no collateral	17.06.2013	75,145
Bonds (PLN)	40,000	5.30%	no collateral	20.06.2013	40,060
Bonds (PLN)	30,000	5.93%	no collateral	15.07.2013	30,372
Bonds (PLN)	50,000	5.19%	no collateral	04.10.2013	50,704
Bonds (PLN)	30,000	5.74%	no collateral	15.11.2013	30,203
Bonds (PLN)	20,000	5.62%	no collateral	28.11.2013	20,089
Debt securities in issue (carrying value)					**2,852,445**

30. Subordinated liabilities

In 2013, just as in 2012, the Bank did not experience any delays in the repayment of principal or interest instalments, nor did it violate any other contractual terms relating to its subordinated liabilities.

SUBORDINATED LIABILITIES	Nominal value	Currency	Interest rate as at 31.12.2013	Maturity/redemption date	Balance of liability (PLN '000)
As at 31 December 2013					
mBank S.A.	100,000	PLN	6.15%	19.12.2022	**100,268**

SUBORDINATED LIABILITIES	Nominal value	Currency	Interest rate as at 31.12.2012	Maturity/redemption date	Balance of liability (PLN '000)
As at 31 December 2012					
mBank S.A.	100,000	PLN	7.76%	19.12.2022	**100,316**

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Movements in the balance of subordinated liabilities

	31.12.2013	31.12.2012
As at the beginning of the period	**100,316**	**100,300**
Increase (due to)	6,722	106,568
- taking a loan	-	100,000
- interest on a loan	6,722	6,568
Decrease (due to)	(6,770)	(106,552)
- loan repayment	-	(100,000)
- repayment of interest on a loan	(6,770)	(6,552)
Subordinated liabilities as at the end of the period	**100,268**	**100,316**
Short-term (up to 1 year)	268	316
Long-term (more than 1 year)	100,000	100,000

31. Other liabilities and provisions

31.1. Other liabilities

	31.12.2013	31.12.2012
Other liabilities (due to)	**19,788**	**3,821**
- accruals	5,847	2,714
- liabilities due to income tax on salaries and VAT	12,913	331
- provisions for unused holidays	598	432
- other	430	344
Total other liabilities	**19,788**	**3,821**
Short-term (up to 1 year)	19,788	3,821
Long-term (more than 1 year)	-	-

31.2. Provisions

	31.12.2013	31.12.2012
Provisions (due to)	**84**	**301**
- provisions for retirement and disability benefits	84	112
- provisions for legal proceedings	-	189
Total provisions	**84**	**301**
Short-term (up to 1 year)	17	191
Long-term (more than 1 year)	67	110

Movements in the period from 01.01.2013 to 31.12.2013	Provision for retirement and disability benefits	Provision for legal proceedings	Total
As at the beginning of the period	**112**	**189**	**301**
- recognition	15	-	15
- reversal	-	(39)	(39)
- utilization	(43)	(150)	(193)
As at the end of the period	**84**	**-**	**84**
Expected provision settlement period:			
Short-term (up to 1 year)	17	-	17
Long-term (more than 1 year)	67	-	67

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Movements in the period from 01.01.2012 to 31.12.2012	Provision for retirement and disability benefits	Provision for legal proceedings	Total
As at the beginning of the period	**100**	**-**	**100**
- recognition	47	189	236
- reversal	-	-	-
- utilization	(35)	-	(35)
As at the end of the period	**112**	**189**	**301**
Expected provision settlement period:			
Short-term (up to 1 year)	2	189	191
Long-term (more than 1 year)	110	-	110

32. Deferred income tax

Deferred income tax assets and provisions are calculated for all temporary differences in accordance with the balance sheet method, using an effective income tax rate that will be applicable in the year of the tax obligation arising (19% both in 2013 and 2012).

Changes in deferred income tax assets and provision are presented below:

Deferred income tax assets	As at 1 January 2013	Recognised in the income statement	Recognised in other comprehensive income	Other changes	As at 31 December 2013
Interest accrued	7,318	(2,590)	-	-	**4,728**
Valuation of derivative financial instruments	103	73	-	-	**176**
Valuation of available-for-sale financial instruments	-	-	-	-	**-**
Amount of impairment write-downs on receivables*	3,858	4,330	-	-	**8,188**
Provisions for employee benefits	390	(161)	-	-	**229**
Impairment write-downs on inventories	569	(569)	-	-	**-**
Accruals	196	288	-	-	**484**
Revenues to be settled (commissions settled using the effective interest rate method)	5,778	634	-	-	**6,412**
Exchange differences	1,188	690	-	-	**1,878**
Total deferred income tax assets	**19,400**	**2,695**	**-**	**-**	**22,095**

Short-term (up to 1 year)	14,611
Long-term (more than 1 year)	7,484

* The item "Amount of impairment write-downs on receivables" refers to write-downs on loans whose non-recoverability will be documented.

Deferred income tax assets	As at 1 January 2012	Recognised in the income statement	Recognised in other comprehensive income	Other changes	As at 31 December 2012
Interest accrued	6,732	586	-	-	**7,318**
Valuation of derivative financial instruments	2,378	(2,275)	-	-	**103**
Valuation of available-for-sale financial instruments	-	-	-	-	**-**
Amount of impairment write-downs on receivables*	3,080	778	-	-	**3,858**
Provisions for employee benefits	352	38	-	-	**390**
Impairment write-downs on inventories	239	330	-	-	**569**
Accruals	137	59	-	-	**196**
Revenues to be settled (commissions settled using the effective interest rate method)	5,609	169	-	-	**5,778**
Exchange differences	-	1,188	-	-	**1,188**
Other write-downs on receivables	12	(12)	-	-	**-**
Total deferred income tax assets	**18,539**	**861**	**-**	**-**	**19,400**

Short-term (up to 1 year)	18,559
Long-term (more than 1 year)	841

*The item "Amount of impairment write-downs on receivables" refers to write-downs on loans whose non-recoverability will be documented.

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Deferred income tax liabilities	As at 1 January 2013	Recognised in the income statement	Recognised in other comprehensive income	Other changes	As at 31 December 2013
Interest accrued	(7,164)	1,691	-	-	**(5,473)**
Valuation of derivative financial instruments	(748)	(1,147)	-	-	**(1,895)**
Valuation of available-for-sale financial instruments	(560)	-	218	-	**(342)**
Provision for employee benefits	-	-	(8)	-	**(8)**
Prepaid costs	(875)	(320)	-	-	**(1,195)**
Difference between tax and balance sheet depreciation/amortisation	(93)	(31)	-	-	**(124)**
Total deferred income tax liabilities	**(9,440)**	**193**	**210**	**-**	**(9,037)**

Short-term (up to 1 year)	(9,037)
Long-term (more than 1 year)	-

Deferred income tax liabilities	As at 1 January 2012	Recognised in the income statement	Recognised in other comprehensive income	As at 31 December 2012
Interest accrued	(6,417)	(747)	-	**(7,164)**
Valuation of derivative financial instruments	(1,228)	480	-	**(748)**
Valuation of available-for-sale financial instruments	(37)	-	(523)	**(560)**
Prepaid costs	(690)	(185)	-	**(875)**
Difference between tax and balance sheet depreciation/amortisation	(162)	69	-	**(93)**
Exchange differences	(1,881)	1,881	-	**-**
Total deferred income tax liabilities	**(10,415)**	**1,498**	**(523)**	**(9,440)**

Short-term (up to 1 year)	(9,440)
Long-term (more than 1 year)	-

Deferred tax recognised in the income statement	31.12.2013	31.12.2012
Interest accrued	(899)	(161)
Valuation of derivative financial instruments	(1,074)	(1,795)
Amount of impairment write-downs on receivables*	4,330	778
Provisions for employee benefits	(161)	38
Impairment write-downs on inventories	(569)	330
Accruals	288	59
Revenues to be settled (commissions settled using the effective interest rate method)	634	169
Prepaid costs	(320)	(185)
Difference between tax and balance sheet depreciation/amortisation	(31)	69
Foreign exchange differences	690	3,069
Other write-downs on receivables	-	(12)
Total deferred tax recognised in the income statement	**2,888**	**2,359**

*The item "Amount of impairment write-downs on receivables" refers to write-downs on loans whose non-recoverability will be documented.

The Bank capitalises impairments write-downs on loans in the event of estimating that the most likely scenario will entail documenting non-recoverability in accordance with applicable tax laws as a result of undertaken debt collection activities.

Deferred tax assets are recognised when it is probable that taxable income will be generated in the future.

33. Litigation pending before a court, an appropriate arbitration authority or public administration authority

As at 31 December 2013, the Bank was not involved in any proceedings before a court, arbitration body, or public administration authority concerning liabilities of the Bank or its subsidiaries which represent at least 10% of the Bank's equity. Moreover, the total value of claims concerning liabilities of the Bank in all proceedings before a court, an arbitration body or a public administration authority as at 31 December 2013 also did not exceed 10% of the Bank's equity.

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As at 31 December 2013, proceedings were pending before the District Court in Poznań concerning an action brought by the Bank against a limited debtor who acquired a mortgaged property from the Bank. The value of the matter at issue is PLN 11,692 thousand.

As at 31 December 2012, proceedings were pending before the District Court in Warsaw (20th Commercial Division) regarding the return of a commission for the early repayment of a loan. As at 31 December 2012, the Bank created a provision of PLN 189 thousand in connection with the proceedings. On 15 May 2013, an agreement was signed, whereby the Bank paid out the amount of PLN 150 thousand from the provision, and the remaining amount of the provision, i.e. PLN 39 thousand, was released.

34. Off-balance sheet liabilities

31.12.2013	Up to 1 year	From 1 to 5 years	Over 5 years	Total
1. Off-balance sheet liabilities granted and received	**951,432**	**197,072**	-	**1,148,504**
Liabilities granted	**782,399**	**197,072**	-	**979,471**
1. Financial liabilities:	782,399	197,072	-	979,471
a) Lending commitments	779,801	189,997	-	969,798
b) Operating lease liabilities	2,598	7,075	-	9,673
Liabilities received:	**169,033**	-	-	**169,033**
a) Financial liabilities received	169,033	-	-	169,033
2. Derivative financial instruments	**1,742,629**	-	**248,832**	**1,991,461**
1. Interest rate derivatives	414,720	-	248,832	663,552
2. Foreign exchange derivatives	1,327,909	-	-	1,327,909
Total off-balance sheet items	**2,694,061**	**197,072**	**248,832**	**3,139,965**

31.12.2012	Up to 1 year	From 1 to 5 years	Total
1. Off-balance sheet liabilities granted and received	**799,104**	**218,477**	**1,017,581**
Liabilities granted	**580,146**	**218,477**	**798,623**
1. Financial liabilities:	580,146	218,477	798,623
a) Lending commitments	578,738	209,695	788,433
b) Operating lease liabilities	1,408	8,782	10,190
2. Other liabilities	-	-	-
Liabilities received:	**218,958**	**-**	**218,958**
a) Financial liabilities received	218,958	**-**	218,958
2. Derivative financial instruments	**2,558,435**	**-**	**2,558,435**
1. Interest rate derivatives	976,353	-	976,353
2. Foreign exchange derivatives	1,582,082	-	1,582,082
Total off-balance sheet items	**3,357,539**	**218,477**	**3,576,016**

35. Pledged assets

In accordance with the Act on the Bank Guarantee Fund, as at 31 December 2013, the Bank held Central Bank's bills in the amount of PLN 1,500 thousand (with a nominal value of PLN 1,500 thousand), whereas as at 31 December 2012 it held Central Bank's bills in the amount of PLN 1,000 thousand (with a nominal value of PLN 1,000 thousand), as well as treasury bonds in the amount of PLN 298 thousand (with a nominal value of PLN 300 thousand) which constituted collateral for the guaranteed deposits protection fund. These bills are shown in the balance sheet under "Investment securities available for sale".

The Bank secured mortgage covered bonds issued with receivables in respect of loans and advances granted, which are described in Note 29.

36. Share capital

As at 31 December 2013, the total number of ordinary shares was 2,750 thousand (as at 31 December 2012: 1,750 thousand) shares with a nominal value of PLN 100 each (as at 31 December 2012: (PLN 100 each). On 23 November 2012, mBank Hipoteczny S.A. carried out a private issue of 1,000,000 ordinary registered shares without pre-emptive rights. On 8 January 2013, the new amount of share capital of mBank Hipoteczny S.A., increased due to the new issue, was entered in the National Court Register. All of the issued shares have been fully paid up.

The Bank did not issue any preference shares, and there are no restrictions on rights related to the shares. All the shares participate in the distribution of dividends to the same extent. The Bank does not have any treasury shares.

The shareholders of mBank Hipoteczny S.A. are presented in the table below:

Shareholder's name	Share capital in PLN '000	Shares		Voting rights at the General Shareholders' Meeting	
		Number of shares in '000	%	Number of shares in '000	%
MLV 45 Sp. z o.o. spółka komandytowa*	208,200	2,082	75.71	2,082	75.71
mBank S.A.	66,800	668	24.29	668	24.29
Total	**275,000**	**2,750**	**100**	**2,750**	**100**

* BRE Holding Sp. z o.o. was transformed into MLV 45 Sp. z o.o. spółka komandytowa. The transformation was registered in the National Court Register on 29 August 2013.

The Bank has no liabilities in respect of a dividend approved for payment.

REGISTERED SHARE CAPITAL (STRUCTURE)						
Series/issue in '000	Type of shares	Number of shares (in thousands)	Series/issue at par value (PLN '000)	Means of covering share capital	Registration date	Right to dividend
500 A series shares	registered	500	A series 50,000	cash	16.04.1999	01.01.2000
850 B series shares	registered	850	B series 85,000	cash	20.09.2000	01.01.2001
400 C series shares	registered	400	C series 40,000	cash	24.04.2006	01.01.2006
1,000 D series shares	registered	1,000	D series 100,000	cash	08.01.2013	01.01.2013

37. Retained earnings

	31.12.2013	31.12.2012
Other supplementary capital	192,315	186,800
General Risk Fund	31,000	27,000
Profit from the previous year	-	228
Profit for the current year	2,154	9,287
Total retained earnings	**225,469**	**223,315**

Other supplementary capital and the General Risk Fund are created as a result of profit appropriation and are intended for the purposes specified in the Memorandum of Association or other legal regulations.

The Bank is obliged to transfer at least 8% of its net profit to its statutory supplementary capital until it has reached the level of one-third of the Bank's share capital. The Bank may also transfer a part of its net profit to the General Risk Fund to cover unforeseen losses.

for the year 2013 (in PLN '000)

According to the Resolution No 2 passed by the General Shareholders' Meeting of mBank Hipoteczny S.A. on 29 April 2013, the net profit of 2012 was distributed as follows:

- supplementary capital — PLN 5,287 thousand,
- General Risk Fund — PLN 4,000 thousand,

The Bank plans to transfer the net profit of 2013 to its statutory supplementary capital and partially to the General Risk Fund.

38. Dividend per share

mBank Hipoteczny S.A. does not plan to pay a dividend for 2013, nor did it pay any for 2012.

39. Cash and cash equivalents

For the purposes of the cash flow statement, cash and cash equivalents comprise the following balances maturing within less than three months of being purchased.

	31.12.2013	31.12.2012
Cash and balances with the Central Bank (Note 18)	7,378	3,069
Amounts due from other banks (Note 19)	22,377	10,282
Investment securities	515,428	484,828
Total cash and cash equivalents	**545,183**	**498,179**

40. Related party transactions

MLV 45 sp. z o.o. spółka komandytowa (formerly: BRE Holding Sp. z o.o.) is the direct parent entity of mBank Hipoteczny S.A. mBank S.A. is the parent entity of MLV 45 sp. z o.o. spółka komandytowa. Commerzbank AG is the ultimate parent company. Commerzbank AG is the direct parent entity of mBank S.A. Until 28 November 2013, the direct subsidiary of mBank Hipoteczny S.A. was BDH Development Sp. z o.o. (previous company name: Bankowy Dom Hipoteczny Sp. z o.o.). The sale of shares in BDH Development Sp. z o.o. is described in Note 23.

All the transactions between the Bank and its related entities were, according to the Management Board, typical and routine transactions concluded on arm's length terms, and their nature and terms resulted from the current operating activities conducted by the Bank. Transactions with related entities concluded in the normal course of operating activities include loans, deposits and derivative transactions.

As at 31 December 2013, the Bank's liabilities to mBank S.A. comprise mainly term deposits totalling PLN 757,809 thousand, a loan of PLN 415,626 thousand and a subordinated loan of PLN 100,268 thousand. As at 31 December 2012, the Bank's liabilities to mBank S.A. comprised mainly term deposits totalling PLN 1,049,799 thousand, a loan of PLN 122,668 thousand and a subordinated loan of PLN 100,316 thousand.

In 2012, the repayment of loans received from mBank S.A., concluded in 2010, amounted to EUR 200,000 thousand.

The following table presents transactions with mBank S.A., broken down by contractual maturities.

31.12.2013	Up to 1 month	From 1 to 3 months	From 3 to 12 months	From 1 to 5 years	Over 5 years	Total
Term deposits	148,728	321,880	287,201			**757,809**
Loans received				415,626		**415,626**
Subordinated loan					100,268	**100,268**

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31.12.2012	Up to 1 month	From 1 to 3 months	From 3 to 12 months	Over 5 years	Total
Term deposits	305,711	373,467	370,621	-	**1,049,799**
Loans received	-	-	122,668	-	**122,668**
Subordinated loan	-	-	-	100,316	**100,316**

Information on the interest rate has been disclosed in Notes 27 and 30.

The most important transactions with related entities in 2013

Agreements concluded with mBank S.A. in 2013:

- On 27 August 2013, a loan agreement for a total amount of EUR 100,000 thousand was concluded for the purpose of financing the Bank's current operations,
- On 23 July 2013, a deposit agreement for a stand-by line was concluded for a total amount of PLN 150,000 thousand,
- On 23 July 2013, a firm-commitment underwriting agreement was concluded for mortgage covered bonds (in EUR) of series HPE2 in a public offering,
- On 18 November 2013, a firm-commitment underwriting agreement was concluded for mortgage covered bonds (in EUR) of series HPE3 in a public offering,
- On 28 November 2013, an agreement was concluded for the sale of shares in the share capital BDH Development Sp. z o.o. for PLN 778 thousand,
- On 28 August 2013, an outsourcing agreement was concluded to entrust agency in the field of banking activities and factual activities related to banking operations pertaining to the organization of a joint sales network and comprehensive service of the mortgage loans granted by mBank Hipoteczny S.A. in cooperation with mBank S.A. under an agency model.

Agreements concluded with BDH Development Sp. z o.o. in 2013:

In 2013, the following agreements for the sale of repossessed properties were concluded with BDH Development Sp. z o.o. (a subsidiary of mBank S.A.):

- On 12 December 2013, an agreement was concluded for the sale of a repossessed property for a total amount of PLN 48,462 thousand, gross,
- On 23 December 2013, an agreement was concluded for the sale of a repossessed property for a total amount of PLN 15,644 thousand, gross,
- On 23 December 2013, an agreement was concluded for the sale of a repossessed property for a total amount of PLN 22,784 thousand, gross,
- On 23 December 2013, an agreement was concluded for the sale of a repossessed property for a total amount of PLN 14,333 thousand, gross,

Repossessed properties have been presented in the statement of financial position under "Other assets" — "Inventories". The profit from the sales of repossessed properties is presented in the income statement under "Other operating income" in the amount of PLN 5,657 thousand (Note 10), while the loss on the sale of inventories is presented in the item "Other operating expenses" in the amount of PLN (2,918) thousand.

Other agreements concluded mBank Group companies:

- On 2 September 2013, a service agreement was concluded with Centrum Operacji Sp. z o.o. for comprehensive handling of complaints and instructions and for administrative and archive-related services pertaining to mortgage loans granted by mBank Hipoteczny S.A. in cooperation with mBank S.A.,

- On 5 September 2013, an agreement was concluded with Aspiro S.A. for credit brokerage services (sales and after-sales) pertaining to mortgage loans granted by mBank Hipoteczny S.A. in cooperation with mBank S.A.,

- On 9 September 2013, an agreement was concluded with BRE Ubezpieczenia TUiR S.A. in respect of TUI offering its "Mieszkam Bezpiecznie" group insurance to the customers who have been granted a mortgage loan by mBank Hipoteczny S.A.,

- On 20 August 2013, an agreement was concluded with BRE Ubezpieczenia TUiR S.A. to cover mortgage loans granted by mBank Hipoteczny S.A. in cooperation with mBank S.A. under its bridging insurance policy.

In 2013, as in 2012, mBank Hipoteczny S.A. did not conclude any transactions with:

- Members of the Management Board and the Supervisory Board of the Bank, their close family members and entities controlled or jointly controlled by these persons,
- Members of the Management Board and the Supervisory Board of mBank S.A., their close family members and entities controlled or jointly controlled by these persons,
- Members of the Management Board and the Supervisory Board of Commerzbank AG, their close family members and entities controlled or jointly controlled by these persons.

The table below presents the amounts of the Bank's transactions with related entities. The amounts of transactions include assets, liabilities and related costs and income as at 31 December 2013 and 31 December 2012.

(PLN '000)	mBank Group companies*		BDH Development Sp. z o.o.		mBank S.A.		Commerzbank AG	
As at the end of the period	**31.12.2013**	**31.12.2012**	**31.12.2013**	**31.12.2012**	**31.12.2013**	**31.12.2012**	**31.12.2013**	**31.12.2012**
Statement of financial position								
Assets	-	-	52,761	-	35,286	15,347	-	6,056
Liabilities	-	-	53,576	47	1,273,979	1,272,894	-	350
Income statement								
Interest income	-	-	-	-	13,938	13,993	12,333	16,754
Interest expense	-	-	-	-	(21,363)	(30,515)	-	-
Commission expense	(43)	(78)	-	-	(2)	-	-	-
Net trading income	-	-	-	-	7,357	3,875	(1,700)	(1,278)
Other operating income	-	-	5,658	-	150	-	-	-
Other operating expenses	(44)	(40)	(2,918)	(31)	-	-	-	-
Overhead costs, depreciation/amortisation and other operating expenses	(715)	(152)	-	-	(114)	-	-	-
Contingent liabilities								
Liabilities received	-	-	-	-	169,033	218,958	-	-
Derivatives (purchase, sales)								
IRS contracts	-	-	-	-	663,552	960,000	-	16,353
FX SWAP contracts	-	-	-	-	1,325,005	575,823	-	1,006,260

* The item "mBank Group companies" includes transactions with the following mBank Group companies: Aspiro S.A., mCentrum Operacji Sp. z o.o., mCorporate Finance S.A., mLeasing, mLocum S.A., Dom Maklerski mBanku S.A.

for the year 2013 (in PLN '000)

Composition and remuneration of Members of the Bank's Management Board

In the first half of 2013, the composition of the Management Board changed. On the day of the General Meeting of Shareholders, i.e. on 29 April 2013, Sven Torsten-Kain's term of office as Member of the Management Board expired. He served as advisor to the Management Board from 1 May to 4 July 2013.

For another term of office, the Supervisory Board, by way of Resolution No 12/2013 of 29 April 2013, appointed the following composition of the Management Board of mBank Hipoteczny S.A.:

Piotr Cyburt	—	President of the Management Board
Marcin Romanowski	—	Member of the Management Board
Marcin Wojtachnio	—	Member of the Management Board

Information on the remuneration and bonuses paid to the Members of the Management Board of the Bank who were performing their functions at the end of 2013, as at 31 December 2013 and 31 December 2012, is presented below:

	Gross remuneration paid in 2013	Bonus for 2012 paid in 2013 (cash settlement of a phantom share-based incentive programme)	Gross remuneration paid in 2012	Bonus for 2011 paid in 2012
Piotr Cyburt	762	54	720	250
Marcin Romanowski	591	27	91	-
Marcin Wojtachnio	405	54	150	-
Total	**1,758**	**135**	**961**	**250**

Remuneration of Members of the Management Board who ceased to perform their functions in 2013:

	Gross remuneration paid in 2013 for performing the function of advisor to the Management Board	Gross remuneration paid in 2013 for performing the function of Member of the Management Board	Severance payment paid in 2013	Gross remuneration paid in 2012 for performing the function of Member of the Management Board	Bonus for 2011 paid in 2012
Sven-Torsten Kain	17	235	1,295	696	232
Total	**17**	**235**	**1,295**	**696**	**232**

Remuneration of Members of the Management Board who ceased to perform their functions in 2012:

	Gross remuneration paid in 2013 for performing the function of advisor to a Member of the Management Board	Gross remuneration paid in 2012 for performing the function of Member of the Management Board	Gross remuneration paid in 2012 for performing the function of advisor to a Member of the Management Board	Bonus for 2011 paid in 2012	Severance payment paid in 2012
Krzysztof Czerkas	55	385	275	220	330
Total	**55**	**385**	**275**	**220**	**330**

On 1 August 2012, Mr Krzysztof Czerkas, Member of the Management Board of mBank Hipoteczny S.A., resigned from his position at mBank Hipoteczny S.A. At the same time, two new Members were appointed to the Management Board of the Company — Mr Marcin Wojtachnio as of 1 August 2012 and Mr Marcin Romanowski as of 15 August 2012. Until 31 January 2013, Mr Krzysztof Czerkas served as advisor to the Management Board of the Bank.

The costs of remuneration of the Management Board recognised in 2013 for serving as Members of the Management Board amounted to PLN 1,993 and in respect of severance payments to PLN 1,295 thousand, while in 2012 these figures amounted to: PLN 2,042 thousand and PLN 330 thousand, respectively.

for the year 2013 (in PLN '000)

In 2013, the accrual for employee and Management Board awards/bonuses amounted to PLN 400 thousand, including accrual for deferred part of variable remuneration for Members of the Management Board and employees having a material impact on the risk profile of the Bank in the amount of PLN 127 thousand.

In 2012 the accrual for employee and Management Board awards/bonuses amounted to PLN 1,511 thousand, including accrual for deferred part of variable remuneration for Members of the Management Board and employees having a material impact on the risk profile of the Bank in the amount of PLN 318 thousand.

The Regulations on variable remuneration for the Members of the Management Board and employees having a material impact on the risk profile of the Bank is discussed in more detail in Note 2.17.

In line with their management contracts and the current length of service as Member of the Management Board, in the event of termination of their management contracts, Members of the Management Board are entitled to a severance pay equivalent to:

- 12 monthly salaries — President of the Management Board,
- 6 monthly salaries — Member of the Management Board

Remuneration of Members of the Bank's Supervisory Board

The composition of the Supervisory Board of mBank Hipoteczny S.A. as at 31 December 2013:

Cezary Kocik	—	Chairman of the Supervisory Board
Hans-Dieter Kemler	—	Deputy Chairman of the Supervisory Board, Member of the Risk Committee
Jolanta Daniewska	—	Member of the Supervisory Board, Member of the Audit Committee
Lidia Jabłonowska-Luba	—	Member of the Supervisory Board, Chairwoman of the Risk Committee
Joerg Hessenmueller	—	Member of the Supervisory Board, Chairman of the Audit Committee, Member of the Risk Committee
Michał Popiołek	—	Member of the Supervisory Board, Member of the Risk Committee
Dariusz Solski	—	Member of the Supervisory Board, Member of the Audit Committee
Piotr Baranek	—	Member of the Supervisory Board, Member of the Risk Committee

On 29 April 2013, the Ordinary General Shareholders' Meeting of mBank Hipoteczny S.A. appointed Mr Dariusz Solski as Member of the Supervisory Board of mBank Hipoteczny S.A. By way of Supervisory Board Resolution No 35 of 12 December 2013, Mr Dariusz Solski was appointed to the Audit Committee, replacing Mr Łukasz Witkowski. In August 2013, Mr Maciej Bieńkowski ceased to serve as Member of the Supervisory Board (resigned on 22 August 2013).

On 30 October 2013, the Extraordinary General Shareholders' Meeting of mBank Hipoteczny S.A. appointed Ms Lidia Jabłonowska-Luba and Mr Piotr Baranek as Members of the Supervisory Board of mBank Hipoteczny S.A. At the same time, Mr Łukasz Witkowski ceased to serve as Member of the Bank's Supervisory Board. By way of Supervisory Board Resolution No 36 of 12 December 2013, Ms Lidia Jabłonowska-Luba was appointed as Chairwoman of the Risk Committee, while Mr Michał Popiołek and Mr Piotr Baranek were appointed as Members of the Risk Committee.

In 2013, Members of the Supervisory Board did not receive any remuneration, except for Ms Jolanta Daniewska, who received remuneration for 2013 in the amount of PLN 36 thousand.

The composition of the Supervisory Board of mBank Hipoteczny S.A. as at 31 December 2012:

Cezary Kocik	—	Chairman of the Supervisory Board
Hans-Dieter Kemler	—	Deputy Chairman of the Supervisory Board, Member of the Risk Committee
Michał Popiołek	—	Member of the Supervisory Board
Jolanta Daniewska	—	Member of the Supervisory Board, Member of the Audit Committee
Maciej Bieńkowski	—	Member of the Supervisory Board
Łukasz Witkowski	—	Member of the Supervisory Board, Member of the Audit Committee, Chairman of the Risk Committee
Joerg Hessenmueller	—	Member of the Supervisory Board, Chairman of the Audit Committee, Member of the Risk Committee

In 2012, Members of the Supervisory Board did not receive any remuneration, except for Ms Jolanta Daniewska, who received remuneration for 2012 in the amount of PLN 36 thousand, and Ms Maria Wojsiat-Przedpełska, who received remuneration in the amount of PLN 9 thousand (not serving as Member of the Supervisory Board since 25 April 2012).

In accordance with paragraph 14, item 5 of the Memorandum of Association of mBank Hipoteczny S.A., the General Shareholders' Meeting decides, by way of a resolution, on appointing and dismissing Members of the Supervisory Board and establishing the terms of their remuneration.

In accordance with paragraph 3, item 9 of the Rules and Regulations of the Supervisory Board of mBank Hipoteczny S.A., the Supervisory Board is responsible for determining the terms of contracts and remuneration for Members of the Bank's Management Board.

41. Information on the registered audit company

On 29 April 2013, the Supervisory Board of BRE Bank Hipoteczny S.A., acting under section 26 paragraph 8 of the Bank's Memorandum of Association, appointed Ernst & Young Audit Sp. z o.o. (currently: Ernst & Young Audyt Polska spółka z ograniczoną odpowiedzialnością s.k.) as auditor of the financial statements of the Bank for 2013.

In connection with the above decision of the Supervisory Board, the Bank concluded an agreement with Ernst & Young Audit Sp. z o.o. (currently: Ernst & Young Audyt Polska spółka z ograniczoną odpowiedzialnością s.k.) for a period of two years, i.e. 2013 and 2014.

Ernst & Young Audyt Polska spółka z ograniczoną odpowiedzialnością s.k. (formerly: Ernst & Young Audit sp. z o.o.) (with its registered office in Warsaw at Rondo ONZ 1, 00-124) is a registered auditor No 130 authorised to audit financial statements.

In the previous years, the Bank did not cooperate with Ernst & Young Audyt Polska spółka z ograniczoną odpowiedzialnością s.k. (formerly: Ernst & Young Audit sp. z o.o.) with regard to audit services.

The audit contract was concluded on 17 June 2013.

The financial statements of the Bank for 2012 were audited by PricewaterhouseCoopers Sp. z o.o. (PwC).

The total fee of Ernst & Young Audyt Polska spółka z ograniczoną odpowiedzialnością s.k. (formerly: Ernst & Young Audit sp. z o.o.) for the period from 1 January 2013 to 31 December 2013 amounted to PLN 197 thousand, including the amount of PLN 98 thousand paid in 2013.

The total fee of PwC for the period from 1 January 2012 to 31 December 2012 amounted to PLN 185 thousand, including the amount of PLN 98 thousand paid in 2012.

The total fee of Ernst & Young Audyt Polska spółka z ograniczoną odpowiedzialnością s.k. (formerly: Ernst & Young Audit sp. z o.o.) for the period from 1 January 2013 to 30 June 2013 amounted to PLN 98 thousand. The amount was paid in full in 2013.

The total fee of PwC for the period from 1 January 2012 to 30 June 2012 amounted to PLN 98 thousand. The amount was paid in full in 2012.

The total fee of Ernst & Young Audyt Polska spółka z ograniczoną odpowiedzialnością s.k. (formerly: Ernst & Young Audit sp. z o.o.) for 2013 amounted to PLN 295 thousand, including the amount of PLN 196 thousand paid in 2013.

The total fee of PwC for 2012 amounted to PLN 283 thousand, including the amount of PLN 196 thousand paid in 2012.

42. Capital adequacy ratio/capital adequacy

The Bank's fundamental principle for capital management is to maintain its capital at a level which ensures stable development of the Bank and covering both the minimum capital requirement and other risks which the Bank deems material. Capital management is based on the principles specified in the Banking Law and in good practices.

The Bank's capital management policies are based on two main pillars:

1. Maintaining the optimum level and structure of equity, using the available methods and measures (retaining the net profit, subordinated loan, issue of shares),
2. Effective use of the existing capital by, inter alia, using systems of capital utilization effectiveness measures, limiting activities which do not generate the anticipated rate of return, developing products with lower capital absorption.

Therefore, effective use of capital forms an integral part of the capital management policies focused on achieving an optimum rate of return on capital and, consequently, creating a stable basis for funding the capital base in future periods, which will enable the capital adequacy ratio to be maintained at the level required by the supervisor (The Polish Financial Supervision Authority — "PFSA"). The capital adequacy ratio, calculated as a quotient of equity and the total capital requirement multiplied by 12.5, should equal as a minimum 8%. Both as at 31 December 2013 and 31 December 2012, the capital adequacy ratio was at a level compliant with the requirements of the Banking Law.

Capital adequacy ratio

The calculation of the Bank's capital adequacy ratio, equity and total capital requirement is made on the following basis:

- The Act of 29 August 1997 — Banking Law (Journal of Laws of 2002 No 72, item 665, as amended),
- Resolution No 76/2010 of the Polish Financial Supervision Authority of 10 March 2010 (Official Journal of PFSA of 2010 No 2, item 11) as amended,
- Resolution No 325/2011 of the Polish Financial Supervision Authority of 20 December 2011 (Official Journal of PFSA of 2011 No 13, item 49),
- Resolution No 208/2011 of the Polish Financial Supervision Authority of 22 August 2011 (Official Journal of PFSA of 2011 No 9, item 34) as amended,
- Resolution No 258/2011 of the Polish Financial Supervision Authority of 4 October 2011 (Official Journal of PFSA of 2011 No 11, item 42),
- Resolution No 384/2008 of the Polish Financial Supervision Authority of 17 December 2008 (Official Journal of PFSA of 2008 No 8, item 38) as amended.

The Bank's equity comprises:

1. Basic funds comprising:
   - principal funds (share capital paid up and registered, supplementary capital and other reserves, excluding all liabilities in respect of preference shares),
   - additional items of basic funds (General Risk Fund for unidentified banking business risk, profit from the previous year, profit under approval by shareholders and net profit for the current reporting year, as calculated in accordance with valid accounting principles, less any expected costs and dividends in amounts not greater than the profit verified by auditors and other items determined by the PFSA),
   - items reducing the basic funds — intangible assets stated at carrying amounts, amounts resulting from the application of the IRB approach to calculate the capital requirement due to credit risk.

2. Supplementary funds comprising:
   - balance sheet items the inclusion of which is decided by the Polish Financial Supervision Authority (including subordinated liabilities),
   - unrealised gains on available-for-sale debt financial instruments in the amount of 80% of their value (before taxation),

- items reducing the supplementary funds — amounts resulting from the application of the IRB approach to calculate the capital requirement due to credit risk.

The total capital requirement comprises the total capital requirement in respect of:

- credit risk,
- operating risk,
- currency risk.

On 14 August 2012, Bundesanstalt für Finanzdienstleistungsaufsicht (BaFin) in cooperation with the Polish Financial Supervision Authority (letter of 27 August 2012) conditionally approved the Bank's application of the internal ratings based approach, with the use of the supervisory approach, in regard to assigning specialised lending exposures to risk categories (IRB slotting approach) to calculate the capital requirement in respect of credit risk. Low importance was assigned to all conditions set out by the PFSA.

In light of the above, since 31 August 2012, when calculating the Bank's capital adequacy ratio, the total capital requirement has been determined taking into account the capital requirement due to credit risk with the application of the IRB approach, in accordance with appendix No 5 to Resolution No 76/2010 of 10 March 2010 (as amended) and in accordance with conditions set out in the consent for its application given by the BaFin and PFSA. At the same time, own funds were determined taking into account the reduction resulting from the IRB approach.

As of 31 December 2013, the Bank's capital adequacy ratio was at 14.92% and as at 31 December 2012 at 11.97%. The total capital requirement of the Bank as at 31 December 2013 amounted to PLN 272,462 thousand, including the capital requirement related to the credit risk of PLN 260,002 thousand (as at 31 December 2012: PLN 281,412 thousand and PLN 268,243 thousand, respectively).

Internal capital

The Bank adjusts its own funds to the level and kind of the risk, it is exposed to, and to the nature, scale and complexity of its business activity. For that purpose, the Bank prepared and implemented the so-called ICAAP process (Internal Capital Adequacy Assessment Process). The aim of this process it to have the own funds at the level adequate to the risk profile and the risk level of the Bank's activities.

The internal capital is the amount of capital estimated by the Bank to cover all material risks identified in the Bank's operations. The internal capital is the sum of the economic capital and the capital required to cover other types of risk.

The process of internal capital adequacy assessment in the Bank is performed on an on-going basis and consists of six stages completed by the organisational units of the Bank. The elements of the process include:

- identification and assessment of relevance of individual types of risk in the Bank's activity,
- calculation of internal capital to cover risks,
- aggregation of capital,
- stress tests,
- monitoring which consists in permanent identification of the risks inherent to the business activities of the Bank and analysis of the level of capital to cover risks.

The process of internal capital adequacy assessment is approved by the Supervisory Board of mBank Hipoteczny S.A. The entire internal process of assessment of the Bank's capital adequacy is subject to annual reviews. The Bank's Management Board is responsible for the internal capital adequacy assessment process.

Due to the fact that both total capital requirement of Bank calculated according to the Resolution No 76/2010 (as amended) and internal capital assessed for the Bank according to Resolution No 258/2011 are lower than the Bank's own funds, the Bank's own funds as at 31 December 2013 were kept at a level consistent with the Banking Law requirements.

As at 31 December 2013, the Bank carried out a validation of the AIRB model.

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Capital adequacy	31.12.2013	31.12.2012
Equity:		
- Share capital	275,000	175,000
- Other supplementary capital	192,315	186,800
- General Risk Fund	31,000	27,000
- Profit from the previous year	-	228
- Unrealised gains on available-for-sale debt instruments	1,441	2,360
- Adjustment of equity for intangible assets	(3,548)	(1,384)
- Subordinated liabilities	100,000	100,000
- Equity reductions resulting from the application of the IRB approach to calculate the capital requirement due to credit risk	(88,215)	(68,839)
Total equity	**507,993**	**421,165**
Risk weighted off-balance sheet assets and liabilities:		
Exposures covered by the IRB approach for the calculation of capital requirement	2,423,060	2,422,378
Specialised lending exposures	2,338,277	2,312,710
- with a 50% risk rate	1,185	-
- with a 70% risk rate	255,217	208,258
- with a 90% risk rate	1,896,188	1,971,347
- with a 115% risk rate	185,687	133,105
Other assets not being credit exposures	84,783	109,668
- with a 100% risk rate	84,783	109,668
Exposures temporarily exempt from the IRB approach	515,088	520,233
Specialised lending exposures	510,404	520,233
- with a 100% risk rate	510,404	520,233
Retail exposures secured on residential property	4,684	-
- with a 75% risk rate	4,684	-
Exposures permanently exempt from the IRB approach	311,872	407,236
- with a 20% risk rate	97,489	120,746
- with a 35% risk rate	3,639	4,348
- with a 75% risk rate	1,146	834
- with a 100% risk rate	209,477	280,936
- with a 150% risk rate	121	372
Total risk weighted off-balance sheet assets and liabilities	**3,250,020**	**3,349,847**
- Derivatives with a 20% risk rate	6	1,210
- Derivatives with a 50% risk rate	-	1,983
Total risk-weighted derivatives	**6**	**3,193**
Total risk weighted derivatives and off-balance sheet assets and liabilities	**3,250,026**	**3,353,040**
Credit risk capital requirement	260,002	268,243
Operating risk capital requirement	12,460	11,841
Currency risk capital requirement	-	1,328
Total capital requirement	**272,462**	**281,412**
Capital adequacy ratio	**14.92%**	**11.97%**

43. Post balance-sheet events

On 16 January 2014, mBank Hipoteczny S.A. issued five-year bonds with a nominal value of PLN 20,000 thousand.

On 28 January 2014, mBank Hipoteczny S.A. issued five-year bonds with a nominal value of PLN 60,000 thousand.

On 17 February 2014, the Bank issued four-year mortgage covered bonds with a nominal value of EUR 7,500 thousand.

On 28 February 2014, the Bank issued fifteen-year mortgage covered bonds with a nominal value of EUR 8,000 thousand.

The Bank act as the assignee under an agreement for the transfer of receivables in respect of an insurance policy. The assignment was made to secure a loan granted by the Bank to a borrower. The borrower had suffered a loss due to a property fire. The insurer paid compensation which did not cover the loss. The Bank, as an entity authorised under the policy, applied for compensation, at first by submitting a request for payment and subsequently, on 4 February 2014, by filing a lawsuit at the District Court in Warsaw thousand against the Insurer for the payment of compensation in the amount of PLN 18,494 thousand.