mBank Hipoteczny

Financial statements of mBank Hipoteczny S.A. according to International Financial Reporting Standards (IFRS) for the year 2014

Selected financial data

The following selected financial data constitute supplementary information to the financial statements of mBank Hipoteczny S.A. for 2014.

Selected financial data		in PLN '000		in EUR '000	
		Year ended 31.12.2014	Year ended 31.12.2013	Year ended 31.12.2014	Year ended 31.12.2013
I.	Interest income	218 996	227 065	52 275	53 922
II.	Fee and commission income	9 632	5 277	2 299	1 253
III.	Net trading income	12 292	3 185	2 934	756
IV.	Operating result	29 475	4 897	7 036	1 163
V.	Profit before income tax	29 475	4 897	7 036	1 163
VI.	Net profit attributable to shareholders of mBank Hipoteczny S.A.	22 371	2 154	5 340	512
VII.	Net cash flows from operating activities	(1 290 686)	87 401	(308 091)	20 755
VIII.	Net cash flows from investing activities	(3 938)	(6 154)	(940)	(1 461)
IX.	Net cash flows from financing activities	1 268 055	(34 243)	302 689	(8 132)
X.	Total net cash flows	(26 569)	47 004	(6 342)	11 162
XI.	Earnings per ordinary share / Diluted earnings per ordinary share (in PLN/EUR)	8,11	0,78	1,94	0,19

Selected financial data		in PLN '000		in EUR '000	
		As at		As at	
		31.12.2014	31.12.2013	31.12.2014	31.12.2013
I.	Total assets	6 176 326	4 782 443	1 449 059	1 153 174
II.	Amounts due to other banks	1 980 634	1 203 488	464 687	290 193
III.	Amounts due to customers	250 012	295 167	58 657	71 173
IV.	Equity attributable to shareholders of mBank Hipoteczny S.A.	624 541	501 963	146 527	121 037
V.	Share capital	285 000	275 000	66 865	66 310
VI.	Number of shares	2 850 000	2 750 000	2 850 000	2 750 000
VII.	Book value per share / Diluted book value per share (in PLN/EUR)	219,14	182,53	51,41	44,01
VIII.	Total capital ratio / capital adequacy ratio (%)	13,31	14,92	13,31	14,92

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 2014 — EUR 1 = PLN 4.2623 and the NBP exchange rate as at 31 December 2013 — EUR 1 = PLN 4.1472,
- for the items of the income statement and the cash flow statement — the rate calculated as the average NBP exchange rate applicable as at the last day of each month in 2014 and 2013 EUR 1 = PLN 4.1893 and EUR 1 = PLN 4.2110, respectively.

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Financial statements in accordance with the International Financial Reporting Standards (IFRS) for the year 2014 (PLN '000)

Income statement

		Year ended 31 December	
	Note	2014	2013
Interest income	7	218 996	227 065
Interest expense	7	(132 813)	(152 286)
Net interest income		**86 183**	**74 779**
Fee and commission income	8	9 632	5 277
Fee and commission expenses	8	(5 586)	(1 584)
Net fee and commission income		**4 046**	**3 693**
Net trading income, including:	9	12 292	3 185
Foreign exchange result		*3 862*	*4 186*
Other net trading income and result on hedge accounting		*8 430*	*(1 001)*
Net income on investments in subsidiaries	23	-	63
Other operating income	10	1 143	7 297
Net impairment write-downs on loans and advances	11	(20 945)	(34 866)
Overhead costs	12	(46 839)	(39 189)
Amortisation and depreciation	24,25	(4 310)	(4 162)
Other operating expenses	13	(2 095)	(5 903)
Operating result		**29 475**	**4 897**
Profit before income tax		**29 475**	**4 897**
Income tax	14	(7 104)	(2 743)
Net profit		**22 371**	**2 154**
Net profit attributable to shareholders of the Bank	15	**22 371**	**2 154**
Weighted average number of ordinary shares / Diluted weighted average number of ordinary shares	15	**2 759 589**	**2 750 000**
Earnings per ordinary share / Diluted earnings per ordinary share (in PLN)	15	**8,11**	**0,78**

Total profit of mBank Hipoteczny S.A. for 2014 and 2013 relates to the result of continued operations.

Explanatory notes presented on pages 8 to 91 constitute an integral part of these financial statements.

Financial statements in accordance with the International Financial Reporting Standards (IFRS) for the year 2014 (PLN '000)

Statement of comprehensive income

		Year ended 31 December	
	Note	2014	2013
Net profit		**22 371**	**2 154**
Other comprehensive income net of tax	16	**269**	**(896)**
Items that may be reclassified to the income statement		**283**	**(931)**
Available-for-sale financial assets (gross)		349	(1 149)
Deferred tax on available-for-sale financial assets		(66)	218
Available-for-sale financial assets (net)		283	(931)
Items that will not be reclassified to the income statement		**(14)**	**35**
Actuarial gains and losses on post-employment benefits (gross)		(17)	43
Deferred tax on actuarial gains and losses on post-employment benefits		3	(8)
Actuarial gains and losses on post-employment benefits (net)		(14)	35
Total comprehensive income net of tax		**22 640**	**1 258**
Net comprehensive income attributable to shareholders of the Bank		**22 640**	**1 258**
Weighted average number of ordinary shares / Diluted weighted average number of ordinary shares		**2 759 589**	**2 750 000**
Net comprehensive income per ordinary share / Diluted net comprehensive income per ordinary share (in PLN)		**8,20**	**0,46**

Explanatory notes presented on pages 8 to 91 constitute an integral part of these financial statements.

Financial statements in accordance with the International Financial Reporting Standards (IFRS) for the year 2014 (PLN '000)

Statement of financial position

ASSETS	Note	31.12.2014	31.12.2013
Cash and balances with the central bank	18	7 669	7 378
Amounts due from other banks	19	30 972	22 377
Derivative financial instruments	20	37 291	12 913
Loans and advances to customers	21	5 325 741	4 045 000
Investment securities available for sale	22	735 220	605 824
Intangible assets	24	5 074	3 548
Tangible fixed assets	25	7 241	9 110
Current income tax assets		1 002	620
Deferred income tax assets	32	11 426	13 058
Other assets, including:	26	14 690	62 615
- inventories		8 192	8 192
TOTAL ASSETS		**6 176 326**	**4 782 443**

LIABILITIES AND EQUITY			
L i a b i l i t i e s			
Amounts due to other banks	27	1 980 634	1 203 488
Derivative financial instruments	20	9 442	278
Amounts due to customers	28	250 012	295 167
Debt securities in issue	29	3 171 588	2 661 407
Hedge accounting adjustments related to fair value of hedged items	3.3.	25 763	-
Subordinated liabilities	30	100 257	100 268
Other liabilities and provisions	31	14 089	19 872
T o t a l l i a b i l i t i e s		**5 551 785**	**4 280 480**
E q u i t y			
Share capital:		**374 938**	**275 000**
- Registered share capital	37	285 000	275 000
- Share premium	38	89 938	-
Retained earnings	39	**247 840**	**225 469**
- Profit from the previous years		225 469	223 315
- Profit for the current year		22 371	2 154
Other components of equity	40	**1 763**	**1 494**
T o t a l e q u i t y		**624 541**	**501 963**
TOTAL LIABILITIES AND EQUITY		**6 176 326**	**4 782 443**
Total capital adequacy ratio / Capital adequacy ratio (%)*	45	**13,31**	**14,92**

* As at 31 December 2014, the total capital ratio was presented, calculated in accordance with the Regulation of the European Parliament and of the Council (EU) No 575/2013 of 26 June 2013 on prudential requirements for credit institutions and investment firms and amending Regulation (EU) No 648/2012 (rules based on "Basel III"). As at 31 December 2013, the capital adequacy ratio was presented, calculated in accordance with the requirements of Article 128 of the Banking Law Act of 29 August 1997, as amended (rules based on "Basel II").

Explanatory notes presented on pages 8 to 91 constitute an integral part of these financial statements.

Financial statements in accordance with the International Financial Reporting Standards (IFRS) for the year 2014 (PLN '000)

Statement of changes in equity

Changes in the period from 1 January 2014 to 31 December 2014

	Note	Share capital			Retained earnings				Other components of equity		Total
		Registered share capital	Share premium	Paid unregistered share capital	Other supplementary capital	General banking risk reserve	Retained profit from the previous years	Profit for the current year	Valuation of available-for-sale financial assets	Actuarial gains and losses on post-employment benefits	
As at 1 January 2014		**275 000**	**-**	**-**	**192 315**	**31 000**	**2 154**	**-**	**1 459**	**35**	**501 963**
Net profit		-	-	-	-	-	-	22 371	-	-	22 371
Other comprehensive income (gross)		-	-	-	-	-	-	-	349	(17)	332
Deferred tax on other comprehensive income		-	-	-	-	-	-	-	(66)	3	(63)
Total comprehensive income		**-**	**-**	**-**	**-**	**-**	**-**	**22 371**	**283**	**(14)**	**22 640**
Transfer to general banking risk reserve	39	-	-	-	-	2 000	(2 000)	-	-	-	-
Transfer to supplementary capital	39	-	-	-	154	-	(154)	-	-	-	-
Issue of shares	37,38	10 000	90 000	-	-	-	-	-	-	-	100 000
Share issue costs	38	-	(62)	-	-	-	-	-	-	-	(62)
Transfer to registered share capital		-	-	-	-	-	-	-	-	-	-
As at 31 December 2014		**285 000**	**89 938**	**-**	**192 469**	**33 000**	**-**	**22 371**	**1 742**	**21**	**624 541**

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	Share premium	Paid unregistered share capital	Other supplementary capital	General banking risk reserve	Retained profit from the previous years	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		-	-	-	-	-	-	2 154	-	-	2 154
Other comprehensive income (gross)		-	-	-	-	-	-	-	(1 149)	43	(1 106)
Deferred tax on other comprehensive income		-	-	-	-	-	-	-	218	(8)	210
Total comprehensive income		**-**	**-**	**-**	**-**	**-**	**-**	**2 154**	**(931)**	**35**	**1 258**
Transfer to general banking risk reserve	39	-	-	-	-	4 000	(4 000)	-	-	-	-
Transfer to supplementary capital	39	-	-	-	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**

Explanatory notes presented on pages 8 to 91 constitute an integral part of these financial statements.

Financial statements in accordance with the International Financial Reporting Standards (IFRS) for the year 2014 (PLN '000)

Statement of cash flows

		Year ended 31 December	
	Note	2014	2013
A. Cash flows from operating activities		**(1 290 686)**	**87 401**
Profit before income tax		**29 475**	**4 897**
Adjustments:		***(1 320 161)***	***82 504***
Income tax paid		(5 917)	(6 414)
Amortisation and depreciation	24,25	4 310	4 162
Impairment of tangible fixed assets	13,25	25	
Interest income (income statement)	7	(218 996)	(227 065)
Interest expenses (income statement)	7	132 813	152 286
Interest received		211 294	236 059
Interest paid		(10 460)	(14 414)
Change in amounts due from other banks	33	(1)	-
Change in assets and liabilities on derivative financial instruments	33	(9 052)	(5 656)
Change in loans and advances to customers	33	(1 279 703)	58 041
Change in investment securities	33	(163 999)	(10 310)
Change in other assets		47 925	27 625
Change in amounts due to other banks	33	(23 078)	(260 440)
Change in amounts due to customers	33	(45 101)	116 091
Change in debt securities in issue	33	19 870	(3 210)
Change in hedge accounting adjustments related to fair value of hedged items		25 763	-
Change in other liabilities and provisions	33	(5 800)	15 793
Result on disposal of intangible assets and tangible fixed assets	13	8	19
Disclosure of intangible assets	24	(62)	-
Net income on investments in subsidiaries	23	-	(63)
Net cash from operating activities		**(1 290 686)**	**87 401**
B. Cash flows from investing activities		**(3 938)**	**(6 154)**
Investing activity inflows		**25**	**798**
Disposal of intangible assets and tangible fixed assets		25	20
Disposal of shares		-	778
Investing activity outflows		**3 963**	**6 952**
Purchase of intangible assets and tangible fixed assets	24,25	3 963	6 302
Purchase of shares		-	650
Net cash from investing activities		**(3 938)**	**(6 154)**
C. Cash flows from financing activities		**1 268 055**	**(34 243)**
Financing activity inflows		**2 051 891**	**1 198 014**
Loans and advances from banks		797 775	421 188
Due to the issue of debt securities	29	1 154 178	776 826
Due to the issue of shares	37,38	99 938	-
Financing activities outflows		**783 836**	**1 232 257**
Repayment of loans and advances from banks		-	129 942
Redemption of debt securities in issue	29	665 000	950 000
Interest paid on loans received, debt securities in issue, subordinated loan		118 836	152 315
Net cash from financing activities		**1 268 055**	**(34 243)**
Net increase / decrease in cash and cash equivalents (A+B+C)		**(26 569)**	**47 004**
Cash and cash equivalents as at the beginning of the reporting period, including:		**545 183**	**498 179**
Cash and balances with the central bank		7 378	3 069
Amounts due from other banks		22 377	10 282
Investment securities with maturity of up to 3 months from the date of purchase		515 428	484 828
Cash and cash equivalents as at the end of the reporting period, including:	**42**	**518 614**	**545 183**
Cash and balances with the central bank	18	7 669	7 378
Amounts due from other banks	19	30 972	22 377
Investment securities with maturity of up to 3 months from the date of purchase		479 973	515 428

Explanatory notes presented on pages 8 to 91 constitute an integral part of these financial statements.

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, mBank Hipoteczny S.A. 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 organisational 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 clients 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 government units 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' real 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 187 employees in 2014 and 144 employees in 2013.

The financial statements were signed by the Management Board of mBank Hipoteczny S.A. on 24 March 2015.

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 2014. These statements are standalone financial statements.

Both as at 31 December 2014 and as at 31 December 2013, mBank Hipoteczny S.A. did not have any subsidiaries.

The financial statements of mBank Hipoteczny S.A. have been prepared in accordance with the International Financial Reporting Standards as adopted for use in the European Union ("IFRS"), 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 principles. 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, i.e. in the period of at least 12 months following the balance sheet date.

2.2. Interest income and expenses

Income statement recognises all the interest income and expenses regarding financial instruments measured at amortised 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 inflows 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 income and interest expenses related to the interest measurement component of derivatives concluded as hedging instruments under fair value hedge are presented in the net interest income in the position interest income/expense on derivatives concluded under the hedge accounting.

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, other financial liabilities with deferred maturity, 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 charge calculation. 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 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, on a straight line basis, 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 expenses.

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

2.4. Revenue and expenses from sale of insurance products bundled with loans

The Bank treats offered insurance products as bundled with financial instruments, in particular when insurance product is offered to the customer only with a given financial instrument, i.e. it is not possible to purchase from the Bank the insurance product which is identical in a legal form, content and economic conditions without purchasing the financial instrument.

The Bank does not offer any insurance products not bundled with financial instruments.

The remuneration included in interest income is recognised over time as part of effective interest rate calculation for the bundled loan. The remuneration included in fee and commission income is recognised partly as upfront income and partly including deferring over time based on the analysis of the stage of completion of the service.

Due to the existence of marginal expenses directly related to the sales of the insurance product, they are recognised upfront by the Bank. In the event where the amount of the above expenses is material, the following approach is applied: expenses directly related to the sales of the insurance product bundled with a loan are settled in a similar manner as income, following the principle of matching income and expenses. A part of expenses is treated as an element adjusting the calculation of effective interest rate for interest income and the remaining part of expenses is recognised in fee and commission expenses as upfront cost or as cost accrued over time.

In relation to insurance products treated as bundled with a loan, the Bank estimates also the part of remuneration which in the future will be returned due to early termination of insurance contract and appropriately decreases interest income or fee and commission income to be recognised.

In the case of bundled products, where the premium is collected on a monthly basis and the customer may take out or give up the insurance on an on-going basis, the income is recognised monthly on a cash basis under commission income.

When recognising insurance income with respect to insurance bundled with a mortgage loan, in relation to premium collected on a one-off basis for the period of two years, the Bank, on a straight line basis and under interest income, aligns the level of income recognised in this period with the level of future remuneration to be received on a regular, monthly basis from premium collected after the second year of the insurance coverage.

2.5. 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.

2.6. Financial assets / Financial liabilities

2.6.1. 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.

<u>Loans and receivables</u>

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 cost), using the effective interest rate.

<u>Available-for-sale financial assets</u>

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/expenses on available-for-sale financial assets are recognised in net interest 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 purchase price (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 rate 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 2.10.

The measurement and the earnings or losses on the sales of financial assets measured at fair value through profit or loss are recognised in net trading income, except for the net interest income on derivatives, which is presented in the net interest income in the position Interest income/expense on derivatives classified into banking book.

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.

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.

2.6.2. 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 benefits 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 loans received,
- loans and advances received,
- other financial liabilities with deferred payment term,
- 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.

2.7. 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.

2.8. 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 3.1.3.

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 acquisition cost 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-downs 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 repayment of the entire current value 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 inflows 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.

A set of measures, defined by internal regulations and related to the renegotiation and restructuring of terms of loan agreements, defined as the Banks policy with respect to forbearance, was described in Note 3.1.7.

2.9. Cash and cash equivalents

Cash and cash equivalents comprise items which mature within three months of the date of purchase, 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.

2.10. Derivative financial instruments and hedge accounting

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 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 of recognising the resulting fair value gain or loss depends on whether the given derivative instrument is designated as a hedging instrument, and if it is, it also depends on the nature of the hedged item.

The Bank designates some derivative instruments as fair value hedges against a recognised liability (issued mortgage covered bonds at a fixed rate). Derivative instruments designated as hedges against positions maintained by the Bank are recorded by means of hedge accounting, subject to the fulfilment of the criteria specified in IAS 39, i.e.:

- At the inception of the hedge there is formal designation and documentation of the hedging relationship and the entity's risk management objective and strategy for undertaking the hedge. That documentation includes identification of the hedging instrument, the hedged item or transaction, the nature of the risk being hedged and how the entity will assess the hedging instruments effectiveness in offsetting the exposure to changes in the hedged item's fair value,
- The hedge is expected to be highly effective in offsetting changes in fair value attributable to the hedged risk, consistently with the originally documented risk management strategy for that particular hedging relationship,
- The effectiveness of the hedge can be reliably measured, i.e. the fair value of the hedged item that is attributable to the hedged risk and the fair value of the hedging instrument can be reliably measured,
- The hedge is assessed on an ongoing basis and determined to have been highly effective throughout the financial reporting periods for which the hedge was designated.

The Bank documents the objectives of risk management and the strategy of concluding hedging transactions, as well as at the time of concluding the respective transactions, the relationship between the hedging instrument and the hedged item. The Bank also documents its own assessment of the effectiveness of fair value hedging transactions, measured both prospectively and retrospectively from the time of their designation and throughout the period of duration of the hedging relationship between the hedging instrument and the hedged item.

Fair value hedges

Changes in the fair value of derivative instruments designated and qualifying as fair value hedges are recognised in the income statement together with any changes in the fair value of the hedged liability that is attributable to the risk hedged by the Bank.

In case a hedge has ceased to fulfil the criteria of hedge accounting, the adjustment to the carrying value of the hedged item for which the effective interest rate method is used is amortised to the income statement over the period to maturity.

Derivative instruments not fulfilling the criteria of hedge accounting

Changes of the fair value of derivative instruments that do not meet the criteria of hedge accounting are recognised in the income statement of the current period.

Rules for calculating write-downs (valuation adjustments) due to counterparty credit risk on the valuation of market-risk derivatives

Credit risk write-downs (valuation adjustments) for derivatives are created for customers 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 31 December 2014, the Bank had EUR 2,171 thousand (PLN 9,253 thousand) of collateral in respect of changes in the valuation of contracts with individual counterparties.

The Bank has the following derivative instruments in its portfolio:

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.

2.11. Intangible assets

Intangible assets are stated according to purchase prices adjusted for the costs of improvements (rebuilding, extension, reconstruction, adaptation or modernisation) and accumulated amortisation and impairment write-downs. Accumulated amortisation is calculated using the straight-line method, taking account of the economic 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 purchase price or manufacturing cost of an intangible asset which meets the recognition criteria.

Computer software

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 over the expected economic useful lives.

Costs of completed development projects

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 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.

Significant intangible assets as at 31 December 2014:

- Software of the agency model with a net value of PLN 1,375 thousand,
- Def3000/CL System with a net value of PLN 309 thousand,
- Software used to perform impairment tests and calculate impairment write-downs of PLN 173 thousand,
- vPlex license with a net value of PLN 159 thousand.

2.12. Tangible fixed assets

The carrying amount is the purchase price or manufacturing cost of a given asset, net of accumulated depreciation and accumulated impairment write-downs.

The purchase price or manufacturing cost 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 purchase price or manufacturing cost 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 purchase price or manufacturing cost 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 purchase price or manufacturing cost 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 selling price 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 disposal costs.

While determining the depreciation period and an annual depreciation rate, the economic 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 using a straight-line method, 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.

Useful lives of the individual groups of fixed assets are as follows:

- Technical equipment and machinery	5–10 years,
- IT equipment	3–7 years,
- Equipment and vehicles	5–10 years,
- Leasehold improvements	in the expected lease/rent period
- 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 purchase price or manufacturing cost, 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

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.

Liabilities or assets for deferred tax are recognised in their full amount according to the balance sheet method in connection with the existence of temporary differences between the tax value of assets and liabilities and their carrying value.

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 financial assets and of revaluation of actuarial gains or losses from the measurement of retirement and disability benefits are 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 price 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 in other operating income.

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. Retirement benefits and other employee benefits

Retirement and disability benefits

The Bank creates provisions for future liabilities in respect of retirement and disability benefits, determined on the basis of estimations of such liabilities, using an actuarial model. Current service cost and net interest on the net defined pension benefit liability are recognised in profit and loss. The 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 carrying 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.

For employees of the Bank having a material impact on the risk profile:

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.

For the Management Board of the Bank:

1) 60% of the discretionary bonus shall be paid in the year in which the discretionary bonus is granted, of which 50% in the form of cash payment and 50% in phantom shares;
2) 40% of the discretionary bonus shall be paid in three equal tranches in three consecutive years after the year in which the bonus is discretionary granted, of which 50% in the form of cash payment and 50% in phantom shares.

The Supervisory Board may decide to suspend as a whole or reduce the deferred tranche amount:

1) in view of the subsequent assessment of the Manager's work in a longer period than 1 financial year,
2) when at least one of the elements included in the Scorecard has not been met.

Moreover, the Supervisory Board may decide to suspend as a whole or reduce the discretionary bonus amount for a given financial year, and with regard to a deferred tranche, in a situation of balance-sheet loss or the threat of the same or of the Bank's insolvency. The suspension as a whole or reduction of the discretionary bonus and deferred tranche may also apply to the Discretionary bonus and deferred tranche paid to the Manager when the agreement has expired or has been terminated.

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

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 funds created by the Bank in compliance with the respective provisions of the law, i.e., the appropriate legislative acts, the Memorandum of Association.

<u>Registered share capital</u>

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

<u>Share premium</u>

Share premium is formed from the share premium obtained from the issue of shares reduced by the attached direct costs incurred with that issue.

- Share issue costs

Costs directly connected with the issue of new shares; they reduce the proceeds from the issue recognised in equity.

<u>Retained earnings</u>

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 earnings from the previous year,
- net profit/loss for the current year.

<u>Other components of equity</u>

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 using a straight-line method over the lease period. The Bank has no finance 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 average NBP 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.

Published standards and interpretations that have been issued and are applicable in the Bank for the annual periods beginning on 1 January 2014:

- Amendments to IAS 32, Financial Instruments: Presentation — Offsetting financial assets and liabilities, published by the International Accounting Standards Board on 16 December 2011, binding for annual periods beginning on or after 1 January 2014. The amendments were endorsed by the European Union on 13 December 2012.

  The amendments aim to eliminate inconsistencies in applying the requirements concerning offsetting financial assets and liabilities criteria.

  The amendments to the standard clarify the criteria that must be met by an entity to be able to offset financial assets and liabilities in the balance sheet, by:

  - clarifying the meaning of "currently has a legally enforceable title to set off", and
  - explaining when some gross settlement systems may be considered equivalent to net settlement of financial assets and liabilities.

  The Bank is of the opinion that the application of the amended standard will have no significant impact on the financial statements in the period of its initial application.

- Amendments to IAS 39, Novation of derivatives and continuation of hedge accounting, published by the International Accounting Standards Board on 27 June 2013, binding for annual periods starting on or after 1 January 2014.

  The amended IAS 39 provided relief from discontinuing the hedge accounting for a derivative that has been designated as a hedging instrument in an existing hedging relationship if the derivative is novated to a central clearing house following the introduction of a new law or regulation and it meets certain criteria.

  The Bank is of the opinion that the application of the amended standard will have no significant impact on the financial statements in the period of its initial application.

- Amendments to IFRS 10, IFRS 12 and IAS 27, Investment Entities, published by the International Accounting Standards Board on 31 October 2012, binding for annual periods starting on or after 1 January 2014. The amendments were endorsed by the European Union on 20 November 2013.

  The amendments define an investment entity and introduce an exception to consolidating particular subsidiaries for investment entities. These amendments require an investment entity to measure those subsidiaries at fair value through profit or loss in accordance with IFRS 9 Financial Instruments in its consolidated and separate financial statements. The amendments also introduce new disclosure requirements for investment entities in IFRS 12 and IAS 27.

The Bank does not meet the definition of an investment entity, therefore the use of the standard will not have a significant impact on the financial statements.

- Amendments to IFRS 10, IFRS 11 and IFRS 12 Consolidated Financial Statements, Joint Arrangements and Disclosure of Interests in Other Entities: Transition Guidance, published by the International Accounting Standards Board on 31 October 2012, binding for annual periods starting on or after 1 January 2014.

  The amendments clarify the date of initial application of IFRS 10 as the beginning of the annual reporting period in which IFRS 10 is applied for the first time. They precise also there is no requirement to adjust comparative periods, if the consolidation conclusion reached at the date of initial application of IFRS 10 is the same when applying IAS 27/SIC 12. Moreover, the amendments clarify additional relief from adjustment of comparative data for periods prior to the immediately preceding period in transition to IFRS 10, IFRS 11 and IFRS 12.

  The Bank is of the opinion that the application of the amended standards had no significant impact on the financial statements in the period of their initial application.

Published standards and interpretations that have been issued and are applicable in the Bank for the annual periods beginning on 1 January 2015:

- IFRIC 21, Levies, published by International Financial Reporting Standard Interpretations Committee on 20 May 2013, binding for annual periods starting on or after 1 January 2014. In the European Union interpretation is applicable for annual periods beginning on or after 17 June 2014.

  The published interpretation is aimed at defining the moment of recognition of a liability to pay a levy if that liability is within the scope of IAS 37 or whose timing and amount are certain in the financial statements, not addressing whether the recognition of a liability to pay a levy gives rise to an asset or an expense.

  The Bank is of the opinion that the application of IFRIC 21 will have no impact on the total level of recognised fees of the financial year, but it may have an impact on the level of such costs recognised in each quarter of the financial year.

- Improvements to IFRSs 2011-2013 were published by the International Accounting Standards Board on 12 December 2013, endorsed by the EU on 18 December 2014 and are binding for annual periods starting on or after 1 July 2014. In the EU, they are applicable for annual periods beginning on or after 1 January 2015.

  The improvements to the following standards were implemented during the cycle: IFRS 1 in terms of clarification of using the IFRSs that are effective by the first-time adopter, IFRS 3 in terms of the elimination from its scope the accounting for the formation of joint arrangement defined in IFRS 11 in the financial statements of the joint arrangement itself, IFRS 13 in terms of the clarification of the exception for measuring the fair value of a group of financial assets and financial liabilities based on price that would have been achieved for sale of net long position or transfer net short position in case of exposure to a specific risk, IAS 40 in terms of the clarification the reference between IFRS 3 and IAS 40 related to classification of a real property as investment property or owner-occupied property.

  The Bank is of the opinion that the application of the amended standards will have no significant impact on the financial statements in the period of their initial application.

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:

- IAS 19 (Amended), Defined Benefit Plans: Employee Contributions, published by the International Accounting Standards Board on 21 November 2013, approved by European Union on 17 December 2014 and binding for annual periods starting on or after 1 July 2014, in EU effective at the latest for financial years beginning on or after 1 February 2015.

The amendment relates only to contributions for defined benefit plans from employees or third parties. The amendment of the Standard is aimed at clarification and simplification the accounting requirements for contributions independent of the number of years of service, i.e. contributions that are a fixed percentage of the employee's salary, a fixed amount throughout the service period or dependent on the employee's age. In accordance with the amendment of the Standard such contributions should be recognised as a reduction in the service cost in the period in which the related service is rendered, instead of attributing the contributions to the periods of service.

The Bank is of the opinion that the application of the amended standard will have no significant impact on the financial statements in the period of its initial application.

- Improvements to IFRSs 2010 – 2012 Cycle were published by the International Accounting Standards Board on 12 December 2013, and were approved by European Union on 17 December 2014. Some of the amendments are binding for annual periods starting on or after 1 July 2014, and some effective prospectively for transactions occurring on or after 1 July 2014, in EU effective at latest for financial years beginning on or after 1 February 2015.

  The improvements to the following standards were implemented during the cycle: IFRS 2 in terms of changing definitions: "vesting condition", "market condition" and adding definitions: "service condition" and "performance condition", IFRS 3 in terms of clarification of classification a contingent consideration by an acquirer, IFRS 8 in terms of disclosure requirement of judgments made by management in applying the aggregation criteria for operating segments and disclosure of reconciliation of the total of the reportable segments' assets to the total assets, IFRS 13 in terms of clarification of doubts for the possibility of simplified measurement of short-term receivables and payables without discounting, when the effect of not discounting is immaterial, IAS 16 and IAS 38 in terms of proportionate restatement of accumulated depreciation or amortization, respectively, when an item of tangible fixed assets or intangible asset, respectively is revalued, IAS 24 in terms of identifying related party which provides key management personnel services to the reporting entity or to the parent of the reporting entity.

  The Bank is of the opinion that the application of the amended standards will have no 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, published by the International Accounting Standards Board on 24 July 2014, represents the final version of the standard, replaces earlier versions of IFRS 9 and completes the International Accounting Standards Board's project to replace IAS 39 Financial Instrument: Recognition and Measurement. The new standard addresses classification and measurement of financial assets and financial liabilities, impairment methodology and hedge accounting. IFRS 9 does not include hedge accounting concerning the portfolio of financial assets or liabilities, which constitutes a separate project of the International Accounting Standards Board. In relation to portfolio hedging of financial assets or liabilities, the Bank is still required to follow the provisions of IAS 39 in this respect. The new standard is binding for annual periods beginning on or after 1 January 2018.

  The Bank is of the opinion that the application of the standard will have an impact on the presentation of these instruments in the financial statements and on the impairment calculation. The Bank is currently estimating this impact.

- IFRS 11 (Amended), Accounting for acquisitions of interests in joint operations, published by the International Accounting Standards Board on 6 May 2014, binding for annual periods beginning on or after 1 January 2016.

  The amended standard requires the acquirer of a share in a joint operation in which the activity constitutes a business, as defined in IFRS 3 Business Combination, to apply all of the principles on business combinations accounting in IFRS 3 and other IFRSs except for those principles that conflict with the guidance in this IFRS. It applies to the acquisition of both the initial interests and additional interests in a joint operation in which the activity of the joint operation constitutes a business. Moreover, the acquirer shall disclose the information required by IFRS 3 and other IFRSs for business combinations.

  The Bank is of the opinion that the application of the amended standard will have no significant impact on the financial statements in the period of its initial application.

- IFRS 14, Regulatory Deferral Accounts, published by the International Accounting Standards Board on 30 January 2014, binding for annual periods starting on or after 1 January 2016.

  The Standard permits an entity that adopts IFRS to continue to use, in its first and subsequent IFRS financial statements, its previous accounting principles for the recognition, measurement, impairment and derecognition of regulatory deferral account balances. The Standard requires to present regulatory deferral account balances as separate line items in the statement of financial position and to present movements in those account balances as separate line items in the statement of profit or loss and other comprehensive income. The disclosures to identify the nature of, and risks associated with, the rate regulation that has resulted in the recognition of regulatory deferral account balances are also required.

  The Bank is of the opinion that the application of the standard will have no significant impact on the financial statements in the period of its initial application.

- IFRS 15, Revenue from Contracts with Customers, published by the International Accounting Standards Board on 28 May 2014, binding for annual periods beginning on or after 1 January 2017.

  IFRS 15 introduces new principles of revenue recognition. The core principle is that an entity recognises revenue to depict the transfer of promised goods and services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. According to a new IFRS 15 revenue is recognised when the customer obtains control of these goods or services. Depending on the fulfilment of certain conditions revenues are either recognised over time throughout the duration of the contract if a performance obligation is satisfied over time, or at a point in time when the customer obtains control of these goods or services.

  The Bank is of the opinion that the application of the standard will have no significant impact on the financial statements in the period of its initial application.

- Amendments to IAS 16 and IAS 38, Clarification of acceptable methods of depreciation and amortization, published by the International Accounting Standards Board on 12 May 2014, binding for annual periods beginning on or after 1 January 2016.

  The amended IAS 16 prohibits the use of a revenue-based method for depreciating tangible fixed assets. A depreciation method that is based on revenue that is generated by an activity of the entity is not appropriate, because the revenue generated by an activity that includes the use of an asset reflects factors other than the consumption of the economic benefits of the asset.

  The amended IAS 38 includes a rebuttable presumption that a revenue-based method for amortization of an intangible asset is inappropriate for the same reasons as in the case of tangible fixed assets presented in amended IAS 16. However, the presumption in case of amended IAS 38 could be overcome in two circumstances: when it can be demonstrated that revenue is highly correlated with the consumption of the economic benefits embodied in an intangible asset and when the right embodied by an intangible asset is expressed as a total amount of revenue to be generated.

  The Bank is of the opinion that the application of the amended standards will have no significant impact on the financial statements in the period of their initial application.

- Amendments to IAS 16 and IAS 41 Agriculture: Bearer Plants published by the International Accounting Standards Board on 30 June 2014, binding for annual periods beginning on or after 1 January 2016.

  The amended IAS 16 and IAS 41 introduce the obligation of recognising bearer plants in the same way as tangible fixed assets and of using the requirements of IAS 16 measuring them either at cost or at revaluated amount. IAS 41 still applies to the produce on those bearer plants, which should be measured at fair value less costs to sell. Bearer animals are not covered by the amendments.

  The Bank is of the opinion that the application of the amended standards will have no significant impact on the financial statements in the period of their initial application.

- Amendments to IAS 27, Equity method in separate financial statements, were published by the International Accounting Standards Board on 12 August 2014, and are binding for annual periods beginning on or after 1 January 2016.

The amended IAS 27 re-establish the possibility of equity method application for investments in subsidiaries, joint ventures and associates in separate financial statements. The entity preparing separate financial statements should account for investments in subsidiaries, joint ventures and associates at cost or according to IFRS 9 or using the equity method as described in IAS 28. The dividend from a subsidiary, a joint venture or an associate is recognised in profit or loss or as a reduction from the carrying amount of the investment if the equity method is used.

The Bank is of the opinion that the application of the amended standard will have no significant impact on the financial statements in the period of its initial application.

- Amendments to IFRS 10 and IAS 28, Sale or contribution of assets between an investor and its associate or joint venture, published by the International Accounting Standards Board on 11 September 2014, binding for annual periods beginning on or after 1 January 2016.

The amendments to IFRS 10 and IAS 28 eliminate inconsistency between these standards and clarify the accounting approach in a situation when a parent loses control of a subsidiary as a result of transaction between a parent and its associate or joint venture. The accounting approach depends on whether contribution of assets to an associate or a joint venture constitute a business as defined in IFRS 3 Business Combinations. If assets constitute a business, the amendments introduce a requirement of full recognition gain or loss resulting from the transaction. If assets do not constitute a business, a gain or loss resulting from the transaction is recognised only to the extent of the unrelated investors' interests in that associate or joint venture.

The Bank is of the opinion that the application of the amended standards will have no significant impact on the financial statements in the period of their initial application.

- Annual Improvements to IFRSs 2012-2014, changing 4 standards, published by the International Accounting Standards Board on 25 September 2014, binding for annual periods beginning on or after 1 January 2016.

The improvements to the following standards were implemented during the cycle: IFRS 5 in the situation when an asset is reclassified from being held for sale to being held for distribution to owners or from being held for distribution to owners to being held for sale, then the change in classification is considered a continuation of the original plan of disposal. Additionally, when assets no longer meet the criteria for held for distribution to owners (without meeting the held-for-sale criteria), the entity should cease to apply held-for-distribution accounting in the same way as it ceases to apply the held-for-sale accounting when they no longer meet the held-for-sale criteria; IFRS 7 when an entity transfers a financial asset retaining the right to service that financial asset for a fee that is included in a servicing contract, whether the entity has a continuing involvement as a result of the servicing contract for the purpose of disclosure requirements. Additionally, IFRS 7 clarifies that disclosures regarding offsetting financial assets and liabilities are not specifically required for all interim periods, unless it is required by IAS 34; IAS 19 in terms of clarification that high quality corporate bonds used to determine a discount rate of post-employment benefit obligations shall be in the same currency as the currency of the post-employment benefit obligations. Assessment whether there is a deep market in such high quality corporate bonds should be made for the currency, not for a country; IAS 34 in terms of clarifying the meaning of disclosure of information' elsewhere in the interim financial statements' and additionally it introduces a requirement to incorporate disclosure in interim financial statement by cross-reference to information in another statement.

The Bank is of the opinion that the application of the amended standards will have no significant impact on the financial statements in the period of their initial application.

- Amendments to IAS 1, Disclosure Initiative, published by the International Accounting Standards Board on 18 December 2014, binding for annual periods starting on or after 1 January 2016.

The amendments to IAS 1 include the clarification of the material information with particular regard to the reduction of immaterial information in financial statements. Moreover, specific items in financial statements may be the subject to both aggregation and disaggregation depending on its materiality. IAS 1 was also completed with the requirements regarding the presentation of subtotals in financial statements. Additionally, the information presented in the notes of financial statements may be presented in a systematic manner, however in determining a systematic manner, the entity shall consider the effect on the understand ability and comparability of its financial statements. The guidelines regarding the identification of significant accounting policies were deleted in the amendments to IAS 1.

The Bank is of the opinion that the application of the amended standards will have no significant impact on the financial statements in the period of their initial application.

- Amendments to IFRS 10, IFRS 12 and IAS 28, Investment entities: applying the consolidation exception, published by the International Accounting Standards Board on 18 December 2014, binding for annual periods starting on or after 1 January 2016.

  The amendments to IFRS 10, IFRS 12 and IAS 28 exempt to the requirement of presenting consolidated financial statements by a parent entity if its ultimate or any intermediate parent entity produces financial statements that are available for public use and comply with IFRSs, in which subsidiaries are consolidated or are measured at fair value through profit or loss. Additionally, the requirement to consolidation was limited to the situation when an investment entity has a subsidiary that is not itself an investment entity and whose main purpose and activities are providing services that relate to the parent entity's investment activities. Moreover, when applying the equity method in an associate or joint venture that is an investment entity, an investor retain the fair value measurement applied by that investment entity associate or joint venture to the investment entity associate's or joint venture's interests in subsidiaries.

  The Bank is of the opinion that the application of the amended standards will have no significant impact on the financial statements in the period of their initial application.

3. Financial risk management

3.1. 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 credit decisions and assessing credit risk.

3.1.1. Collaterals

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 pledge register, 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 mortgage lending value, approved by the Banking Supervision Commission — currently the Polish Financial Supervision Authority — and issued based on the Act of 29 August 1997 on covered bonds and mortgage banks (consolidated text Journal of Laws of 2003, No 99, item 919 as amended), 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 mortgage lending value issued by mortgage banks. Thus, the Bank ensures that the value of collateral for a credit exposure secured with a mortgage is sufficient throughout the term of an agreement. This assurance is based on the analysis of return on a given real 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 a mortgage collateral 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 mortgage register in the first place — for refinancing the commercial properties, financing the commercial real estate developers, financing the housing developers, financing land purchase, loans for natural persons, loans for natural person — agency model, pooling,
- 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 developers, loans for natural persons, loans for natural person — agency model, pooling,
- 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 blank promissory note agreement — 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 or SPVs established by local government units.

In the case of commercial loans, 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.

In accordance with IFRS 10, the Bank conducts analysis of the assessment of the Bank's control of entities. The Bank did not make any investments in securities or shares of other business entities, providing it with current ability to direct the relevant activities of these entities and does not have any subsidiaries or affiliates, therefore the analysis concerns possible interactions between the Bank and entities credited by the Bank.

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 legal collateral taking into account the nature of the transaction, i.e. 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.

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

The Bank uses rating models to analyse the quality of the loan portfolio, which are updated on an annual basis. The rating system currently covers more than 85.29% of the sum total of risk weighted exposures in accordance with the standard method.

The Bank uses rating models:

- for the purpose of credit risk management, including to make credit decisions, assess credit risk of transactions and capital adequacy — in the case of the commercial portfolio,
- for the purpose of credit risk management, including to make credit decisions, assess credit risk of transactions, determine impairment write-downs and, ultimately, for the purpose of capital adequacy — for exposures forming part of the retail portfolio acquired in cooperation with mBank S.A.

Commercial portfolio.

In the area of commercial loans, the Bank uses rating system to assess the risk of transactions, covering 11 rating models dedicated to individual segments of the commercial property market and the transition function model enabling the determination of a supervisory category based on score assigned as part of the internal model.

Ratings analysing the structure of transactions are applicable with respect to financing executed:

- using "project finance" where, as a rule, the borrower is a special purpose vehicle,
- for various types of transactions that relate to financing or refinancing the construction/purchase 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 to be used as commercial premises, offices or warehouses.

The Bank's models take into account different stages of financing of transactions — financing of construction or financing of purchase/refinancing of completed real property. The criteria cover areas related to:

- real property: location, legal status, functional properties of premises,
- characteristics of local market: relationship between demand and supply for a given type of premises, business activity ratio in the region,
- analysis of cash flows generated by the real property: amount, stability, currency adjustment, stress tests,
- quality assessments concerning the project sponsor and its financial potential, as well as intention to support the project.

The Bank applies an aggregation method, assigning exposures to relevant risk categories, specifying supervisory values of expected loss (EL) and risk weights.
Assignment to relevant supervisory categories is conducted after the risk assessment for the transaction using internal rating models developed by the Bank and the transition function model, providing a transformation of the score assigned as part of the above internal models into supervisory categories.

Retail loan portfolio acquired in cooperation with mBank S.A.

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 2014.

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 real 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 is 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.

Additional information.

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 organisational form of borrowers.

Capital requirement for credit risk calculated using the advanced internal rating-based approach is presented in Note 45.

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.

Loans to individuals are monitored on a monthly basis for the timeliness of repayment and regularities as regards the established effective mortgage collateral. In the same period, the implementation of all contractual obligations of the customer is monitored (including insurance of the real property and assignment of rights under policies).

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. Moreover, the implementation of the investment and settlements with contractors is monitored on a monthly basis — in the case of financing of construction.

As disclosed in Note 3.1.5., non-overdue, unimpaired loans account for 92.17% of the gross amount of loans and advances to customers. The remaining 7.83% of the amount of the loan portfolio represents past due, unimpaired loans (4.41%) as well as impaired loans (3.42%).

3.1.3. Impairment measurement

The Bank measures the impairment of credit exposures in accordance with the International Accounting Standard No 39.

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
- retail loan portfolio acquired in cooperation with mBank S.A.

The commercial portfolio is divided into two sub-portfolios to distinguish between commercial loans (development loans, commercial loans and loans to legal entities) and other loans to sole traders.

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

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.

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.

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 due to a visible deterioration of creditworthiness of the debtor,
b) Bank's disposal of exposure at a significant economic loss associated with changes of 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.

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 Bank calculates impairment charges based on a case-by-case analysis (commercial and public sector portfolio) and portfolio analysis (retail portfolio and those exposures from the commercial and public sector portfolio for which the case-by-case analysis did not reveal any impairment).

The process of calculation of impairment write-downs in the case-by-case analysis consists in:

a) determining the estimated future cash flows (repayments) both from the collateral and repayments made by borrowers, taking into account planned costs,
b) calculation of the difference between the carrying amount of a given asset and the current value of estimated recoveries and costs discounted using the effective interest rate,
c) impairment write-down of accounting records.

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.

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 in the portfolio analysis.

The portfolio analysis covers all retail and commercial loans which are not subject to the case-by-case analysis. For the purposes of impairment measurement in the portfolio analysis the Bank does not use the rating model. It, however, uses parameters, estimated for the purpose of this analysis, specifying the cure ratio, faulty collateral ratio and the recovery to collateral ratio (ZLGD, BD, CRR), as well as the debt to collateral ratio (LTV), used to calculate LGD in the portfolio analysis and, additionally, PD and LIP parameters. The Bank assumes that current LIP is 6 months. The PD parameter is currently determined using 18-month time series. Each separate portfolio has its own set of ZLGD, BD, CRR and PD parameters.

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

Financial statements in accordance with the International Financial Reporting Standards (IFRS) for the year 2014 (PLN '000)

Retail loan portfolio acquired in cooperation with mBank S.A.

It is assumed that there is evidence of impairment of a retail exposure if a natural person who has obligations due to a given product is in the state of default, i.e.:

a) overdue status of at least one credit facility of the debtor continues for a period exceeding 90 days and the total amount of past due credit exposures of the debtor (overdue status exceeding 31 days) exceeds PLN 500,
b) one of the customer's transactions is subject to restructuring,
c) a loan receivable is sold at a substantial economic credit loss,
d) the Bank files a request to initiate enforcement proceedings, bankruptcy or reorganisation proceedings (resulting in a possible omission of or delay in repayment) by the debtor,
e) impairment charge has been created as a result of significant deterioration in the customer's creditworthiness.

The gross carrying amount of the portfolio of retail loans acquired as part of cooperation with mBank S.A., as at 31 December 2014, was PLN 784,440 thousand.

Starting from September 2014, the calculation of impairment write-downs for balance sheet credit exposures and provisions for off-balance sheet credit exposures is based on risk parameters determined using the methodology applied for the purpose of the advanced internal rating-based approach (AIRB). These parameters are subject to adjustments in order to comply with applicable regulations.

The main change was the method of recognising the impairment which, in the new method of estimation, is based on all available credit data of the customer and not on data available with respect to a single product, as it was before.

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

As at the end of 2014 and 2013, 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. 92.17% 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 2013: 86.60% and 100%, respectively).

Maximum exposure to credit risk — financial effect of collaterals

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

As at 31 December 2014	Gross amount	Established impairment write-downs	Impairment write-downs without the collateral cash flows	Financial effect of collaterals
Balance sheet data				
Amounts due from other banks	**30 972**	**-**	**-**	**-**
Loans and advances to customers, including:	**5 413 440**	**(87 699)**	**(203 483)**	**115 784**
Corporate customers	4 375 564	(85 356)	(196 144)	110 788
Individual customers	862 951	(2 291)	(7 287)	4 996
Public sector customers	174 925	(52)	(52)	-
Total balance sheet data	**5 444 412**	**(87 699)**	**(203 483)**	**115 784**
Off-balance sheet data				
Loan commitments	1 076 968	(1)	(5)	4
Total off-balance sheet data	**1 076 968**	**(1)**	**(5)**	**4**

As at 31 December 2013	Gross amount	Established impairment write-downs	Impairment write-downs 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**
Corporate customers	3 799 524	(73 527)	(234 642)	161 115
Individual customers	95 754	(1 994)	(6 044)	4 050
Public sector customers	225 302	(67)	(67)	-
Other receivables	8	-	-	-
Total balance sheet data	**4 142 965**	**(75 588)**	**(240 753)**	**165 165**
Off-balance sheet data				
Loan commitments	969 798	-	-	-
Total off-balance sheet data	**969 798**	**-**	**-**	**-**

3.1.5. Loans and advances to customers and banks

Loans and advances to customers	31.12.2014		31.12.2013	
	exposure (PLN '000)	share/coverage (%)	exposure (PLN '000)	share/coverage (%)
Not overdue, without impairment recognised	4 989 802	92,17	3 568 460	86,60
Overdue, without impairment recognised	238 774	4,41	333 463	8,09
Items with impairment recognised	184 864	3,42	218 665	5,31
Total gross	**5 413 440**	**100,00**	**4 120 588**	**100,00**
Impairment write-down on loans not overdue, without impairment recognised	(8 214)	0,15	(6 528)	0,16
Impairment write-down on loans overdue, without impairment recognised	(487)	0,01	(678)	0,02
Impairment write-down on loans with impairment recognised	(78 998)	1,46	(68 382)	1,66
Total impairment write-down	**(87 699)**	**1,62**	**(75 588)**	**1,84**
Total net	**5 325 741**	**98,38**	**4 045 000**	**98,16**

The table below presents amounts due from banks:

Amounts due from other banks	31.12.2014		31.12.2013	
	exposure (PLN '000)	share/coverage (%)	exposure (PLN '000)	share/coverage (%)
Not overdue, without impairment recognised	30 972	100,00	22 377	100,00
Total gross	**30 972**	**100,00**	**22 377**	**100,00**
Total net	**30 972**	**100,00**	**22 377**	**100,00**

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

Financial statements in accordance with the International Financial Reporting Standards (IFRS) for the year 2014 (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.

	score from internal models		31.12.2014	31.12.2013
	[SCOREmin	SCOREmax)		
Exposures permanently exempted from the IRB approach	no rating	no rating	580 153	664 702
Exposures temporarily exempted from the IRB approach — specialised lending, including:			-	473 361
- supervisory category 1	48	54	-	4 941
- supervisory category 2	26	48	-	461 080
- supervisory category 3	12	26	-	7 340
Exposures temporarily exempted from the IRB approach — retail portfolio acquired in cooperation with mBank S.A.			780 380	6 097
Exposures subject to the IRB approach — specialised lending, including:			3 629 269	2 424 292
- supervisory category 1	48	54	5 642	4 958
- supervisory category 2	26	48	3 132 300	2 243 279
- supervisory category 3	12	26	433 326	149 280
- supervisory category 4	1	12	5 787	-
- supervisory category 5	default	default	52 214	26 775
Other receivables	no rating	no rating	-	8
Total			**4 989 802**	**3 568 460**

To calculate the capital requirement in respect of credit risk, the Bank applies the advanced internal rating-based approach, with the use of the supervisory approach in regard to assigning risk categories to exposures due to specialised lending. The assignment to a relevant supervisory category is conducted after the transaction risk assessment, using internal rating models developed by the Bank and the transition function model, providing a transformation of the score assigned as part of the internal models into supervisory categories. Individual supervisory categories listed in the table above specify the supervisory risk weights and expected losses.

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

	31.12.2014	31.12.2013
Corporate customers	3 965 062	3 264 411
Individual customers	849 815	84 388
Public sector customers	174 925	219 653
Other receivables	-	8
Total customers	**4 989 802**	**3 568 460**
Banks	30 972	22 377
Total	**5 020 774**	**3 590 837**

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

	31.12.2014	31.12.2013
Loans and advances with limited credit risk	420 687	473 994
Loans and advances with standard credit risk	4 516 901	3 057 654
Loans and advances with increased credit risk	52 214	36 812
Total	**4 989 802**	**3 568 460**

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.

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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 credit exposures.

Evaluation of the credit quality of derivatives

	31.12.2014	31.12.2013
Derivatives with limited credit risk	37 291	12 913
Total	**37 291**	**12 913**

All derivative transactions (except FX SPOT transactions) as at 31 December 2014 and 31 December 2013 were transactions concluded with mBank S.A., therefore the Bank assesses the amount of credit risk associated with such instruments as limited credit risk.

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 granted in cooperation with mBank S.A., 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 recognise 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 2014)	Corporate customers	Individual customers	Public sector customers	Total customers
up to 30 days	180 581	6 314	-	186 895
from 31 to 60 days	-	172	-	172
from 61 to 90 days	624	467	-	1 091
more than 90 days	50 616	-	-	50 616
Total	**231 821**	**6 953**	**-**	**238 774**

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

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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	Corporate customers	Individual customers	Total customers
31 December 2014			
Impaired loans and advances (gross amount)	178 681	6 183	184 864
Estimated recovery from contributions and collaterals	**101 531**	**3 944**	**105 475**
Impairment write-downs	**77 074**	**1 924**	**78 998**
Bank and mortgage value of real estate constituting collateral for loans	**247 962**	**16 506**	**264 468**
31 December 2013			
Impaired loans and advances (gross amount)	212 864	5 801	218 665
Estimated recovery from contributions and collaterals	**146 365**	**3 713**	**150 078**
Impairment write-downs	**66 523**	**1 859**	**68 382**
Bank and mortgage value of real estate constituting collateral for loans	**247 295**	**15 446**	**262 741**

In 2014, just as in 2013, 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 revaluating 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.

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3.1.6. 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 real 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.

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.

In 2014, the Bank did not reposes any collateral. As at 31 December 2014 and 31 December 2013, the value of repossessed collateral amounted to PLN 8,192 thousand.

Changes in repossessed collateral

	Period from 01.01.2014 to 31.12.2014	Period from 01.01.2013 to 31.12.2013
As at the beginning of the period	**8 192**	**89 073**
Increase (due to)	-	11 314
- repossessed real estate	-	8 172
- activated transaction costs	-	20
- reversal of impairment write-downs on sold properties	-	3 122
Decrease (due to)	-	(92 195)
- sale of real estate	-	(92 066)
- establishment of impairment write-downs	-	(129)
As at the end of the period	**8 192**	**8 192**

3.1.7. Policy of mBank Hipoteczny S.A. on forbearance

The Bank offers forbearance to assist customers who are temporarily in financial distress and are unable to meet their original contractual repayment terms, through agreements with less restrictive terms of repayment, without which financial difficulties would prevent satisfactory repayment under the original terms and conditions of the loan agreement.

These agreements may be initiated by the customer or the Bank and include debt restructuring, new repayments schedule, capital repayments deferrals with interest repayments kept.

The type of concession offered should be appropriate to the nature and the expected duration of the customer's financial distress. Clear demonstration from the customer of both willingness and ability to repay is necessary to conclude agreement. Before any concession is granted, an assessment of customer's ability to repay is undertaken to ensure suitability of the offer.

The Bank renegotiates loan agreements with customers in financial difficulties to maximise possibility of receivables repayment and minimise the risk of default.

In relation to retail customers, in accordance with the Forbearance policy, forbearance measures may take various forms, depending on the type and scale of the customer's financial problems. Short-term measures consist mainly in temporary reduction of instalment amounts or suspension of principal instalments while maintaining the repayment of interest. For customers under long term financial distress extension of contractual repayment schedule may be offered by the Bank, which can include instalments reduction.

For the corporate clients in financial distress, the Bank applies, in accordance with the forbearance policy, a broad range of measures aimed at supporting the business process, starting from abandoning activities to which the Bank is entitled in the case of violation of contractual terms or covenants and finishing on restructuring of loan agreements. Restructuring agreement may waive or ease additional terms included in the original agreement, if such strategy is optimal for the survival of the customer's business.

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The risk of non-repayment of the portfolio of products covered by the forbearance policy is mitigated by the amount of PLN 543,961 thousand of collateral accepted, therefore the possible impact of this portfolio on the deterioration of quality of the entire portfolio of the Bank is significantly limited.

Forbearance activities have been an integral part of mBank Hipoteczny S.A.'s risk management for many years. Due to the adaptation of the reporting requirements of the EBA in 2014 (ITS on Supervisory reporting on forbearance and non-performing exposures under article 99(4) of Regulation (EU) No. 575/2013), the recognition and recording of forbearance was changed. Therefore, data currently available in the Bank's systems and used for reporting purposes are not comparable with previous years' data.

As at the end of 2014, the structure of loan portfolio in the forbearance category at mBank Hipoteczny was as follows:

Balance sheet data	Gross value	Of which defaulted	Provisions created	Net value
Loans and advances to customers, including:	336 133	197 029	35 453	300 680
Individual customers	375	-	1	374
Corporate customers	335 758	197 029	35 452	300 306
Total balance sheet data	**336 133**	**197 029**	**35 453**	**300 680**

The size of the portfolio of customers who received a concession from the Bank remains insignificant in relation to the total size of the Bank's loan portfolio. The share of the forborne portfolio is 6.2% of the whole portfolio. More than half of the forborne portfolio (58.62%) is recognised in the default category. The portfolio of exposures in the default category was covered by write-downs in 17.99%. The risk of non-repayment of the forbearance portfolio is mitigated by collateral accepted in the form of mortgage on real property with the mortgage lending value of PLN 543,961 thousand (including PLN 347,529 thousand in the default category).

Changes of the carrying amount of exposures in the forbearance category

	Gross value	Of which defaulted	Provisions created	Net value
Balance as at 31 December 2013	**226 338**	**219 312**	**41 332**	**185 006**
Outputs	(61 524)	(54 499)	(8 057)	(53 467)
Change in exposure	(16 760)	(16 760)	1 535	(18 295)
New forbearance	188 079	48 976	643	187 436
Balance as at 31 December 2014	**336 133**	**197 029**	**35 453**	**300 680**

Exposures in the forbearance category by the nature of the concession granted, as at 31 December 2014

Type of concession (31 December 2014)	Gross value	Of which defaulted	Provisions created	Net value
Refinancing	22 125	22 125	46	22 079
Modification of terms and conditions	314 008	174 904	35 407	278 601
Total	**336 133**	**197 029**	**35 453**	**300 680**

Unimpaired exposures in the forbearance category by period of overdue

Forborne exposures without impairment recognised (31 December 2014)	Gross value	Of which defaulted	Provisions created	Net value
Not overdue	175 687	45 963	365	175 322
up to 30 days	17 983	8 603	37	17 946
from 31 to 90 days	-		-	-
more than 90 days	45 571	45 571	88	45 483
Total	**239 241**	**100 137**	**490**	**238 751**

Financial statements in accordance with the International Financial Reporting Standards (IFRS) for the year 2014 (PLN '000)

Impaired exposures in the forbearance category by period of overdue

Forborne exposures with impairment recognised (31 December 2014)	Gross value	Of which defaulted	Provisions created	Net value
Not overdue	54 372	54 372	23 537	30 835
up to 30 days	-	-	-	-
from 31 to 90 days	12 902	12 902	900	12 002
more than 90 days	29 618	29 618	10 526	19 092
Total	**96 892**	**96 892**	**34 963**	**61 929**

Exposures in the forbearance category by industry structure

As at 31 December 2014	Gross value	Of which defaulted	Provisions created	Net value
Activity related to the real estate market	202 689	100 958	34 310	168 379
Building industry	96 071	96 071	1 065	95 006
Professional, scientific and technical activity	36 998	-	77	36 921
Individuals	375	-	1	374
Total	**336 133**	**197 029**	**35 453**	**300 680**

Retail banking

The Bank does not treat loans with amended terms as subject to forbearance policy in cases when the amendments result from the customer's request and there are no current or expected financial difficulties of the customer and, additionally, modifications of the contractual conditions meet the criteria of decision policy for a healthy portfolio. In the normal course of cooperation with a customer, a customer who is not in financial distress applies for modification of contractual terms, e.g. with respect to renegotiation of pricing conditions due to a change in market conditions or to improve its ability to service another loan. If such application meets all criteria for a decision and is provided on market conditions, then such loan is not classified in the forbearance category.

In a case when a customer applies for an extension of maturity, reduction of the amount of instalments paid or other easement of terms and when this results from the customer's financial difficulties, the modified agreements are treated as forbearance products covered by the forbearance policy and are appropriately disclosed in the financial statements.

Forbearance products available in retail banking are offered only to customers who are in financial distress. The type of the forbearance product offered depends on the scale and nature of the customer's financial distress.

The following list does not exhaust all possible forbearance measures that are subject to the forbearance policy, but it includes the most common which are:

- using an individual repayment schedule,
- maturity extension/ extension of loan duration,
- restructuring,
- interest deferrals,
- principal deferrals,

assuming that the failure to apply the changes could result in the failure to repay the loan, and consequently in the loss on the part of the Bank.

Forbearance measures of a short-tem nature focus on temporary reductions of instalment amounts and may take the form of principal repayments suspension with only interest repayments kept.

For customers under long term financial distress extension of contractual repayment schedule or debt restructuring may be offered. In case of debt refinancing, as a rule, client is reclassified into the default category.

The need to grant another forbearance product results in a reclassification of the product to the non-performing category, and when there is no regular servicing, when the overdue period exceed 90 days, the customer is reclassified to the default category.

This portfolio is subject to regular review and reporting to the Risk Division management. The effectiveness of undertaken actions, regularity of restructured products' service in respect of types of products and clients' segment are subject to assessment.

The Bank ceases to recognise the product as forborne when:

- the loan repayment is recognised as performing,
- at least 2 years after recognising exposure as performing have passed or the contract was never in the non-performing category when the concession was granted,
- regular proceeds in significant amounts occurred on account of held receivables or interest (delays in repayment on the contract not exceeding 31 DPD in a material amount), at least from the middle of the trial period,
- none of the debtor exposures is overdue more than 31 days at the end of the trial period, in the amount of more than PLN 500.

The portfolio of products with the forbearance status in the retail part, as at 31 December 2014, amounted to PLN 375 thousand.

Corporate banking

Credit relationships between the Bank and corporate clients are based on products for which the granting conditions take into account the type of business activity conducted by the Client and are subject to negotiations.

Mortgage loans renegotiated due to commercial reasons, e.g. in the case of material improvement of the client's financial position or in order to maintain relationship with the client when there is no difficult credit situation are not treated as forbearance and are not subject to the following disclosure.

Forbearance exists only then due to current or future difficult financial position of the client, the Bank grants products on conditions below standard conditions applicable at the Bank which, in different circumstances, would not be accepted.

Modification of terms is treated as a concession subject to the forbearance policy when it improves the client's ability to repay the debt or prevents the client's default.

For the corporate clients in financial distress, the Bank applies a broad range of measures aimed at supporting the business process of the Client, however the following list does not exhaust all possible forbearance restructuring measures that are subject to the forbearance policy, but it includes the most common which are:

- loan increase,
- change of the repayment schedule,
- extension of the lending period,
- restructuring (medium or long term refinancing),
- capitalisation of interest,
- reduction of the Bank's margin,
- providing a grace period for the repayment of principal while maintaining the repayment of interest,
- covenant waiver.

An impairment assessment based on a case-by-case analysis is performed in each situation when any criterion of recognising an exposure as default was found, in accordance with methodology applicable at the Bank.

The portfolio of loans classified to the forbearance category is subject to a special monitoring at the Bank by all units participating in the lending process and to an assessment whether there are any indications of permanent impairment of the Bank's receivables. Transactions classified to this category remain in this portfolio and are disclosed as forbearance for at least 24 months after the date of granting the concession (so-called trial period). In order to conclude that the customer has returned to the regular category the debt must be serviced in a proper manner and there must be no amount overdue at the end of the trial period. A customer may be removed from the forbearance portfolio before the end of the trial period only when the debt has been paid in full.

All credit products granted to a customer handled in the restructuring area in the Bad Loans Section in the Credit Risk Department have the forbearance status and are subject to disclosure.

The portfolio of products with the forbearance status in the corporate part, as at 31 December 2014, amounted to PLN 335,758 thousand.

3.1.8. Debt instruments: investment securities

The value of investment securities and amounted to PLN 735,220 thousand as at 31 December 2014, compared to PLN 605,824 thousand as at 31 December 2013. Both as at 31 December 2014 and as at 31 December 2013, debt instruments had a rating of A on the scale of Fitch Rating agency. Investment securities with a carrying amount of PLN 200,614 thousand constitute an additional collateral of liabilities in respect of mortgage and public sector covered bonds issued. Investment securities with a carrying amount of PLN 2,123 thousand constitute a collateral of liabilities in respect of the guaranteed deposits protection fund. Investment securities with collaterals have been presented in Note 36.

Both as at 31 December 2014 and as at 31 December 2013, all investment securities were neither past due nor impaired.

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

<u>Risk of geographical concentration</u>

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.

<u>Risk of concentration of large exposures, risk of concentration of exposures</u>

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 organisation, 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.

Risk of industry concentration

The Bank concentrates its activities on granting loans secured with a mortgage on real estate to legal entities, loans to local government units, 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.

As at 30 November 2014, the limit of concentration of exposure to a group of affiliates, specified in Article 71 section 1 of the Banking Law, was exceeded at the Bank. The total exposure to a group of affiliates constituted 29.1% of the Bank's own funds. The exceeding of the limit of 25% of own funds was of a technical nature and did not constitute an increase in the Bank's risk. As at 31 December 2014, no limits were 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 estimating risk parameters. 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 estates 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 mortgage lending value, 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.

No	Industries	Net carrying amount (PLN '000)	Share in the portfolio (%)	Net carrying amount (PLN '000)	Share in the portfolio (%)
		31.12.2014		31.12.2013	
1.	Activity related to the real estate market	2 683 891	50,39	2 580 077	63,78
2.	Building industry	1 300 492	24,42	903 963	22,35
3.	Individuals	818 811	15,37	46 678	1,15
4.	Activity related to culture, entertainment and leisure	215 545	4,05	217 392	5,37
5.	Public administration and defence; Compulsory social security	114 284	2,15	155 919	3,86
6.	Professional, scientific and technical activity	101 799	1,91	20 502	0,51
7.	Health protection and social welfare	62 761	1,18	71 786	1,78
8.	Activity related to accommodation and catering services	19 079	0,36	22 303	0,55
9.	Water supply; Sewage and waste management and activity related to reclamation	8 062	0,15	9 757	0,24
10.	Other	1 017	0,02	16 623	0,41
	Total	**5 325 741**	**100,00**	**4 045 000**	**100,00**

3.3. 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 applies fair value hedge accounting. The interest rate risk is the only type of risk hedged for which hedge accounting is applied. The result on hedged items and hedging instruments is presented in the following tables. The hedge is assessed on an ongoing basis and determined to have been highly effective. The Bank documents its own assessment of the effectiveness of fair value hedging transactions, measured both prospectively and retrospectively from the time of their designation and throughout the period of duration of the hedging relationship between the hedging instrument and the hedged item.

Description of the hedging relation

The Bank hedges against the risk of change in fair value of fixed-interest rate mortgage covered bonds issued by the Bank. The hedged risk results from changes in interest rates.

Hedged items

The hedged items are fixed-interest rate mortgage covered bonds with the nominal value of EUR 93,000 thousand.

Hedging instruments

Interest Rate Swap transactions are the hedging instruments swapping the fixed interest rate for a variable interest rate.

Presentation of the result from hedged and hedging transactions

Fair value adjustment of the hedged liabilities as well as valuation of the hedging instruments is recognised in the income statement as the income from trading operation, except for interest income and expenses related to the interest measurement component of hedging instruments which are presented in the position of interest income/expenses on derivatives concluded under the hedge accounting.

The following table presents hedged items as at 31 December 2014. In the following table, the nominal value was presented in EUR thousands, while the carrying amount and hedge accounting differences concerning the fair value in PLN thousands.

Debt financial instruments by type	Nominal value	Interest rate as at 31.12.2014	Redemption date	Carrying value of liability	Hedge accounting adjustments related to fair value
Covered bonds (EUR)	30 000	2,75%	2020-07-28	127 338	4 275
Covered bonds (EUR)	8 000	3,50%	2029-02-28	34 407	3 976
Covered bonds (EUR)	15 000	3,50%	2029-03-15	64 564	7 477
Covered bonds (EUR)	20 000	3,20%	2029-05-30	85 223	9 709
Covered bonds (EUR)	20 000	1,12%	2018-10-22	85 000	326
Total hedged items				**396 532**	**25 763**

The following table presents hedged items as at 31 December 2014. In the following table, the nominal value was presented in EUR thousands, while the fair value and changes in the fair value due to hedge accounting in PLN thousands.

Derivative instruments	Nominal value	Transaction end date	Fair value of asset	Fair value of liability	Change in the fair value due to hedge accounting
IRS (EUR)	30 000	2020-07-28	8 527	-	4 062
IRS (EUR)	8 000	2029-02-28	5 553	-	4 287
IRS (EUR)	15 000	2029-03-15	10 114	-	8 062
IRS (EUR)	20 000	2029-05-30	9 789	-	10 531
IRS (EUR)	20 000	2018-10-22	-	45	345
Total hedging items			**33 983**	**45**	**27 287**

<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.

<u>Off-balance sheet credit liabilities</u>

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 creditworthiness deteriorating, therefore, the likely amount of the related loss is much lower than the total amount of unused loan liabilities.
The Bank has organisational 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 analysis.

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 inter-bank 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 2014, VaR amounted to PLN 70.5 thousand, with the confidence level amounting to 99%. As at 31 December 2013, VaR amounted to PLN 115 thousand, with the confidence level amounting to 99%.

The value of the Bank's average VaR in the period from 1 January 2014 to 31 December 2014 and in the period from 1 January 2013 to 31 December 2013 is presented in the table below.

PLN '000	12 months until 31.12.2014		12 months until 31.12.2013	
	average	maximum	average	maximum
Interest rate risk	88	195	109	203
Currency risk	35	318	53	1 083
Total VaR	**122**	**342**	**162**	**1 073**

<u>Stress tests and scenario analysis</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 2014, the risk amount resulting from this scenario was PLN 776 thousand, whereas the average risk amount for this scenario in the period from 1 January 2014 to 31 December 2014 was PLN 899 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 test	31.12.2014			31.12.2013		
	Total	Interest rate risk	Currency risk	Total	Interest rate risk	Currency risk
Amount of risk in PLN '000	776	(3 538)	4 314	516	(3 545)	4 061

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 repricing gap. The repricing 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 1,693 thousand as at 31 December 2014, whereas its average in the period from 1 January 2014 to 31 December 2014 was PLN 981 thousand, as at 31 December 2013 it was PLN 214 thousand, and the average in the period from 1 January 2013 to 31 December 2013 was PLN 1,988 thousand.

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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 activity 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.

The table below shows the Bank's exposures exposed to currency risk as at 31 December 2014 and as at 31 December 2013. The table shows the Bank's assets and liabilities at carrying amounts, by currency.

31.12.2014	PLN	EUR	USD	Total
Assets				
Cash and balances with the central bank	7 669	-	-	**7 669**
Amounts due from other banks	17 596	13 067	309	**30 972**
Derivative financial instruments	3 308	33 983	-	**37 291**
Loans and advances to customers	2 657 009	2 587 260	81 472	**5 325 741**
Investment securities available for sale	735 220	-	-	**735 220**
Intangible assets	5 074	-	-	**5 074**
Tangible fixed assets	7 241	-	-	**7 241**
Deferred income tax assets	11 426	-	-	**11 426**
Current income tax assets	1 002	-	-	**1 002**
Other assets	14 576	114	-	**14 690**
Total assets	**3 460 121**	**2 634 424**	**81 781**	**6 176 326**
Liabilities				
Amounts due to other banks	851 679	1 077 316	51 639	**1 980 634**
Derivative financial instruments	33	6 027	3 382	**9 442**
Amounts due to customers	201 423	48 354	235	**250 012**
Debt securities in issue	2 274 478	897 110	-	**3 171 588**
Hedge accounting adjustments related to fair value of hedged tems	-	25 763	-	**25 763**
Subordinated liabilities	100 257	-	-	**100 257**
Other liabilities and provisions	14 089	-	-	**14 089**
Total liabilities	**3 441 959**	**2 054 570**	**55 256**	**5 551 785**
Net balance sheet position	**18 162**	**579 854**	**26 525**	**624 541**
Loan commitments	**811 777**	**265 191**	**-**	**1 076 968**

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	1 832 872	2 114 934	97 194	**4 045 000**
Investment securities available for sale	605 824	-	-	**605 824**
Intangible assets	3 548	-	-	**3 548**
Tangible fixed assets	9 110	-	-	**9 110**
Deferred income 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	**2 569 525**	**2 115 622**	**97 296**	**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	2 289 209	372 198	-	**2 661 407**
Subordinated liabilities	100 268	-	-	**100 268**
Other liabilities and provisions	19 872	-	-	**19 872**
Liabilities exposed to currency risk, in total	**2 703 957**	**1 530 396**	**46 127**	**4 280 480**
Net balance sheet position	**(134 432)**	**585 226**	**51 169**	**501 963**
Loan commitments	**554 211**	**415 587**	**-**	**969 798**

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)	31.12.2014	31.12.2013
for items expressed in PLN	4 585	5 228
for items expressed in USD	3	12
for items expressed in EUR	316	49

While calculating these values, it was assumed that the structure of assets and liabilities recognised in the financial statements as at 31 December 2014 and as at 31 December 2013 would not change within the following year and that the Bank would not take any actions to change the exposure to risk.

In 2014, the level of interest rate risk was maintained at a similar level to 2013 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.

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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.

31.12.2014	Up to 1 month	From 1 to 3 months	From 3 to 12 months	From 1 to 5 years	Over 5 years	Non-interest rate items	Total
Assets							
Cash and balances with the central bank	7 669	-	-	-	-	-	**7 669**
Amounts due from other banks	30 972	-	-	-	-	-	**30 972**
Derivative financial instruments	11 833	15 670	9 788	-	-	-	**37 291**
Loans and advances to customers	2 076 917	1 376 122	1 872 702				**5 325 741**
Investment securities available for sale	479 973	-	204 716	50 531	-	-	**735 220**
Total assets	**2 607 364**	**1 391 792**	**2 087 206**	**50 531**	**-**	**-**	**6 136 893**
Liabilities							
Amounts due to other banks	1 066 319	626 167	288 148	-	-	-	**1 980 634**
Derivative financial instruments	3 806	1 302	4 334	-	-	-	**9 442**
Amounts due to customers	228 358	2 923	16 167	-	-	2 564	**250 012**
Debt securities in issue	1 013 216	536 309	1 225 531	84 999	311 533	-	**3 171 588**
Subordinated liabilities	-	100 257	-	-	-	-	**100 257**
Total liabilities	**2 311 699**	**1 266 958**	**1 534 180**	**84 999**	**311 533**	**2 564**	**5 511 933**
Balance sheet gap	**295 665**	**124 834**	**553 026**	**(34 468)**	**(311 533)**	**(2 564)**	**624 960**

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	Non-interest rate items	Total
Assets							
Cash and balances with the central bank	7 378	-	-	-	-	-	**7 378**
Amounts due from other banks	22 377	-	-	-	-	-	**22 377**
Derivative financial instruments	6 326	980	5 607	-	-	-	**12 913**
Loans and advances to customers	1 274 999	1 265 877	1 503 463	653	-	8	**4 045 000**
Investment securities available for sale	515 428	-	42 005	48 391	-	-	**605 824**
Total assets	**1 826 508**	**1 266 857**	**1 551 075**	**49 044**	**-**	**8**	**4 693 492**
Liabilities							
Amounts due to other banks	428 248	488 039	287 201	-	-	-	**1 203 488**
Derivative financial instruments	-	278	-	-	-	-	**278**
Amounts due to customers	272 956	12 291	5 937	-	-	3 983	**295 167**
Debt securities in issue	845 485	342 389	1 350 000		123 533		**2 661 407**
Subordinated liabilities	-	100 268	-	-	-	-	**100 268**
Total liabilities	**1 546 689**	**943 265**	**1 643 138**	**-**	**123 533**	**3 983**	**4 260 608**
Balance sheet gap	**279 819**	**323 592**	**(92 063)**	**49 044**	**(123 533)**	**(3 975)**	**432 884**

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 sector covered bonds with long maturity dates, and it satisfies its current demand for financing on the inter-bank 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.

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In 2014 and 2013, the Bank monitored 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 2014 and 31 December 2013, as well as the average, minimum and extreme values of liquidity norms:

liquidity norm	value as at 31.12.2014	average	minimum	maximum
M1	PLN 511,619 thousand	PLN 417,672 thousand	PLN 238,194 thousand	PLN 588,803 thousand
M2	2,610	1,884	1,366	3,101
M3	36,521	31,461	29,130	38,992
M4	1,082	1,082	1,041	1,129

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

In 2014 and 2013, 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 maturity dates. The amounts denominated in foreign currencies were converted to PLN using the average NBP exchange rate binding as at the balance sheet date.

Liabilities (by contractual dates of maturity) as at 31 December 2014

	Up to 1 month	From 1 to 3 months	From 3 months to 1 year	From 1 to 5 years	Over 5 years	Total
Assets (by expected dates of maturity)						
Cash and balances with the central bank	7 809	-	-	-	-	7 809
Amounts due from other banks	30 895	-	-	-	-	30 895
Loans and advances to customers	53 225	84 591	424 144	2 141 354	4 289 126	6 992 440
Available-for-sale investment securities	480 000	-	208 331	49 345	-	737 676
Total assets	**571 929**	**84 591**	**632 475**	**2 190 699**	**4 289 126**	**7 768 820**
Liabilities (by contractual dates of maturity)						
Amounts due to other banks	131 262	207 200	613 490	1 104 171	-	2 056 123
Amounts due to customers	229 023	2 287	16 307	-	-	247 617
Liabilities in respect of debt securities in issue	11 154	62 873	568 670	1 997 934	934 252	3 574 883
Subordinated liabilities	-	1 386	4 174	22 270	116 741	144 571
Total liabilities	**371 439**	**273 746**	**1 202 641**	**3 124 375**	**1 050 993**	**6 023 194**
Net liquidity gap	**200 490**	**(189 155)**	**(570 166)**	**(933 676)**	**3 238 133**	**1 745 626**

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

	Up to 1 month	From 1 to 3 months	From 3 months to 1 year	From 1 to 5 years	Over 5 years	Total
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
Available-for-sale investment securities	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**
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**
Net liquidity gap	**70 163**	**(315 221)**	**(432 285)**	**(652 299)**	**2 615 120**	**1 285 478**

The amounts disclosed in the analysis of maturity dates 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 exchange rate binding as at the balance sheet date. The amounts disclosed in the table are non-discounted contractual cash outflows.

31.12.2014

Derivative financial instruments to be settled on a net basis	within 1 month	from 1 to 3 months	from 3 months to 1 year	from 1 to 5 years	over 5 years	Total
Interest rates swaps (IRS)	-	770	(857)	132	-	**45**
Total net valuation	**-**	**770**	**(857)**	**132**	**-**	**45**

31.12.2013

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

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. The amounts denominated in foreign currencies were converted to PLN using the average NBP exchange rate binding as at the balance sheet date.

31.12.2014

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	111 434	115 082	396 394	**622 910**
- inflows	107 398	113 122	391 270	**611 790**

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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**

4. Fair value of financial assets and liabilities

Fair value is the price that would be received for the sale of an asset or paid for the transfer of a liability in an orderly transaction between market participants at the measurement date. A fair value measurement assumes that the transaction of selling the asset or transferring a liability occurs either:

- on the main market for the asset or liability,
- in the absence of a main market, for the most advantageous market for the asset or liability.

The main and the most advantageous markets must be both available to the Bank.

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 significant 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:

<u>Amounts due from other banks</u>

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.

<u>Loans and advances to customers</u>

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.

Receivables from loans and advances to customers are presented at level 3 in the fair value hierarchy.

<u>Investment securities available for sale</u>

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.

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.

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Financial instruments on the liabilities side are:

- bank accounts balances,
- loans and advances received,
- other financial liabilities with deferred payment term,
- 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 Bank has assumed that the fair value of liabilities in current accounts, loans received, other financial liabilities with deferred maturity, 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.

<u>Debt securities in issue (covered bonds and bonds)</u>

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	31.12.2014		31.12.2013	
	Carrying value	Fair value	Carrying value	Fair value
Financial assets				
Cash and balances with the central bank	**7 669**	**7 669**	**7 378**	**7 378**
Amounts due from other banks	**30 972**	**30 972**	**22 377**	**22 377**
Loans and advances to customers, including:	**5 325 741**	**5 384 068**	**4 045 000**	**4 057 222**
Corporate customers	4 290 209	4 339 196	3 725 996	3 746 120
Individual customers	860 660	868 451	93 761	84 473
Public sector customers	174 872	176 421	225 235	226 621
Other receivables	-	-	8	8
Total financial assets	**5 364 382**	**5 422 709**	**4 074 755**	**4 086 977**
Financial liabilities				
Amounts due to other banks	**1 980 634**	**1 980 634**	**1 203 488**	**1 203 488**
Amounts due to customers, including:	**250 012**	**250 012**	**295 167**	**295 167**
Corporate customers	249 831	249 831	294 978	294 978
Individual customers	161	161	174	174
Public sector customers	20	20	15	15
Debt securities in issue	**3 171 588**	**3 108 731**	**2 661 407**	**2 649 432**
Subordinated liabilities	**100 257**	**100 257**	**100 268**	**100 268**
Total financial liabilities	**5 502 491**	**5 439 634**	**4 260 330**	**4 248 355**

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The table below presents the fair value hierarchy of financial assets and liabilities measured at fair value in accordance with the assumptions described above, exclusively for disclosure as at 31 December 2014 and 31 December 2013.

31.12.2014	including:	Level 1 Prices quoted in active markets	Level 2 Valuation techniques based on observable market data	Level 3 Other valuation techniques
VALUATION ONLY FOR PURPOSES OF DISCLOSURE				
Financial assets				
Cash and balances with the central bank	7 669	-	-	7 669
Amounts due from other banks	30 972	-	-	30 972
Loans and advances to customers	5 384 068	-	-	5 384 068
Financial liabilities				
Amounts due to other banks	1 980 634	-	-	1 980 634
Amounts due to customers	250 012	-	-	250 012
Debt securities in issue	3 108 731	-	-	3 108 731
Subordinated liabilities	100 257	-	-	100 257
Total financial assets	**5 422 709**	**-**	**-**	**5 422 709**
Total financial liabilities	**5 439 634**	**-**	**-**	**5 439 634**

31.12.2013	including:	Level 1 Prices quoted in active markets	Level 2 Valuation techniques based on observable market data	Level 3 Other valuation techniques
VALUATION ONLY FOR PURPOSES OF DISCLOSURE				
Financial assets				
Cash and balances with the central bank	7 378	-	-	7 378
Amounts due from other banks	22 377	-	-	22 377
Loans and advances to customers	4 057 222	-	-	4 057 222
Financial liabilities				
Amounts due to other banks	1 203 488	-	-	1 203 488
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 assets	**4 086 977**	**-**	**-**	**4 086 977**
Total financial liabilities	**4 248 355**	**-**	**-**	**4 248 355**

The following tables present fair value hierarchy of financial assets and liabilities recognised in the statement of financial position of the Bank at their fair values.

31.12.2014	including:	Level 1 Prices quoted in active markets	Level 2 Valuation techniques based on observable market data	Level 3 Other valuation techniques
RECURRING FAIR VALUE MEASUREMENTS				
FINANCIAL ASSETS				
Available-for-sale investment securities, including:	**735 220**	**255 246**	**479 974**	**-**
- treasury bonds	255 246	255 246	-	-
- money bills	479 974	-	479 974	-
Derivative financial instruments, including:	**37 291**	**-**	**37 291**	**-**
- Interest-bearing instruments	37 125	-	37 125	-
- Foreign exchange instruments	166	-	166	-
TOTAL FINANCIAL ASSETS	**772 511**	**255 246**	**517 265**	**-**

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31.12.2014	including:	Level 1 Prices quoted in active markets	Level 2 Valuation techniques based on observable market data	Level 3 Other valuation techniques
FINANCIAL LIABILITIES				
Derivative financial instruments	**9 442**	**-**	**9 442**	**-**
Interest-bearing instruments	77	-	77	-
Foreign exchange instruments	9 365	-	9 365	-
TOTAL FINANCIAL LIABILITIES	**9 442**	**-**	**9 442**	**-**
RECURRING FAIR VALUE MEASUREMENTS				
TOTAL FINANCIAL ASSETS	**772 511**	**255 246**	**517 265**	-
TOTAL FINANCIAL LIABILITIES	**9 442**	**-**	**9 442**	-

31.12.2013	including:	Level 1 Prices quoted in active markets	Level 2 Valuation techniques based on observable market data	Level 3 Other valuation techniques
RECURRING FAIR VALUE MEASUREMENTS				
FINANCIAL ASSETS				
Available-for-sale investment securities, including:	**605 824**	**90 396**	**515 428**	**-**
- treasury bonds	90 396	90 396	-	-
- money bills	515 428	-	515 428	-
Derivative financial instruments	**12 913**	**-**	**12 913**	**-**
Interest-bearing instruments	339	-	339	-
Foreign exchange instruments	12 574	-	12 574	-
TOTAL FINANCIAL ASSETS	**618 737**	**90 396**	**528 341**	**-**

31.12.2013	including:	Level 1 Prices quoted in active markets	Level 2 Valuation techniques based on observable market data	Level 3 Other valuation techniques
FINANCIAL LIABILITIES				
Derivative financial instruments	**278**	**-**	**278**	**-**
Interest-bearing instruments	277	-	277	-
Foreign exchange instruments	1	-	1	-
Total financial liabilities	**278**	**-**	**278**	**-**
RECURRING FAIR VALUE MEASUREMENTS				
TOTAL FINANCIAL ASSETS	**618 737**	**90 396**	**528 341**	-
TOTAL FINANCIAL LIABILITIES	**278**	**-**	**278**	-

In case of financial instruments valuated in repetitive way to the fair value classified as level 1 and 2 in hierarchy of fair value, any cases in which transfer between these levels may occur, are monitored by relevant departments of the Bank on the basis of internal guidelines.

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 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 financial asset.

Impairment of non-financial assets — inventories

Impairment write-downs on repossessed real properties are calculated on a semi-annual and annual basis. The calculation of impairment involves comparing the selling prices of real properties (apartments) on a comparable market 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 real property values for the entire population.

Deferred income tax assets

The Bank capitalises in the deferred tax the value of impairment write-downs on loans in case of the occurrence of events allowing to consider the uncollectibility of loans as probable, in accordance with applicable tax regulations, including as a result of conducted 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 Program 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, Fourth and Fifth Assessment Period corresponding to 2012, 2012-2013, 2012-2014, 2013-2015 and 2014-2016, 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 annual 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 2014 amounted to PLN 899.7 thousand, whereas as at 31 December 2013 it amounted to PLN 250 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). In 2014, the sale of retail loans was supplemented with a "pooling" model, under which the Bank acquires mortgage loans granted by mBank S.A. which may constitute a basis for the issue covered bonds. 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 developers,
- loans to commercial real estate developers,
- loans for land purchase,
- Loans to individual customers,
- Loans to individual customers — agency model, pooling.

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 and malls, 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 secured by local government units (commercial companies established by local governments, public health care institutions).

Loans to housing 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, pooling — 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. This segment also includes pooling loans — housing receivables acquired from the parent entity — loans in PLN granted to individuals for housing purposes, secured by a mortgage.

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 sector 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 sector 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 loans for local government units 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 loans for local government units).

Remaining income statement items are divided either by the share of average credit exposure in the year, or share of risk-weighted assets in the case of depreciation and administrative expenses. 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.

In 2014, the Bank changed the key for dividing individual items of the income statement to individual segments. The main change included the application of average balance sheet values from the last 12 months instead of values as at the end of the period. In connection with this change, the comparative data were restated accordingly.

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 operating 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 Bank's Management Board on a regular basis.

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Period from 01.01.2014 to 31.12.2014	Loans for refinancing commercial real estates	Loans to local government units	Loans to housing developers	Loans to commercial real estate developers	Loans for land purchase	Loans to individuals	Loans to individuals — agency model, pooling	Total	Income statement
Interest income	130 689	20 865	35 433	16 514	2 936	1 423	11 136	218 996	218 996
Interest expense	(66 305)	(22 441)	(20 649)	(9 994)	(1 594)	(1 739)	(10 091)	(132 813)	(132 813)
Net interest income	**64 384**	**(1 576)**	**14 784**	**6 520**	**1 342**	**(316)**	**1 045**	**86 183**	**86 183**
Fee and commission income	4 311	513	817	1 951	42	47	1 951	9 632	9 632
Fee and commission expenses	(816)	(125)	(132)	(102)	(10)	(11)	(4 390)	(5 586)	(5 586)
Net impairment write-downs on loans and advances	(15 756)	18	(6 521)	(588)	2 189	(38)	(249)	(20 945)	(20 945)
Amortisation/depreciation and overhead costs	(35 297)	(1 046)	(4 020)	(5 212)	(303)	(387)	(4 884)	(51 149)	(51 149)
Other income statement items	7 826	232	891	1 156	66	86	1 083	11 340	11 340
Segment result (before tax)	**24 652**	**(1 984)**	**5 819**	**3 725**	**3 326**	**(619)**	**(5 444)**	**29 475**	**29 475**

31.12.2014	Loans for refinancing commercial real estates	Loans to local government units	Loans to housing developers	Loans to commercial real estate developers	Loans for land purchase	Loans to individuals	Loans to individuals — agency model, pooling	Non-allocated assets items	Total	Statement of financial position
Loans and advances to customers	**3 187 138**	**420 561**	**446 454**	**430 921**	**21 856**	**36 459**	**782 352**	**-**	**5 325 741**	**5 325 741**
Other assets	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**850 585**	**850 585**	**850 585**
Segment assets	**3 187 138**	**420 561**	**446 454**	**430 921**	**21 856**	**36 459**	**782 352**	**850 585**	**6 176 326**	**6 176 326**

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.

Financial statements in accordance with the International Financial Reporting Standards (IFRS) for the year 2014 (PLN '000)

Period from 01.01.2013 to 31.12.2013	Loans for refinancing commercial real estates	Loans to local government units	Loans to housing developers	Loans to commercial real estate developers	Loans for land purchase	Loans to individuals	Loans to individuals — agency model, pooling	Total	Income statement
Interest income	136 891	29 704	39 241	12 279	6 848	2 032	70	227 065	227 065
Interest expense	(79 368)	(30 980)	(25 935)	(8 899)	(4 404)	(2 475)	(225)	(152 286)	(152 286)
Net interest income	**57 523**	**(1 276)**	**13 306**	**3 380**	**2 444**	**(443)**	**(155)**	**74 779**	**74 779**
Fee and commission income	3 262	497	829	559	76	50	4	5 277	5 277
Fee and commission expenses	(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)
Amortisation/depreciation and overhead costs	(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)	**2 866**	**(1 970)**	**4 478**	**(51)**	**1 324**	**(1 546)**	**(204)**	**4 897**	**4 897**

31.12.2013	Loans for refinancing commercial real estates	Loans to local government units	Loans to housing developers	Loans to commercial real estate developers	Loans for land purchase	Loans to individuals	Loans to individuals — agency model, pooling	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.

Financial statements in accordance with the International Financial Reporting Standards (IFRS) for the year 2014 (PLN '000)

7. Net interest income

	Year ended 31 December	
	2014	2013
Interest income		
Loans and advances, including the unwind of discount relating to impairment write-down, of which:	183 158	182 677
- interest income on impaired loans and advances	7 645	10 426
Cash and short-term deposits	519	518
Investment securities	17 333	17 687
Interest income on derivatives classified into banking book	15 180	26 183
Interest income on derivatives concluded under hedge accounting	2 806	-
Total interest income	**218 996**	**227 065**

	Year ended 31 December	
	2014	2013
Interest expense		
Due to settlements with banks	(20 269)	(14 740)
Due to settlements with customers	(1 734)	(2 049)
Due to the issue of debt securities	(104 705)	(128 776)
Due to subordinated loan	(6 105)	(6 721)
Total interest expense	**(132 813)**	**(152 286)**
Total net interest income	**86 183**	**74 779**

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

	Year ended 31 December	
	2014	2013
Interest income		
From banking sector	30 401	40 402
From other entities, including:	188 595	186 663
- from corporate customers	163 881	166 823
- from individual customers	12 371	3 902
- from public sector	12 343	15 938
Total interest income	**218 996**	**227 065**

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

	Year ended 31 December	
	2014	2013
Interest expense		
From banking sector	(26 374)	(21 461)
From other entities, including:	(1 734)	(2 049)
- from corporate customers	(1 734)	(2 049)
From own issuances	(104 705)	(128 776)
Total interest expense	**(132 813)**	**(152 286)**

Financial statements in accordance with the International Financial Reporting Standards (IFRS) for the year 2014 (PLN '000)

8. Net fee and commission income and expense

	Year ended 31 December	
	2014	2013
Fee and commission income		
Credit-related fees and commissions	9 202	4 909
Commissions from bank accounts	381	330
Commissions from money transfers	49	38
Total fee and commission income	**9 632**	**5 277**
Fee and commission expenses		
Costs of real estate analyses and valuations related to the lending activity	(3 915)	-
Costs related to the debt instrument's issue program (covered bonds and bonds)	(660)	(982)
Commission expense from the stand-by credit line	(519)	(482)
Cost of servicing loan products	(348)	(51)
Other	(144)	(69)
Total fee and commission expense	**(5 586)**	**(1 584)**
Total net fee and commission income	**4 046**	**3 693**

9. Net trading income

	Year ended 31 December	
	2014	2013
Foreign exchange result	**3 862**	**4 186**
Net exchange differences on translation	25 194	(2 471)
Valuation of foreign currency derivatives	(21 332)	6 657
Other net trading income and result on hedge accounting	**8 430**	**(1 001)**
Interest rate risk instruments	6 906	(1 001)
Hedge accounting, including:	1 524	-
- net profit on hedged items	(25 763)	-
- net profit on hedging instruments	27 287	-
Total net trading income	**12 292**	**3 185**

Foreign exchange result covers realised and unrealised, positive and negative exchange rate differences, as well as profits and losses on spot transactions and futures contracts. The result on operations on interest-bearing instruments covers the result on interest rate swap contracts which have not been designated as hedging instruments.

In the first half of 2014, the Bank implemented fair value hedge accounting in relation to issued fixed-interest rate mortgage covered bonds issued. Interest Rate Swap is the hedging instrument swapping the fixed interest rate for a variable interest rate. As at 31 December 2014, there were five hedging relations concluded, presented in Note 3.3.

Financial statements in accordance with the International Financial Reporting Standards (IFRS) for the year 2014 (PLN '000)

10. Other operating income

	Year ended 31 December	
	2014	**2013**
Income from sales of services	493	470
Income from recovering receivables designated previously as prescribed, remitted or uncollectible	37	51
Income from the inventories sale transaction	-	5 658
Revenue from sales of receivables	-	841
Income from the release of the provisions for future liabilities, bonuses and legal proceedings	187	170
Refund of reliefs on new technologies	98	-
Disclosure of intangible assets	62	-
Other	266	107
Total other operating income	**1 143**	**7 297**

11. Net impairment write-downs on loans and advances

	Year ended 31 December	
	2014	**2013**
Net write-downs on loans and advances to customers (Note 21)	(20 944)	(34 866)
Net write-downs for contingent liability towards customers	(1)	-
Net impairment write-downs on loans and advances	**(20 945)**	**(34 866)**

12. Overhead costs

	Year ended 31 December	
	2014	**2013**
Staff-related expenses	(28 410)	(22 832)
Material costs	(15 581)	(14 211)
Contribution and payments to the Bank Guarantee Fund	(1 822)	(1 726)
Taxes and fees	(830)	(267)
Contributions to the Social Benefits Fund	(196)	(153)
Total overhead costs	**(46 839)**	**(39 189)**

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	
	2014	**2013**
Wages and salaries	(23 469)	(18 870)
Social security expenses	(2 856)	(2 317)
Costs of retirement benefits	(10)	(15)
Provision for unused employee leaves	(206)	(303)
Costs of long-term employee benefits	(650)	(127)
Other employee benefits	(1 219)	(1 200)
Total staff-related expenses	**(28 410)**	**(22 832)**

In 2014, the average number of employees at the Bank was 187 (in 2013: 144).

Financial statements in accordance with the International Financial Reporting Standards (IFRS) for the year 2014 (PLN '000)

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	
	2014	**2013**
Loss on the sales of assets repossessed for debts (inventories) and costs of their maintenance	(685)	(5 327)
Costs of execution proceedings	(552)	(392)
Compensation, penalties and fines paid	(282)	(1)
Costs arising from impairment write-downs created for other receivables (excluding loans)	(209)	-
Costs of creation of impairment write-offs on tangible fixed assets	(25)	-
Loss on sales or liquidation of fixed assets and intangible assets	(8)	(19)
Inventories revaluation write-downs	-	(129)
Donations made	-	(5)
Other	(334)	(30)
Total other operating expenses	**(2 095)**	**(5 903)**

14. Income tax expense

	Year ended 31 December	
	2014	**2013**
Current income tax	(5 535)	(5 631)
Deferred income tax (Note 32)	(1 569)	2 888
Total income tax	**(7 104)**	**(2 743)**
Profit before tax	**29 475**	**4 897**
Income tax calculated at the rate applicable in a given fiscal year (19%)	(5 600)	(930)
Non-taxable income	188	607
Non-deductible tax costs, including	(1 708)	(2 443)
- value of write-downs on receivables	(1 296)	(1 926)
- costs of the prudent fee to the Bank Guarantee Fund	(116)	-
- increase in the value of a repossessed property to fair value	-	(427)
- other	(296)	(90)
Adjustments in respect of current tax from prior years	16	23
Total income tax expense	**(7 104)**	**(2 743)**
Effective tax rate calculation		
Profit before income tax	29 475	4 897
Income tax	(7 104)	(2 743)
Effective tax rate	**24,10%**	**56,01%**
Nominal tax rate	**19,00%**	**19,00%**

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.

Financial statements in accordance with the International Financial Reporting Standards (IFRS) for the year 2014 (PLN '000)

15. Profit per share

	Year ended 31 December	
	2014	2013
Basic:		
Net profit from activities attributable to shareholders of mBank Hipoteczny S.A.	22 371	2 154
Weighted average number of ordinary shares	2 759 589	2 750 000
Basic net profit per share (in PLN per share)	**8,11**	**0,78**
Diluted:		
Net profit attributable to shareholders of mBank Hipoteczny S.A., applied during the estimation of diluted profit per share	22 371	2 154
Weighted average number of ordinary shares for diluted profit per share	2 759 589	2 750 000
Diluted net profit per share (in PLN per share)	**8,11**	**0,78**

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.

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	
	2014	2013
Items that may be reclassified to the income statement	**283**	**(931)**
Available-for-sale financial assets:	283	(931)
- gross amount	349	(1 149)
- deferred tax	(66)	218
Items that will not be reclassified to the income statement	**(14)**	**35**
Actuarial gains and losses on post-employment benefits	(14)	35
- gross amount	(17)	43
- deferred tax	3	(8)
Other comprehensive income, net	**269**	**(896)**

Financial statements in accordance with the International Financial Reporting Standards (IFRS) for the year 2014 (PLN '000)

17. Disclosures concerning the components of other comprehensive income

	Year ended 31 December	
	2014	**2013**
Items that may be reclassified to the income statement, including:	**283**	**(931)**
Available-for-sale financial assets	**283**	**(931)**
Unrealised gains on debt instruments recognised in the financial year (net)	283	-
Unrealised losses on debt instruments recognised in the financial year (net)	-	(931)
Items that will not be reclassified to the income statement, including:	**(14)**	**35**
Actuarial gains and losses on post-employment benefits	**(14)**	**35**
Actuarial gains	-	35
Actuarial losses	(14)	-
Other comprehensive income, net	**269**	**(896)**

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 7,669 thousand as at 31 December 2014. As at 31 December 2013, the Bank maintained PLN 7,378 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 7,451 thousand for the period from 31 December 2014 to 1 February 2015,
- PLN 5,883 thousand for the period from 31 December 2013 to 30 January 2014,

As at 31 December 2014, the interest rate on the cash maintained as a mandatory reserve was 1.80%, as compared to 2.475% as at 31 December 2013.

19. Amounts due from other banks

	31.12.2014	**31.12.2013**
Deposits with other banks (overnight deposits)	15 001	22 001
Current accounts	15 971	376
Included in cash equivalents	**30 972**	**22 377**
Total (gross) amounts due from other banks	**30 972**	**22 377**
Total (net) amounts due from other banks	**30 972**	**22 377**
Short-term amounts due from other banks (up to 1 year)	30 972	22 377

All amounts due were due from Polish banks and were not impaired.

In 2014, the average amount-weighted interest rates on deposits with other banks were as follows: EUR – 0.2%, PLN – 2.28%, USD – 0.1%. In 2013: EUR – 0.05%, PLN – 2.57%.

Financial statements in accordance with the International Financial Reporting Standards (IFRS) for the year 2014 (PLN '000)

20. Derivative financial instruments

	Nominal amount		Fair value	
	purchase	disposal	assets	liabilities
As at 31 December 2014				
Derivative financial instruments held for trading				
Foreign exchange derivatives				
- FX swap contracts	650 937	657 085	166	9 365
Total OTC derivatives	**650 937**	**657 085**	**166**	**9 365**
Total foreign exchange derivatives	**650 937**	**657 085**	**166**	**9 365**
Interest rate derivatives				
- IRS contracts	850 000	850 000	3 142	32
Total OTC interest rate derivatives	**850 000**	**850 000**	**3 142**	**32**
Total interest rate derivatives	**850 000**	**850 000**	**3 142**	**32**
Total assets / liabilities held for trading	**1 500 937**	**1 507 085**	**3 308**	**9 397**
Derivatives held for hedging				
Derivatives designated as fair value hedges	396 394	396 394	33 983	45
- IRS contracts	396 394	396 394	33 983	45
Total derivatives held for hedging	**396 394**	**396 394**	**33 983**	**45**
Total recognised derivative assets /liabilities	**1 897 331**	**1 903 479**	**37 291**	**9 442**
Total recognised derivative assets /liabilities held for trading	**1 897 331**	**1 903 479**	**37 291**	**9 442**
Short-term (up to 1 year)	1 500 937	1 507 085	3 308	9 397
Long-term (over 1 year)	396 394	396 394	33 983	45

	Nominal amount		Fair value	
	purchase	disposal	assets	liabilities
As at 31 December 2013				
Derivative financial instruments held for trading				
Foreign exchange derivatives				
- FX swap contracts	671 834	656 073	12 573	-
Total OTC derivatives	**671 834**	**656 073**	**12 573**	**-**
Total foreign exchange derivatives	**671 834**	**656 073**	**12 573**	**-**
Interest rate derivatives				
- IRS contracts	331 776	331 776	340	278
Total OTC interest rate derivatives	**331 776**	**331 776**	**340**	**278**
Total interest rate derivatives	**331 776**	**331 776**	**340**	**278**
Total assets / liabilities held for trading	**1 003 610**	**987 849**	**12 913**	**278**
Total recognised derivative assets /liabilities	**1 003 610**	**987 849**	**12 913**	**278**
Total recognised derivative assets /liabilities held for trading	**1 003 610**	**987 849**	**12 913**	**278**
Short-term (up to 1 year)	1 003 610	987 849	12 913	9
Long-term (over 1 year)	-	-	-	269

Financial statements in accordance with the International Financial Reporting Standards (IFRS) for the year 2014 (PLN '000)

21. Loans and advances to customers

	31.12.2014	31.12.2013
Loans and advances to corporate customers	**4 375 564**	**3 799 524**
Loans and advances to individual customers	**862 951**	**95 754**
Loans and advances to the public sector	**174 925**	**225 302**
Other receivables	**-**	**8**
Loans and advances from customers (gross)	**5 413 440**	**4 120 588**
Impairment write-downs on loan and advances to customers (negative amount)	(87 699)	(75 588)
Loans and advances from customers (net)	**5 325 741**	**4 045 000**
Short-term (up to 1 year)	427 185	406 311
Long-term (over 1 year)	4 898 556	3 638 689

As at 31 December 2014, the gross value of loans to corporate customers, individual customers and the public sector in the Bank's loan portfolio, carrying floating interest rates, amounted to PLN 5,412,748 thousand, and the gross value of loans carrying fixed interest rates amounted to PLN 692 thousand. As at 31 December 2013, the value of loans carrying floating interest rates amounted to PLN 4,119,463 thousand, and the value of loans carrying fixed interest rates amounted to PLN 1,117 thousand.

Impairment write-downs on loans and advances

	31.12.2014	31.12.2013
Incurred but not identified losses		
Gross balance sheet exposure	5 228 576	3 901 923
Impairment write-downs on exposures analysed on a portfolio basis	(8 701)	(7 205)
Net balance sheet exposure	**5 219 875**	**3 894 718**
Impaired receivables		
Loans to corporate customers	178 699	212 864
Loans to individual customers	6 165	5 801
Total gross balance sheet exposure	**184 864**	**218 665**
Impairment write-down on impaired exposures	(78 998)	(68 383)
Net balance sheet exposure	**105 866**	**150 282**

Movements in impairment write-downs on loans and advances

	Impairment write-downs as at 01.01.2014	Write-downs created	Reversal of write-downs	Receivables written-off	Impairment write-downs as at 31.12.2014
Corporate customers	(73 528)	(36 112)	15 451	8 833	(85 356)
Individual customers	(1 993)	(760)	462	-	(2 291)
Public sector customers	(67)	-	15	-	(52)
Total movements in impairment write-downs on loans and advances	(75 588)	(36 872)	15 928	8 833	(87 699)

	Impairment write-downs as at 01.01.2013	Write-downs created	Reversal of write-downs	Receivables written-off	Impairment write-downs as at 31.12.2013
Corporate customers	(44 936)	(44 341)	10 225	5 524	(73 528)
Individual customers	(1 213)	(1 620)	840	-	(1 993)
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)

Financial statements in accordance with the International Financial Reporting Standards (IFRS) for the year 2014 (PLN '000)

22. Investment securities

	31.12.2014			31.12.2013		
	Investment securities without pledge	Pledged investment securities	Total investment securities	Investment securities without pledge	Pledged investment securities	Total investment securities
Debt securities:	**532 483**	**202 737**	**735 220**	**604 324**	**1 500**	**605 824**
Issued by government	52 510	202 737	255 247	90 396	-	90 396
- government bonds	52 510	202 737	255 247	90 396	-	90 396
Issued by central bank	479 973	-	479 973	513 928	1 500	515 428
- central bank's bills	479 973	-	479 973	513 928	1 500	515 428
Total debt securities	**532 483**	**202 737**	**735 220**	**604 324**	**1 500**	**605 824**
Short-term (up to 1 year)	532 483	152 207	684 690	555 933	1 500	557 433
Long-term (over 1 year)	-	50 530	50 530	48 391	-	48 391

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

	31.12.2014	31.12.2013
Investment securities		
As at the beginning of the period	**605 824**	**566 258**
Additions	26 485 896	23 617 741
Disposals (sale, redemption and forfeiture)	(26 356 849)	(23 577 026)
Gains / losses from changes in fair value	349	(1 149)
As at the end of the period	**735 220**	**605 824**

23. Investments in subsidiaries

As at 31 December 2014, 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.

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 BDH shares in the Bank's books was PLN 715 thousand.

On 26 November 2013, the District Court for the Capital City of Warsaw, 12th 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".

Financial statements in accordance with the International Financial Reporting Standards (IFRS) for the year 2014 (PLN '000)

24. Intangible assets

	31.12.2014	31.12.2013
Concessions, patents, licences and similar assets, including:	3 725	1 970
- computer software	3 725	1 970
Intangible assets under development	1 349	1 578
Total intangible assets	**5 074**	**3 548**

Movements in intangible assets

Movements in the period from 01.01.2014 to 31.12.2014	Acquired computer software	Intangible assets under development	Total
Gross value of intangible assets as at the beginning of the period: 01.01.2014	**10 797**	**1 578**	**12 375**
Increase (due to)	**2 835**	**2 280**	**5 115**
- purchase	733	2 280	3 013
- transfer from intangible assets under development	2 040	-	2 040
- other increases	62	-	62
Decrease (due to)	**-**	**(2 509)**	**(2 509)**
- transfer from intangible assets under development	-	(2 040)	(2 040)
- other decreases	-	(469)	(469)
Gross value of intangible assets as at the end of the period 31.12.2014	**13 632**	**1 349**	**14 981**
Accumulated amortisation as at the beginning of the period: 01.01.2014	**(8 827)**	**-**	**(8 827)**
Amortisation for the period (due to):	**(1 080)**	**-**	**(1 080)**
- amortisation charges	(1 080)	-	(1 080)
Accumulated amortisation as at the end of the period 31.12.2014	**(9 907)**	**-**	**(9 907)**
Net value of intangible assets as at the end of the period 31.12.2014	**3 725**	**1 349**	**5 074**

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 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 as at the end of the period 31.12.2013	**(8 827)**	**(185)**	**-**	**(9 012)**
Net value of intangible assets as at the end of the period 31.12.2013	**1 970**	**-**	**1 578**	**3 548**

25. Tangible fixed assets

	31.12.2014	31.12.2013
Technical equipment and machinery	5 718	6 599
Vehicles	620	978
Fixed assets under construction	-	390
Other fixed assets	903	1 143
Total tangible fixed assets	**7 241**	**9 110**

Financial statements in accordance with the International Financial Reporting Standards (IFRS) for the year 2014 (PLN '000)

Movements in tangible fixed assets

Movements in the period from 01.01.2014 to 31.12.2014	Equipment	Vehicles	Other fixed assets	Fixed assets under construction	Total
Gross value of tangible fixed assets as at the beginning of the period: 01.01.2014	**18 118**	**2 457**	**5 167**	**390**	**26 132**
Increase (due to)	**1 552**	**-**	**257**	**18**	**1 827**
- purchase	675	-	257	18	950
- transfer from fixed assets under construction	408	-	-	-	408
- other increases	469	-	-	-	469
Decrease (due to)	**(627)**	**(246)**	**(442)**	**(408)**	**(1 723)**
- sale	-	(246)	-	-	(246)
- scrapping	(627)	-	(442)	-	(1 069)
- transfer from fixed assets under construction	-	-	-	(408)	(408)
Gross value of tangible fixed assets as at the end of the period 31.12.2014	**19 043**	**2 211**	**4 982**	**-**	**26 236**
Accumulated amortisation as at the beginning of the period: 01.01.2014	**(11 519)**	**(1 479)**	**(4 024)**	**-**	**(17 022)**
Amortisation for the period (due to):	**(1 806)**	**(87)**	**(55)**	**-**	**(1 948)**
- amortisation charges	(2 430)	(308)	(492)	-	(3 230)
- sale	-	221	-	-	221
- scrapping	624	-	437	-	1 061
Accumulated amortisation as at the end of the period 31.12.2014	**(13 325)**	**(1 566)**	**(4 079)**	**-**	**(18 970)**
Impairment charge as at the beginning of the period: 01.01.2014	**-**	**-**	**-**	**-**	**-**
- increase	-	(25)	-	-	(25)
Impairment charge as at the end of the period 31.12.2014	**-**	**(25)**	**-**	**-**	**(25)**
Net value of tangible fixed assets as at the end of the period 31.12.2014	**5 718**	**620**	**903**	**-**	**7 241**

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 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 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**

Financial statements in accordance with the International Financial Reporting Standards (IFRS) for the year 2014 (PLN '000)

26. Other assets

	31.12.2014	31.12.2013
Other, including:	**14 690**	**62 615**
- inventories	8 192	8 192
- income receivable	2 966	313
- other prepayments	1 253	725
- debtors	1 895	-
- receivables from the sale of inventories	-	52 761
- other	384	624
Total other assets	**14 690**	**62 615**
Short-term (up to 1 year)	14 690	62 615
Long-term (over 1 year)	-	-

Inventories consist of repossessed assets, as described in the note 3.1.6.

27. Amounts due to other banks

	31.12.2014	31.12.2013
Term deposits (including overnight deposits)	396 627	787 862
Loans received	1 228 221	415 626
Other financial liabilities with deferred payment term	346 533	-
Liabilities in respect of cash collateral	9 253	-
Total amounts due to other banks	**1 980 634**	**1 203 488**
Short-term (up to 1 year)	925 224	788 768
Long-term (over 1 year)	1 055 410	414 720
Fixed rate deposits	396 627	787 862

Other financial liabilities with deferred payment term relate to a liability resulting from agreements concluded with mBank S.A. on the transfer of a portfolio of retail loans secured with a mortgage on real estate and an agreement on the transfer of a commercial loan secured with a mortgage. The transactions were described in Note 43.

All loans received are based on floating interest rates.

In 2014, the average amount-weighted interest rates on term deposits were as follows: EUR – 0.3%, PLN – 2.37%, USD – 0.26%, In 2013: EUR – 0.37%, PLN – 2.73%, USD – 0.49%.

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 raised.

Financial statements in accordance with the International Financial Reporting Standards (IFRS) for the year 2014 (PLN '000)

28. Amounts due to customers

	31.12.2014	31.12.2013
Corporate customers:	**249 834**	**294 978**
Cash in current accounts	191 638	226 551
Term deposits (including overnight deposits)	55 810	64 633
Other liabilities (in respect of):	2 386	3 794
- cash collateral	915	2 169
- other	1 471	1 625
Individual customers:	**160**	**174**
Other liabilities (in respect of):	160	174
- cash collateral	65	65
- other	95	109
Public sector customers:	**18**	**15**
Other liabilities (in respect of):	18	15
- other	18	15
Total amounts due to customers	**250 012**	**295 167**
Short-term (up to 1 year)	249 108	292 933
Long-term (over 1 year)	904	2 234

29. Debt securities issued

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 sector 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 Organisation 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 2014 amounted to PLN 2,667,214 thousand,
- 31 December 2013 amounted to PLN 1,978,248 thousand,

Total nominal value of public sector covered bonds issued as at:

- 31 December 2014 amounted to PLN 350,000 thousand,
- 31 December 2013 amounted to PLN 350,000 thousand,

The carrying amount of covered bonds issued as at 31 December 2014 and 31 December 2013 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 2014 amounted to PLN 3,263,858 thousand,
- 31 December 2013 amounted to PLN 2,404,717 thousand,

In addition, the basis for the issue of mortgage covered bonds as at 31 December 2014 were treasury bonds with the nominal value of PLN 160,000 thousand. As at 31 December 2013, there was no additional collateral for the issue of covered bonds.

According to the Act on covered bonds and mortgage banks, the Bank is eligible to refinance mortgage-backed loans not exceeding 60% of the mortgage lending value 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 2014 amounted to PLN 2,653,030 thousand,
- 31 December 2013 amounted to PLN 2,019,926 thousand,

Both as at 31 December 2014 and 31 December 2013, mortgage covered bonds were backed by loan receivables secured by mortgages entered as the first item in the mortgage register.

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

- 31 December 2014 amounted to PLN 421,805 thousand,
- 31 December 2013 amounted to PLN 480,604 thousand,

As at 31 December 2014, the public sector covered bonds issued were backed by treasury bonds with the nominal value of PLN 30,000 thousand. As at 31 December 2013, there was no additional collateral for the issue of public sector covered bonds.

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 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 2014 amounted to PLN 2,667,214 thousand,
- 31 December 2013 amounted to PLN 1,978,248 thousand,

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 2014 amounted to PLN 350,000 thousand,
- 31 December 2013 amounted to PLN 350,000 thousand,

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

Financial statements in accordance with the International Financial Reporting Standards (IFRS) for the year 2014 (PLN '000)

As at 31.12.2014

Debt financial instruments by type	Nominal value	Interest rate as at 31.12.2014	Guarantee / collateral	Redemption date	Amount of liability
Long-term issues (with original maturity of over 1 year)					
Covered bonds (PLN)	100 000	3,03%	Mortgage cover bonds register	2015-05-15	100 342
Covered bonds (PLN)	100 000	3,56%	Mortgage cover bonds register	2015-07-07	101 695
Covered bonds (PLN)	100 000	3,99%	Public sector cover bonds register	2015-07-28	101 663
Covered bonds (PLN)	100 000	3,66%	Mortgage cover bonds register	2015-09-28	100 891
Covered bonds (PLN)	100 000	3,23%	Public sector cover bonds register	2015-11-30	100 240
Covered bonds (PLN)	200 000	3,15%	Mortgage cover bonds register	2016-04-20	201 072
Covered bonds (PLN)	150 000	4,09%	Public sector cover bonds register	2016-09-28	151 384
Covered bonds (PLN)	100 000	3,73%	Mortgage cover bonds register	2016-11-15	100 343
Covered bonds (PLN)	200 000	3,30%	Mortgage cover bonds register	2017-04-20	201 000
Covered bonds (PLN)	200 000	3,03%	Mortgage cover bonds register	2017-06-16	199 944
Covered bonds (PLN)	200 000	3,74%	Mortgage cover bonds register	2018-06-15	199 882
Covered bonds (PLN)	80 000	3,05%	Mortgage cover bonds register	2019-06-21	79 963
Covered bonds (PLN)	300 000	3,62%	Mortgage cover bonds register	2022-07-28	303 335
Covered bonds (PLN)	200 000	3,62%	Mortgage cover bonds register	2023-02-20	202 017
Covered bonds (EUR)	10 000	2,08%	Mortgage cover bonds register	2017-10-19	42 745
Covered bonds (EUR)	7 500	1,10%	Mortgage cover bonds register	2018-02-15	31 945
Covered bonds (EUR)	50 000	1,21%	Mortgage cover bonds register	2018-10-22	213 164
Covered bonds (EUR)	20 000	1,12%	Mortgage cover bonds register	2018-10-22	85 000
Covered bonds (EUR)	50 000	0,95%	Mortgage cover bonds register	2019-10-15	212 724
Covered bonds (EUR)	30 000	2,75%	Mortgage cover bonds register	2020-07-28	127 338
Covered bonds (EUR)	8 000	3,50%	Mortgage cover bonds register	2029-02-28	34 407
Covered bonds (EUR)	15 000	3,50%	Mortgage cover bonds register	2029-03-15	64 564
Covered bonds (EUR)	20 000	3,20%	Mortgage cover bonds register	2029-05-30	85 223
Bonds (PLN)	50 000	3,31%	no collateral	2015-03-16	50 072
Bonds (PLN)	20 000	4,14%	no collateral	2019-01-16	20 342
Bonds (PLN)	60 000	3,48%	no collateral	2019-01-21	60 293
Debt securities in issue (carrying value)					**3 171 588**

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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 cover bonds register	2014-04-28	25 174
Covered bonds (PLN)	200 000	4,11%	Mortgage cover bonds register	2014-07-28	203 435
Covered bonds (PLN)	100 000	4,07%	Mortgage cover bonds register	2015-09-28	100 921
Covered bonds (PLN)	100 000	3,94%	Mortgage cover bonds register	2014-11-28	100 307
Covered bonds (PLN)	100 000	3,88%	Public sector cover bonds register	2015-11-30	100 238
Covered bonds (PLN)	200 000	3,85%	Mortgage cover bonds register	2016-04-20	201 194
Covered bonds (PLN)	100 000	3,70%	Mortgage cover bonds register	2015-05-15	100 366
Covered bonds (PLN)	200 000	3,68%	Mortgage cover bonds register	2017-06-16	199 855
Covered bonds (PLN)	100 000	3,59%	Mortgage cover bonds register	2015-07-07	101 613
Covered bonds (PLN)	200 000	4,00%	Mortgage cover bonds register	2017-04-20	201 127
Covered bonds (PLN)	200 000	4,39%	Mortgage cover bonds register	2018-06-15	199 796
Covered bonds (EUR)	10 000	2,24%	Mortgage cover bonds register	2017-10-19	41 580
Covered bonds (PLN)	100 000	4,40%	Mortgage cover bonds register	2016-11-15	100 391
Covered bonds (PLN)	100 000	4,01%	Public sector cover bonds register	2015-07-28	101 576
Covered bonds (PLN)	150 000	4,50%	Public sector cover bonds register	2016-09-28	151 421
Covered bonds (PLN)	80 000	3,70%	Mortgage cover bonds register	2019-06-21	79 973
Covered bonds (EUR)	30 000	2,75%	Mortgage cover bonds register	2020-07-28	123 533
Covered bonds (EUR)	50 000	1,35%	Mortgage cover bonds register	2018-10-22	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**

Movements in the balance of debt securities issued

	31.12.2014	31.12.2013
As at the beginning of the period	**2 661 407**	**2 852 445**
Increase (due to)	1 278 672	903 726
- issue	1 154 178	776 826
- accrued interest	104 705	126 900
- currency translation differences	19 789	-
Decrease (due to)	(768 491)	(1 094 764)
- redemption	(665 000)	(950 000)
- interest repayment	(103 491)	(140 304)
- currency translation differences	-	(4 460)
As at the end of the period	**3 171 588**	**2 661 407**

Short-term (up to 1 year)	564 374	608 159
Long-term (over 1 year)	2 607 214	2 053 248

Fixed interest rate debt securities issued	396 532	133 481
Floating interest rate debt securities issued	2 775 056	2 527 926

30. Subordinated liabilities

SUBORDINATED LIABILITIES	Nominal value	Currency	Interest rate as at 31.12.2014	Maturity / redemption date	Balance of liability (PLN '000)
As at 31 December 2014					
mBANK S.A.	100 000	PLN	5,56%	19.12.2022	**100 257**

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**

Movements in the balance of subordinated liabilities

	31.12.2014	31.12.2013
As at the beginning of the period	**100 268**	**100 316**
Increase (due to)	6 105	6 722
- taking a loan	-	-
- interest on a loan	6 105	6 722
Decrease (due to)	(6 116)	(6 770)
- loan repayment	-	-
- repayment of interest on a loan	(6 116)	(6 770)
Subordinated liabilities as at the end of the period	**100 257**	**100 268**
Short-term (up to 1 year)	257	268
Long-term (over 1 year)	100 000	100 000

31. Other liabilities and provisions

31.1. Other liabilities

	31.12.2014	31.12.2013
Other liabilities (due to)	**14 001**	**19 788**
- accruals	11 474	5 847
- settlements with insurers	1 102	43
- provisions for unused holidays	672	598
- liabilities due to income tax on salaries and VAT	307	12 913
- other	446	387
Total other liabilities	**14 001**	**19 788**
Short-term (up to 1 year)	14 001	19 788
Long-term (over 1 year)	-	-

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31.2. Provisions

	31.12.2014	31.12.2013
Provisions (due to)	**88**	**84**
- off-balance sheet contingent liabilities granted	1	-
- provisions for retirement and disability benefits	88	84
Total provisions	**88**	**84**
Short-term (up to 1 year)	10	17
Long-term (over 1 year)	78	67

Movements in provisions for post-employment employee benefits — retirement and disability pension provision

	31.12.2014	31.12.2013
Provisions as at the beginning of the period	**84**	**112**
- write-down on the provision	7	9
- interest cost	3	6
- actuarial gains and losses are recognised in other comprehensive income	17	(43)
- benefits paid	(23)	-
Provisions as at the end of the period	**88**	**84**
Expected provision settlement period:		
Short-term (up to 1 year)	9	17
Long-term (over 1 year)	79	67

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 2014 and 2013).

Changes in deferred tax assets and provision are presented below:

Deferred income tax assets	As at 01.01.2014	Recognised in the income statement	Recognised in other comprehensive income	As at 31.12.2014
Interest accrued	4 728	7 338	-	**12 066**
Valuation of derivative financial instruments	176	2 032	-	**2 208**
Valuation of available-for-sale financial instruments	-	-	-	**-**
Amount of impairment write-downs on receivables*	8 188	1 887	-	**10 075**
Provisions and other liabilities related to employment benefits	229	697	-	**926**
Impairment write-downs on inventories	-	-	-	**-**
Accruals	484	916	-	**1 400**
Revenues to be settled (commissions settled using the effective interest rate method)	6 412	1 457	-	**7 869**
Foreign exchange differences	1 878	(1 878)	-	**-**
Total deferred income tax assets	**22 095**	**12 449**	**-**	**34 544**

Short-term (up to 1 year)	31 640
Long-term (over 1 year)	2 904

*The item "Amount of impairment write-downs on receivables" refers to write-downs on loans for which the Bank expects that their non-recoverability will be documented.

Financial statements in accordance with the International Financial Reporting Standards (IFRS) for the year 2014 (PLN '000)

Deferred income tax liabilities	As at 01.01.2014	Recognised in the income statement	Recognised in other comprehensive income	As at 31.12.2014
Interest accrued	(5 473)	(4 204)	-	**(9 677)**
Valuation of derivative financial instruments	(1 895)	(3 752)	-	**(5 647)**
Valuation of available-for-sale financial instruments	(342)	-	(66)	**(408)**
Provisions and other liabilities related to employment benefits	(8)	-	3	**(5)**
Prepaid costs	(1 195)	(3 639)	-	**(4 834)**
Foreign exchange differences	-	(2 356)	-	**(2 356)**
Difference between tax and balance sheet depreciation/amortisation	(124)	(67)	-	**(191)**
Total deferred income tax liabilities	**(9 037)**	**(14 018)**	**(63)**	**(23 118)**

Short-term (up to 1 year)	(23 118)
Long-term (over 1 year)	-

Deferred income tax assets (net)	As at 01.01.2014	Recognised in the income statement	Recognised in other comprehensive income	As at 31.12.2014
Total deferred income tax assets (net)	**13 058**	**(1 569)**	**(63)**	**11 426**

Short-term (up to 1 year)	8 522
Long-term (over 1 year)	2 904

Deferred income tax assets	As at 01.01.2013	Recognised in the income statement	Recognised in other comprehensive income	As at 31.12.2013
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 and other liabilities related to employment 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**
Foreign 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 (over 1 year)	7 484

*The item "Amount of impairment write-downs on receivables" refers to write-downs on loans for which the Bank expects that their non-recoverability will be documented.

Deferred income tax liabilities	As at 01.01.2013	Recognised in the income statement	Recognised in other comprehensive income	As at 31.12.2013
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)**
Provisions and other liabilities related to employment 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 (over 1 year)	-

Deferred income tax assets (net)	As at 01.01.2013	Recognised in the income statement	Recognised in other comprehensive income	As at 31.12.2013
Total deferred income tax assets (net)	**9 960**	**2 888**	**210**	**13 058**

Short-term (up to 1 year)	5 574
Long-term (over 1 year)	7 484

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Deferred tax recognised in the income statement	31.12.2014	31.12.2013
Interest accrued	3 134	(899)
Valuation of derivative financial instruments	(1 720)	(1 074)
Amount of impairment write-downs on receivables*	1 887	4 330
Provisions and other liabilities related to employment benefits	697	(161)
Impairment write-downs on inventories	-	(569)
Accruals	916	288
Revenues to be settled (commissions settled using the effective interest rate method)	1 457	634
Prepaid costs	(3 639)	(320)
Difference between tax and balance sheet depreciation/amortisation	(67)	(31)
Exchange differences	(4 234)	690
Total deferred tax recognised in the income statement	**(1 569)**	**2 888**

*The item "Amount of impairment write-downs on receivables" refers to write-downs on loans for which the Bank expects that their 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. Differences between the balance-sheet changes in items and changes in such items recognised under operating activities in the statement of cash flows

The following table provides additional information to the statement of cash flows and presents differences between the balance-sheet changes in items and changes in such items recognised under operating activities in the statement of cash flows.

PLN '000	Year ended 31 December	
	2014	2013
Amounts due from other banks, change resulting from balance-sheet balances	(8 595)	(12 095)
Interest accrued and not yet received in the current year	1	-
Interest accrued in the previous year and received in the current year	(2)	
Exclusion of change in cash and cash equivalents	8 595	12 095
Change in amounts due from other banks, in total	**(1)**	**-**
Derivative financial instruments, change resulting from balance-sheet values	(15 214)	(1 968)
Interest accrued and not received / not paid in the current year	9 748	3 587
Interest accrued in the previous year, and received / paid in the current year	(3 586)	(7 275)
Change in respect of derivative financial instruments, in total	**(9 052)**	**(5 656)**
Loans and advances to customers, change resulting from balance-sheet values	(1 280 741)	63 155
Interest accrued and not yet received in the current year	26 517	17 713
Interest accrued in the previous year and received in the current year	(25 479)	(22 827)
Change in loans and advances to customers	**(1 279 703)**	**58 041**
Investment securities available for sale, change resulting from balance-sheet values	(129 396)	(39 566)
Interest accrued and not yet received in the current year	3 060	2 875
Interest accrued in the previous year and received in the current year	(2 557)	(3 070)
Exclusion of change in cash and cash equivalents	(35 455)	30 600
Valuation recognised in other comprehensive income	349	(1 149)
Change in investment securities, in total	**(163 999)**	**(10 310)**
Amounts due to other banks, change resulting from balance-sheet values	777 146	31 021
Interest accrued and not paid in the current year	(6 256)	(3 684)
Interest accrued in the previous year and paid in the current year	3 807	3 469
Exclusion of change in cash from financing activities	(797 775)	(291 246)
Change in amounts due to other banks, in total	**(23 078)**	**(260 440)**
Amounts due to customers, change resulting from balance-sheet values	(45 155)	116 134
Interest accrued and not paid in the current year	(132)	(186)
Interest accrued in the previous year and paid in the current year	186	143
Change in amounts due to customers, in total	**(45 101)**	**116 091**
Debt securities in issue, change resulting from balance-sheet values	510 181	(191 038)
Interest accrued and not paid in the current year	(28 132)	(21 462)
Interest accrued in the previous year and paid in the current year	26 999	36 116
Exclusion of change in cash from financing activities	(489 178)	173 174
Change in debt securities in issue, in total	**19 870**	**(3 210)**
Subordinated liabilities, change resulting from balance-sheet values	(11)	(48)
Interest accrued and not paid in the current year	(259)	(270)
Interest accrued in the previous year and paid in the current year	270	318
Change in subordinated liabilities, in total	**-**	**-**
Other liabilities and provisions, change resulting from balance-sheet values	(5 783)	15 750
Actuarial valuation of provisions for post-employment benefits recognised in other comprehensive income	(17)	43
Change in other liabilities and provisions, in total	**(5 800)**	**15 793**

Financial statements in accordance with the International Financial Reporting Standards (IFRS) for the year 2014 (PLN '000)

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

In 2014, the Bank was not involved in any proceedings before a court, arbitration body, or public administration authority which represent at least 10% of the Bank's equity.

As at 31 December 2014, proceedings were pending before the District Court in Poznań concerning an action brought by the Bank against a limited borrower who acquired a mortgaged real property from the Bank. Value of the subject of dispute is PLN 11,692 thousand.
The Bank acts as the assignee under an agreement for assignment 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 real property fire. The Insurer paid compensation which did not cover the loss. The Bank, as an authorised entity 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, 20th Commercial Division, against the Insurer for the payment of compensation in the amount of PLN 18,494 thousand. After the lawsuit was filed the Insurer has voluntarily satisfied a part of the Bank's claim by paying to the Bank the net amount of PLN 6,523 thousand. On 24 February 2014 the Court issued a payment order instructing the Insurer to pay to the Bank the amount of PLN 18,494 thousand with the statutory interest. On 26 March 2014, the Insurer successfully filed an objection against the payment order. On 10 June 2014 the Bank filed a reply to the objection of the Insurer and extended the amount claimed by PLN 1,324 thousand by way of capitalised interest together with statutory interest due as from the date of filing the lawsuit until the date of payment. In November 2014, the case was submitted to mediation, however none of the parties agreed to the mediation. As at 31 December 2014 the date of the first hearing was not appointed.

35. Off-balance sheet liabilities

31.12.2014	Up to 1 year	From 1 to 5 years	Over 5 years	Total
1. Off-balance sheet liabilities granted and received	**1 089 041**	**166 956**	**-**	**1 255 997**
Liabilities granted	**918 862**	**166 956**	**-**	**1 085 818**
1. Financial liabilities:	918 862	166 956	-	1 085 818
a) Lending commitments	915 896	161 072	-	1 076 968
b) Operating lease liabilities	2 966	5 884	-	8 850
Liabilities received:	**170 179**	**-**	**-**	**170 179**
a) Financial liabilities received	170 179	-	-	170 179
2. Derivative financial instruments	**3 008 022**	**170 492**	**622 296**	**3 800 810**
1. Interest rate derivatives	1 700 000	170 492	622 296	2 492 788
2. Foreign exchange derivatives	1 308 022	-	-	1 308 022
Total off-balance sheet items	**4 097 063**	**337 448**	**622 296**	**5 056 807**

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**

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36. Pledged assets

In accordance with the Act on the Bank Guarantee Fund, as at 31 December 2014, the Bank held treasury bonds in the amount of PLN 2,123 thousand (with a nominal value of PLN 2,000 thousand), whereas as at 31 December 2013 it held Central Bank's bills in the amount of PLN 1,500 thousand (with a nominal value of PLN 1,500 thousand) which constituted collateral for the guaranteed deposits protection fund. These assets are shown in the balance sheet under "Investment securities available for sale".

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

Additionally, the Bank secured mortgage and public sector covered bonds issued with treasury bonds with the total value of PLN 200,614 thousand.

37. Registered share capital

As at 31 December 2014, the total number of ordinary shares was 2,850,000 (as at 31 December 2013: 2,750,000) shares with a nominal value of PLN 100 each (as at 31 December 2013: PLN 100 each). On 13 November 2014, mBank Hipoteczny S.A. carried out a private issue of 100,000 ordinary registered shares without pre-emptive rights. On 30 December 2014, 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	Equity (PLN)	Shares		Voting rights at the General Shareholders' Meeting	
		Number of shares	%	Number of shares	%
MLV 45 Sp. z o.o. spółka komandytowa*	208 214 300	2 082 143	73,06	2 082 143	73,06
mBank S.A.	76 785 700	767 857	26,94	767 857	26,94
Total	**285 000 000**	**2 850 000**	**100,00**	**2 850 000**	**100,00**

*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) AS AT 31 DECEMBER 2014							
Share type	Type of preference	Type of restrictions	Number of shares	Series / issue at par value (PLN)	Means of covering share capital	Registration date	Right to dividend
registered	-	-	500 000	50 000 000	cash	16.04.1999	01.01.2000
registered	-	-	850 000	85 000 000	cash	20.09.2000	01.01.2001
registered	-	-	400 000	40 000 000	cash	24.04.2006	01.01.2006
registered	-	-	1 000 000	100 000 000	cash	08.01.2013	01.01.2013
registered	-	-	100 000	10 000 000	cash	30.12.2014	01.01.2015
Total number of shares			**2 850 000**				
Total registered share capital				**285 000 000**			

38. Share premium

Share premium is formed from the share premium obtained from the issue of shares reduced by the direct costs incurred with that issue. This capital is intended to cover all losses that may result from the business activity of the Bank.

In 2014, share premium resulted from the issue of shares described in Note 37.

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39. Retained earnings

	31.12.2014	31.12.2013
Other supplementary capital	192 469	192 315
General banking risk reserve	33 000	31 000
Profit for the current year	22 371	2 154
Total retained earnings	**247 840**	**225 469**

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.

According to the Resolution No 2 passed by the General Shareholders' Meeting of mBank Hipoteczny S.A. on 11 April 2014, the net profit of 2013 was distributed as follows:

- supplementary capital — PLN 154 thousand,
- General Risk Fund — PLN 2,000 thousand.

The Bank plans to transfer the net profit of 2014 to its statutory supplementary capital and partially to the General Risk Fund.

40. Other components of equity

	31.12.2014	31.12.2013
Available-for-sale financial assets	**1 742**	**1 459**
Unrealised gains on debt instruments	1 742	1 459
Actuarial gains and losses on post-employment benefits	**21**	**35**
Actuarial gains of the defined benefit pension plan	21	35
Total comprehensive income net of tax	**1 763**	**1 494**

41. Dividend per share

mBank Hipoteczny S.A. does not plan to pay a dividend for 2014, nor did it pay any for 2013.

42. 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.

	31.12.2014	31.12.2013
Cash and balances with the central bank (Note 18)	7 669	7 378
Amounts due from other banks (Note 19)	30 972	22 377
Central bank's bills	479 973	515 428
Total cash and cash equivalents	**518 614**	**545 183**

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43. Related party transactions

MLV 45 sp. z o.o. spółka komandytowa 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 (formerly: BRE Holding Sp. z o.o.). 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.).

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, liabilities in respect of debt securities in issue, deposits and derivative transactions.

The following table presents financial liabilities towards mBank S.A., broken down by contractual maturity dates.

31.12.2014	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	117 527	204 262	74 838	-	-	**396 627**
Loans received	-	-	171 038	1 057 183	-	**1 228 221**
Other financial liabilities with deferred payment term	-	-	346 533	-	-	**346 533**
Subordinated loan	-	-	-	-	100 257	**100 257**
Covered bonds and bonds in issue	-	-	88 080	315 883	8 392	**412 355**
Derivative financial instruments	3 812	1 296	4 289	45	-	**9 442**
Liabilities in respect of cash collateral	9 253	-	-	-	-	**9 253**

Other financial liabilities with deferred payment term relate to a liability resulting from agreements concluded with mBank S.A. on the transfer of a portfolio of retail loans secured with a mortgage on real estate and an agreement on the transfer of a commercial loan secured with a mortgage.

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**
Covered bonds and bonds in issue	-	99	139 456	440 814	-	**580 369**
Derivative financial instruments	-	-	8	-	269	**277**

Information on the interest rate of deposits has been disclosed in Note 27. Information on the interest rate of the subordinated loan has been disclosed in Note 30.

<u>The most important agreements/transactions concluded with related companies in 2014</u>

<u>Agreements concluded with mBank S.A. in 2014:</u>

1. On 3 March 2014, an agreement on cooperation in servicing developers for whom mBank S.A. opens and maintains an Open Housing Escrow Account and mBank Hipoteczny S.A. grants a loan for a development project.
2. On 5 June 2014, a licence agreement for using the trademark in the scope related to business activity conducted by mBank Hipoteczny S.A.
3. On 24 July 2014, a deposit agreement was concluded, under which mBank S.A. undertakes to place a deposit with mBank Hipoteczny S.A., the value of which will not exceed PLN 150,000 thousand.
4. On 28 August 2014, a framework agreement on the acquisition of portfolios of receivables in respect of mortgage-backed loans in order to refinance them through the issue of mortgage covered bonds and on entrusting mBank S.A. with further servicing of the acquired portfolios by mBank Hipoteczny S.A. was signed. The agreement sets out principles under which mBank S.A. will transfer the portfolios to mBank Hipoteczny S.A. and mBank Hipoteczny S.A. will acquire them from mBank S.A. in order to refinance them through the issue of mortgage covered bonds. The following agreements were concluded as part of this agreement:

- Portfolio transfer agreement concluded on 28 August 2014, under which mBank Hipoteczny S.A. acquired from mBank S.A. a retail portfolio of mortgage-backed loans with the fair value of PLN 839 thousand;
- Portfolio transfer agreement concluded on 30 September 2014, under which mBank Hipoteczny S.A. acquired from mBank S.A. a retail portfolio of mortgage-backed loans with the fair value of PLN 306,818 thousand;

5. On 10 September 2014, a loan agreement was signed for a loan in the amount up to PLN 1,183,750 thousand which can be drawn in PLN or EUR, for the purpose of financing current operations.
6. On 20 October 2014, a commercial loan transfer agreement was signed, under which mBank Hipoteczny S.A. acquired from mBank S.A. a receivable secured with a mortgage on commercial property with the value of EUR 8,600 thousand.

<u>Agreements concluded with mBank Group companies:</u>

1. On 7 January 2014, mBank Hipoteczny S.A. and BRE Ubezpieczenia Sp. z o. o. concluded an agreement on the payment of a cash bonus.
2. On 12 May 2014, a group insurance contract with BRE Ubezpieczenia TUiR S.A. was concluded, in respect of covering the repayment of loan instalments by the Bank Customers with a group insurance by BRE Ubezpieczenia TUiR S.A.

<u>Agreements concluded with Commerzbank AG in 2014:</u>

1. On 13 February 2014, an agreement was concluded for the acquisition by Commerzbank AG of mortgage covered bonds (in EUR) of series HPE4 on the secondary market, with the nominal value of EUR 7,500 thousand.
2. On 26 February 2014, an agreement was concluded for the acquisition by Commerzbank AG of mortgage covered bonds (in EUR) of series HPE5 on the secondary market, with the nominal value of EUR 8,000 thousand.
3. On 13 March 2014, an agreement was concluded for the acquisition by Commerzbank AG of mortgage covered bonds (in EUR) of series HPE6 on the secondary market, with the nominal value of EUR 15,000 thousand.
4. On 28 May 2014, an agreement was concluded for the acquisition by Commerzbank AG of mortgage covered bonds (in EUR) of series HPE7 on the secondary market, with the nominal value of EUR 20,000 thousand.

In 2014, as in 2013, 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 as at 31 December 2014 and 31 December 2013 and related costs and income for 2014 and 2013.

(PLN '000)	mBank Group companies*		BDH Development Sp. z o.o.		mBANK S.A.		Commerzbank AG		Commerzbank Group companies**	
As at the end of the period	**31.12.2014**	**31.12.2013**	**31.12.2014**	**31.12.2013**	**31.12.2014**	**31.12.2013**	**31.12.2014**	**31.12.2013**	**31.12.2014**	**31.12.2013**
Statement of financial position										
Assets	4 317	-	-	52 761	68 412	35 286	-	-	-	-
Liabilities	4 374	28 442	-	53 576	2 502 849	1 854 349	-	-	425 888	207 085

(PLN '000)	mBank Group companies*		BDH Development Sp. z o.o.		mBANK S.A.		Commerzbank AG		Commerzbank Group companies**	
Year ended	**31.12.2014**	**31.12.2013**	**31.12.2014**	**31.12.2013**	**31.12.2014**	**31.12.2013**	**31.12.2014**	**31.12.2013**	**31.12.2014**	**31.12.2013**
Income statement										
Interest income	291	-	-	-	18 305	13 938	-	12 333	-	-
Interest expense	212	464	-	-	(42 015)	(48 185)	-	-	3 226	323
Fee and commission income	1 686	-	-	-	-	-	-	-	-	-
Fee and commission expenses	(38)	(43)	-	-	(905)	(2)	-	-	-	-
Net trading income	-	-	-	-	12 859	7 357	-	(1 700)	-	-
Other operating income	-	-	-	5 658	240	150	-	-	-	-
Other operating expenses	(5)	(44)	-	(2 918)	-	-	-	-	-	-
Overhead costs, amortisation and depreciation	(1 099)	(715)	-	-	(3 364)	(114)	-	-	-	-
Contingent liabilities										
Liabilities received	-	-	-	-	170 179	169 033	-	-	-	-
Derivatives (purchase, sales)										
IRS contracts	-	-	-	-	2 492 788	663 552	-	-	-	-
FX SWAP contracts	-	-	-	-	1 306 742	1 325 005	-	-	-	-

*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., BRE Ubezpieczenia TUiR S.A., BRE Ubezpieczenia Sp. z o.o., BRE Agent Ubezpieczeniowy Sp. z o. o.

** The item "Commerzbank Group companies" includes transactions of acquisition of mortgage covered bonds on the secondary market by Comdirect Bank AG.

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

As at 31 December 2014 and 31 December 2013, the composition of the Management Board was as follows:

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 2014, as at 31 December 2014 and 31 December 2013, is presented below:

	Gross remuneration paid in 2014	Other benefits paid in 2014	Discretionary award paid in 2014	Gross remuneration paid in 2013	Other benefits paid in 2013	Bonus for 2012 paid in 2013 (cash settlement of a phantom share-based incentive program)
Piotr Cyburt	756	8	-	762	15	54
Marcin Romanowski	731	8	-	591	5	27
Marcin Wojtachnio	480	6	90	405	6	54
Total	**1 967**	**22**	**90**	**1 758**	**26**	**135**

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 an advisor to the Management Board	Other benefits paid in 2013	Gross remuneration paid in 2013 for performing the function of the Member of the Management Board	Severance payment paid in 2013
Sven-Torsten Kain	17	12	235	1 295
Total	**17**	**12**	**235**	**1 295**

In 2014 the accrual for employee and Management Board awards/bonuses amounted to PLN 4,104 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 899.7 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 — Members 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 2014:

1. Cezary Kocik - Chairman of the Supervisory Board,
2. Hans-Dieter Kemler - Deputy Chairman of the Supervisory Board, Member of the Audit Committee, Member of the Risk Committee,
3. Jörg Hessenmüller - Member of the Supervisory Board, Chairman of the Audit Committee, Member of the Risk Committee,
4. Lidia Jabłonowska-Luba - Member of the Supervisory Board, Chairwoman of the Risk Committee,
5. Michał Popiołek - Member of the Supervisory Board, Member of the Risk Committee,

6. Dariusz Solski - Member of the Supervisory Board, Member of the Audit Committee,
7. Mariusz Tokarski - Member of the Supervisory Board, Member of the Audit Committee.

On 11 April 2014, the Supervisory Board was appointed for the ninth term of office by the Annual General Meeting of mBank Hipoteczny S.A. in the above composition, except for Mr Mariusz Tokarski who was appointed Member of the Supervisory Board on 3 July 2014 and member of the Audit Committee on 16 July 2014.

The following persons were not appointed Members of the Supervisory Board of mBank Hipoteczny S.A. for the ninth term of office: Ms Jolanta Daniewska and Mr. Piotr Baranek (Members of the Supervisory Board during the previous term of office).

On 2 July 2014, Mr Hans-Dieter Kemler was appointed to the Audit Committee.

In 2014, Members of the Supervisory Board did not receive any remuneration, except for Ms Jolanta Daniewska, who, as a Member of the Supervisory Board during the previous term of office for the period until the expiry of that term of office, received remuneration for 2014 in the amount of PLN 12 thousand and Mr Mariusz Tokarski, who received remuneration for 2014 in the amount of PLN 18 thousand (for the period from being appointed until 31 December 2014).

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

1. Cezary Kocik - Chairman of the Supervisory Board,
2. Hans-Dieter Kemler - Deputy Chairman of the Supervisory Board, Member of the Risk Committee,
3. Jolanta Daniewska - Member of the Supervisory Board, Member of the Audit Committee,
4. Lidia Jabłonowska-Luba - Member of the Supervisory Board, Chairwoman of the Risk Committee,
5. Jörg Hessenmüller - Member of the Supervisory Board, Chairman of the Audit Committee, Member of the Risk Committee,
6. Michał Popiołek - Member of the Supervisory Board, Member of the Risk Committee,
7. Dariusz Solski - Member of the Supervisory Board, Member of the Audit Committee,
8. Piotr Baranek - Member of the Supervisory Board, Member 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.

In accordance with paragraph 14, item 5 of the Memorandum of Association of mBank Hipoteczny S.A., the General Shareholders' Meeting decides, by resolution, on appointing and recalling 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.

44. Information on the registered audit company

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

The total fee of Ernst & Young Audyt Polska spółka z ograniczoną odpowiedzialnością s.k. (formerly: Ernst & Young Audit sp. z o.o.) for 2014 amounted to PLN 303 thousand.

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 450 thousand.

45. Capital adequacy ratio / capital adequacy

One of the main tasks of the balance sheet management is to ensure an appropriate level of capital. Within the framework of the Bank's capital management policy, mBank Hipoteczny S.A. prepares the guidelines for the most effective planning and use of capital basis which:

- are compliant with external and internal regulations in force,
- guarantee a continuity of financial targets achievement, which render an appropriate rate of return for shareholders,
- ensure the maintenance of a strong capital basis being a fundamental support for business development.

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

- maintenance of an optimal level and structure of own funds with the application of available methods and means, like retention of net profit, subordinated loan or issue of shares,
- effective use of existing capital, among others through application of a set of measures of effective use of the capital, limitation of activities that do not provide an expected rate of return and development of products with lower capital absorption.

Effective use of capital is an integral part of the capital management policy oriented at reaching an optimal rate of return on capital and as a result forming a stable fundament of reinforcement of the capital basis in future periods. This enables to maintain the Common Equity Tier 1 capital ratio and the total capital ratio at least on the level required by the supervision authority.

The strategic capital objectives of the Bank are aimed at maintaining the capital ratio above the level of 12% and the as well as the Common Equity Tier 1 capital ratio above the level of 9%.

Capital ratios / Capital adequacy ratio

Until 31 December 2013 the calculation of the capital adequacy ratio, the own funds and the total capital requirement in the Bank was made according to the following regulations:

- 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 258/2011 of the Polish Financial Supervision Authority of 4 October 2011 (Official Journal of PFSA of 2011 No 11, item 42),
- 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 384/2008 of the Polish Financial Supervision Authority of 17 December 2008 (Official Journal of PFSA of 2008 No 8, item 38) as amended,
- Resolution No 387/2008 of the Polish Financial Supervision Authority of 17 December 2008 (Official Journal of PFSA of 2008 No 8, item 41).

Beginning from 1 January 2014 the calculation of capital ratios, own funds and the total risk exposure amount in the Bank is made according to Regulation (EU) No 575/2013 of the European Parliament and of the Council of 26 June 2013 on prudential requirements for credit institutions and investment firms and amending Regulation (EU) No 648/2012 (hereinafter referred to as CRR Regulation) and other Commission (EU) implementing regulations to the CRR Regulation.

As at 31 December 2014, the capital ratio of mBank Hipoteczny S.A. amounted to 13.31% (as at 31 December 2013: 14.92%). At the same time, the Common Equity Tier 1 capital ratio of mBank Hipoteczny S.A. amounted to 10.95% (as at 31 December 2013: 11.98%).

Own funds

In accordance with the CRR Regulation, own funds consist of Common Equity Tier 1 capital, Additional Tier 1 capital and Tier 2 capital, however items that could be treated as Additional Tier 1 capital are not identified in mBank Hipoteczny S.A.

Common Equity Tier 1 capital of mBank Hipoteczny S.A. contains:

- equity instruments and the related share premium accounts,
- retained earnings,
- accumulated other comprehensive income,
- general risk funds,
- independently identified interim profits,
- items deducted from a Common Equity Tier 1 capital (including: additional value adjustments, intangible assets, negative amounts resulting from the calculation of expected loss amounts, net impairment losses and regulatory adjustments relating to unrealised gains and losses).

Tier 2 capital of mBank Hipoteczny S.A. contains subordinated liabilities.

As at 31 December 2014, own funds of the Bank amounted to PLN 563,947 thousand (as at 31 December 2013: PLN 507,993 thousand).

Total risk exposure amount

The total risk exposure amount contains:

- risk weighted exposure amounts for credit risk, counterparty credit risk and dilution risk and free deliveries,
- total operational risk exposure amount.

In calculation of the Bank's capital ratios, the total risk exposure amount is determined taking into account the credit risk exposure amount, applying 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).

In the second quarter of 2014, the Bank was given permission to apply the IRB slotting approach for another 3 models, as a result of which the coverage of the loan portfolio with the advanced internal rating-based approach increased, as at the end of 2014, to 86.35% of credit risk exposures determined using the standard method.

As at 31 December 2014, the total risk exposure amount of the Bank was PLN 4,236,952 thousand, including the credit risk exposure of PLN 4,078,327 thousand.

As at 31 December 2013, the total risk exposure amount of the Bank was PLN 3,405,776 thousand, including the credit risk exposure of PLN 3,250,026 thousand.

Financial leverage ratio

As of 1 January 2014, the Bank calculates the Common Equity Tier 1 capital, regulatory adjustment of the Common Equity Tier 1 capital and the total exposure amount for the purpose of calculation of the financial leverage ratio, based on provisions of the CRR Regulation.

As at 31 December 2014, the financial leverage ratio amounted to 6.93% and was calculated as the simple arithmetical mean of monthly leverage ratios during the fourth quarter. At the same time, the average Common Equity Tier 1 capital in the fourth quarter was PLN 424,457 thousand, while the average total exposure in the fourth quarter amounted to PLN 6,122,637 thousand.

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.

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Internal capital is the amount of capital estimated and required to cover all material risks identified in the Bank's operations. Internal capital is the total sum of the economic capital to cover risks included in economic capital calculation and capital necessary to cover other risks (including hard to quantify risks).

The Internal Capital Adequacy Assessment Process 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:

- risk inventory in the Bank's operations,
- calculation of internal capital for coverage of risk,
- stress tests,
- planning of economic capital,
- 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 Internal Capital Adequacy Assessment Process 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 Management Board of mBank Hipoteczny S.A. is responsible for the Internal Capital Adequacy Assessment Process.

Capital adequacy	31.12.2014	31.12.2013
Common Equity Tier 1 capital	**463 947**	**407 993**
- Equity instrument eligible as Common Equity Tier 1 capital	374 938	275 000
- Retained earnings	13 816	-
- other accumulated comprehensive income	1 762	1 441
- other reserves	192 469	192 315
- General banking risk reserves	33 000	31 000
- Additional value adjustments in the Tier 1 transitional period	(1 762)	-
- Intangible assets	(4 964)	(3 548)
- IRB shortfall of credit risk adjustments to expected losses	(133 465)	(88 215)
- Other deductions from Common Equity Tier 1 capital	(11 847)	-
Tier 2 capital	**100 000**	**100 000**
- equity instruments and subordinated loans eligible as Tier 2 capital	100 000	100 000
I. Own funds	**563 947**	**507 993**
II. Risk weighted exposure amounts for credit risk, counterparty credit risk, dilution risk and deliveries with deferred settlement date:	**4 078 327**	**3 250 026**
- with application of standardised approach	3 429 080	2 423 066
- with application of AIRB approach	649 247	826 960
III. Total operational risk exposure amount	**158 625**	**155 750**
IV. Total risk exposure amount	**4 236 952**	**3 405 776**
V. Common Equity Tier 1 capital ratio	**10,95%**	**11,98%**
VI. Total capital ratio	**13,31%**	**14,92%**
VII. Internal capital	**349 008**	**293 346**

In the absence of implementation into national law of Directive 2013/36/EC of the European Parliament and of the Council of 26 June 2013 on access to the activity of credit institutions and the prudential supervision of credit institutions and investment firms, amending Directive 2002/87/EC and repealing Directives 2006/48/EC and 2006/49/EC, and the absence of competent authorities to perform the functions and duties provided for in the aforesaid Directive and Regulation (EU) No 575/2013 of the European Parliament and of the Council of 26 June 2013 on prudential requirements for credit institutions and investment firms and amending Regulation (EU) No 648/2012, inter alia, with regard to assessment whether the issues of instruments in common equity Tier I comply with the criteria set out in Article 28 of the aforesaid Regulation, there is uncertainty as to the classification of instruments, issued on 13 November 2014, as instruments in common equity Tier 1. Pursuant to Article 26(3) of the aforesaid Regulation in respect of issues taking place after 28 June 2013, the institutions classify equity instruments as instruments in common equity Tier I only after they obtain approvals from relevant authorities. If the issue of instruments of 13 November 2014 were not included in common equity Tier I, the common equity Tier I ratio would be 8.59%, and the equity Tier I ratio and the total equity ratio would not change as at 31 December 2014.

46. Post balance-sheet date events

On 30 January 2015, a portfolio transfer agreement was concluded between mBank S.A. and mBank Hipoteczny S.A. Under this agreement, mBank Hipoteczny S.A. acquired a retail portfolio of mortgage-backed loans with the fair value of PLN 114,917 thousand from mBank S.A.

On 3 February 2015, the Management Board of mBank Hipoteczny S.A., by way of resolution No 10/2015, decided to terminate the cash bonus agreement concluded on 7 January 2014 between mBank Hipoteczny S.A. and BRE Ubezpieczenia Sp. z o.o. The agreement with BRE Ubezpieczenia Sp. z o.o. will be terminated by mutual consent of the Parties, as of 31 March 2015.

On 20 February 2015, mBank Hipoteczny S.A. issued 7-year variable-interest rate mortgage covered bonds with a nominal value of EUR 200,000 thousand.

On 25 February 2015, mBank Hipoteczny S.A. issued 7-year fixed-interest rate mortgage covered bonds with a nominal value of EUR 20,000 thousand.

On 25 February 2015, the Bank concluded a new hedging relation to hedge against the interest rate risk. The hedged item are fixed-interest rate mortgage covered bonds issued on 25 February 2015, with a nominal value of EUR 20,000 thousand. The hedged item is an IRS transaction with a nominal value of EUR 20,000 thousand, swapping the fixed interest rate for a variable interest rate.