mBank S.A.
IFRS Financial Statements
2021

Official Financial Statements of mBank S.A. for 2021 was prepared in accordance with the requirements of the ESEF. This document is not the official version of the Financial Statements of mBank S.A. for 2021, but was prepared on the basis of the original prepared in the ESEF format and is a copy of it. This document was not the subject of the attestation procedures performed by the statutory auditor.

This document is a translation from the original Polish version. In case of any discrepancies between the Polish and English versions, the Polish version shall prevail.

Selected financial data

The selected financial data are supplementary information to these financial statements of mBank S.A. for 2021.

SELECTED FINANCIAL DATA	PLN thousand		EUR thousand	
	Year ended 31 December		Year ended 31 December	
	2021	2020	2021	2020
I. Interest income	3 879 243	4 109 239	847 459	918 430
II. Fee and commission income	2 532 315	2 095 250	553 209	468 296
III. Net trading income	78 317	183 724	17 109	41 063
IV. Operating profit	(273 324)	1 043 144	(59 710)	233 146
V. Profit (loss) before income tax	(680 227)	572 996	(148 602)	128 067
VI. Net profit (loss)	(1 215 353)	93 047	(265 506)	20 796
VII. Net cash flows from operating activities	9 863 509	(2 736 186)	2 154 781	(611 548)
VIII. Net cash flows from investing activities	(417 555)	(278 830)	(91 219)	(62 320)
IX. Net cash flows from financing activities	(1 218 481)	(1 014 965)	(266 189)	(226 848)
X. Total net increase / decrease in cash and cash equivalents	8 227 473	(4 029 981)	1 797 373	(900 715)
XI. Basic earnings / (losses) per share (in PLN/EUR)	(28.68)	2.20	(6.27)	0.49
XII. Diluted earnings / (losses) per share (in PLN/EUR)	(28.63)	2.20	(6.25)	0.49
XIII. Declared or paid dividend per share (in PLN/EUR)	-	-	-	-

SELECTED FINANCIAL DATA	PLN thousand		EUR thousand	
	As at		As at	
	31.12.2021	31.12.2020 - restated	31.12.2021	31.12.2020 - restated
I. Total assets	191 873 819	170 745 007	41 717 141	36 999 438
II. Amounts due to other banks	3 420 001	2 624 286	743 575	568 667
III. Amounts due to customers	159 905 991	137 778 034	34 766 707	29 855 689
IV. Equity	13 381 823	16 467 692	2 909 471	3 568 452
V. Share capital	169 540	169 468	36 861	36 723
VI. Number of shares	42 384 884	42 367 040	42 384 884	42 367 040
VII. Book value per share (in PLN/EUR)	315.72	388.69	68.64	84.23
VIII. Total capital ratio	19.01	22.95	19.01	22.95

The following exchange rates were used in translating selected financial data into euro:

- for items of the statement of financial position – exchange rate announced by the National Bank of Poland as at 31 December 2021: EUR 1 = PLN 4.5994 and 31 December 2020: EUR 1 = PLN 4.6148 PLN;
- for items of the income statement – exchange rate calculated as the arithmetic mean of exchange rates announced by the National Bank of Poland as at the end of each month of 2021 and 2020: EUR 1 = PLN 4.5775 and EUR 1 = PLN 4.4742 respectively.

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INCOME STATEMENT

	Note	Year ended 31 December	
		2021	**2020**
Interest income, including:	5	3 879 243	4 109 239
Interest income accounted for using the effective interest method		*3 409 087*	*3 647 495*
Income similar to interest on financial assets at fair value through profit or loss		*470 156*	*461 744*
Interest expenses	5	(257 066)	(568 077)
Net interest income		**3 622 177**	**3 541 162**
Fee and commission income	6	2 532 315	2 095 250
Fee and commission expenses	6	(712 664)	(636 291)
Net fee and commission income		**1 819 651**	**1 458 959**
Dividend income	7	30 095	31 271
Net trading income	8	78 317	183 724
Gains or losses on non-trading financial assets mandatorily at fair value through profit or loss	9	3 744	17 740
Gains less losses from derecognition of assets and liabilities not measured at fair value through profit or loss	10	76 622	95 114
Other operating income	11	44 314	45 343
Impairment or reversal of impairment on financial assets not measured at fair value through profit or loss	14	(782 861)	(1 031 276)
Result on provisions for legal risk related to foreign currency loans	34	(2 758 079)	(1 021 714)
Overhead costs	12	(1 817 885)	(1 774 844)
Depreciation	25,26	(376 780)	(376 363)
Other operating expenses	13	(212 639)	(125 972)
Operating profit (loss)		**(273 324)**	**1 043 144**
Tax on the Bank's balance sheet items		(577 565)	(500 030)
Share in profits (losses) of entities under the equity method	23	170 662	29 882
Profit (loss) before income tax		**(680 227)**	**572 996**
Income tax expense	15	(535 126)	(479 949)
Net profit (loss)		**(1 215 353)**	**93 047**

Net profit (loss)	**16**	**(1 215 353)**	**93 047**
Weighted average number of ordinary shares	**16**	**42 369 790**	**42 355 695**
Earnings (losses) per share (in PLN)	**16**	**(28.68)**	**2.20**
Weighted average number of ordinary shares for diluted earnings	**16**	**42 450 509**	**42 379 726**
Diluted earnings (losses) per share (in PLN)	**16**	**(28.63)**	**2.20**

Notes presented on pages 10–163 constitute an integral part of these Financial Statements.

IFRS Financial Statements 2021 (PLN thousand)

STATEMENT OF COMPREHENSIVE INCOME

	Note	Year ended 31 December	
		2021	2020
Net profit (loss)		**(1 215 353)**	**93 047**
Other comprehensive income net of tax, including:	**17**	**(1 881 075)**	**249 412**
Items that may be reclassified subsequently to the income statement			
Exchange differences on translation of foreign operations (net)		4 803	2 854
Cash flows hedges (net)	17	(901 645)	283 530
Share of other comprehensive income of entities under the equity method (net)	17	(28 110)	9 898
Debt instruments at fair value through other comprehensive income (net)	17	(974 268)	(40 635)
Items that will not be reclassified to the income statement			
Actuarial gains and losses relating to post-employment benefits (net)	17	6 709	(6 235)
Reclassification to investment properties (net)	17	11 436	-
Total comprehensive income (net)		**(3 096 428)**	**342 459**

Notes presented on pages 10–163 constitute an integral part of these Financial Statements.

IFRS Financial Statements 2021 (PLN thousand)

STATEMENT OF FINANCIAL POSITION

ASSETS	Note	31.12.2021	31.12.2020 - restated	01.01.2020 - restated
Cash and balances with the Central Bank	18	12 087 608	3 939 298	7 861 776
Financial assets held for trading and derivatives held for hedges	19	2 581 174	2 493 535	2 921 749
Non-trading financial assets mandatorily at fair value through profit or loss, including:	20	1 221 063	1 585 029	2 035 189
Equity instruments		*148 466*	*136 480*	*87 597*
Debt securities		*81 128*	*76 068*	*133 774*
Loans and advances to customers		*991 469*	*1 372 481*	*1 813 818*
Financial assets at fair value through other comprehensive income	21	54 162 657	47 731 612	30 298 647
Financial assets at amortised cost, including:	22	114 326 977	109 527 366	100 942 738
Debt securities		*16 632 915*	*15 952 501*	*11 234 873*
Loans and advances to banks		*11 194 916*	*10 845 844*	*7 337 703*
Loans and advances to customers		*86 499 146*	*82 729 021*	*82 370 162*
Fair value changes of the hedged items in portfolio hedge of interest rate risk	19	1 055 478	-	-
Investments in subsidiaries	23	2 357 068	2 204 922	2 164 112
Non-current assets and disposal groups classified as held for sale	24	31 247	-	91 605
Intangible assets	25	1 111 479	1 013 746	823 109
Tangible assets	26	1 204 680	1 246 496	945 606
Investment properties	27	127 510	-	-
Current income tax assets		28 077	22 826	11 878
Deferred income tax assets	32	721 324	206 924	273 257
Other assets	28	857 477	773 253	491 052
TOTAL ASSETS		**191 873 819**	**170 745 007**	**148 860 718**
LIABILITIES AND EQUITY				
LIABILITIES				
Financial liabilities held for trading and derivatives held for hedges	19	2 044 601	1 414 374	987 933
Financial liabilities measured at amortised cost, including:	29	172 634 071	149 315 812	128 979 983
Amounts due to banks		*3 420 001*	*2 624 286*	*1 180 782*
Amounts due to customers		*159 905 991*	*137 778 034*	*121 936 987*
Debt securities issued		*6 683 623*	*6 335 165*	*3 361 997*
Subordinated liabilities		*2 624 456*	*2 578 327*	*2 500 217*
Fair value changes of the hedged items in portfolio hedge of interest rate risk	19	110 033	59 624	136
Liabilities classified as held for sale	24	7 425	-	-
Provisions	31	839 698	515 211	369 612
Current income tax liabilities		54 467	225 029	150 859
Deferred income tax liabilities	32	89	89	82
Other liabilities	30	2 801 612	2 747 176	2 257 106
TOTAL LIABILITIES		**178 491 996**	**154 277 315**	**132 745 711**
EQUITY				
Share capital:		**3 593 944**	**3 587 035**	**3 579 818**
Registered share capital	37	169 540	169 468	169 401
Share premium	38	3 424 404	3 417 567	3 410 417
Retained earnings:	39	**11 248 903**	**12 460 606**	**12 364 550**
- Profit from previous years		12 464 256	12 367 559	12 364 550
- Profit (loss) for the current year		(1 215 353)	93 047	-
Other components of equity	40	**(1 461 024)**	**420 051**	**170 639**
TOTAL EQUITY		**13 381 823**	**16 467 692**	**16 115 007**
TOTAL LIABILITIES AND EQUITY		**191 873 819**	**170 745 007**	**148 860 718**

Total capital ratio		**19.01**	**22.95**	**22.84**
Common Equity Tier I capital ratio		**16.23**	**19.59**	**19.42**
Book value		**13 381 823**	**16 467 692**	**16 115 007**
Number of shares		**42 384 884**	**42 367 040**	**42 350 367**
Book value per share (in PLN)		**315.72**	**388.69**	**380.52**

Notes presented on pages 10–163 constitute an integral part of these Financial Statements.

IFRS Financial Statements 2021 (PLN thousand)

STATEMENT OF CHANGES IN EQUITY

Changes from 1 January to 31 December 2021

	Share capital		Retained earnings		Other components of equity	Total
	Registered share capital	Share premium	Profit from the previous years	Loss for the current year		
Equity as at 1 January 2021	**169 468**	**3 417 567**	**12 460 606**	**-**	**420 051**	**16 467 692**
Total comprehensive income	**-**	**-**	**-**	**(1 215 353)**	**(1 881 075)**	**(3 096 428)**
Issuance of ordinary shares	72	-	-	-	-	72
Stock option program for employees	**-**	**6 837**	**3 650**	**-**	**-**	**10 487**
value of services provided by the employees	-	-	*10 487*	-	-	*10 487*
settlement of exercised options	-	*6 837*	*(6 837)*	-	-	-
Equity as at 31 December 2021	**169 540**	**3 424 404**	**12 464 256**	**(1 215 353)**	**(1 461 024)**	**13 381 823**

Changes from 1 January to 31 December 2020

	Share capital		Retained earnings		Other components of equity	Total
	Registered share capital	Share premium	Profit from the previous years	Profit for the current year		
Equity as at 1 January 2020	**169 401**	**3 410 417**	**12 364 550**	**-**	**170 639**	**16 115 007**
Total comprehensive income	**-**	**-**	**-**	**93 047**	**249 412**	**342 459**
Issuance of ordinary shares	67	-	-	-	-	67
Stock option program for employees	**-**	**7 150**	**3 009**	**-**	**-**	**10 159**
value of services provided by the employees	-	-	*10 159*	-	-	*10 159*
settlement of exercised options	-	*7 150*	*(7 150)*	-	-	-
Equity as at 31 December 2020	**169 468**	**3 417 567**	**12 367 559**	**93 047**	**420 051**	**16 467 692**

IFRS Financial Statements 2021 (PLN thousand)

STATEMENT OF CASH FLOWS

	Note	Year ended 31 December	
		2021	2020 - restated
Profit (loss) before income tax		**(680 227)**	**572 996**
Adjustments:		***10 543 736***	***(3 309 182)***
Income taxes paid		(818 904)	(413 446)
Depreciation	25,26	389 157	388 271
Foreign exchange (gains) losses related to financial activities		222 425	627 795
(Gains) losses on investing activities		(155 925)	(122 416)
Change of valuation of investment in subsidiaries not measured at equity method	23	(78)	1 643
Dividends received	7	(30 095)	(31 271)
Interest income (income statement)	5	(3 879 243)	(4 109 239)
Interest expense (income statement)	5	257 066	568 077
Interest received		4 122 518	4 869 710
Interest paid		(226 000)	(672 734)
Changes in loans and advances to banks		(279 558)	(3 584 761)
Changes in financial assets and liabilities held for trading and hedging derivatives		(1 572 774)	1 325 997
Changes in loans and advances to customers		(9 028 245)	(4 252 701)
Changes in debt securities at fair value through other comprehensive income		(2 144 622)	(13 932 407)
Changes in securities at amortised cost		(753 545)	(4 717 628)
Changes in non-trading equity securities mandatorily at fair value through profit or loss		(17 046)	8 823
Changes in other assets		45 162	(370 206)
Changes in amounts due to banks		827 197	1 651 006
Changes in amounts due to customers		23 212 050	16 056 654
Changes in issued debt securities		(62 715)	2 772 464
Changes in provisions		324 487	145 599
Changes in other liabilities		112 424	481 588
A. Cash flows from operating activities		**9 863 509**	**(2 736 186)**
Disposal of shares in subsidiaries		5 147	92 047
Disposal of intangible assets and tangible fixed assets		833	1 886
Dividends received	7	30 095	31 271
Acquisition of shares in subsidiaries	23	(17 039)	-
Purchase of intangible assets and tangible fixed assets		(436 591)	(404 034)
B. Cash flows from investing activities		**(417 555)**	**(278 830)**
Proceeds from other loans and advances	29	2 309 950	35 000
Issue of debt securities		72	67
Issue of ordinary shares		-	(196 140)
Repayments of loans advances from banks		(1 358 250)	-
Repayments of other loans and advances		(2 020 661)	(178 042)
Redemption of debt securities		-	(479 271)
Payments due to other financial liabilities		(89 901)	(111 846)
Payments due to lease agreements		(59 691)	(84 733)
C. Cash flows from financing activities		**(1 218 481)**	**(1 014 965)**
Net increase / decrease in cash and cash equivalents (A+B+C)		**8 227 473**	**(4 029 981)**
Effect of exchange rate changes in cash and cash equivalents		(9 649)	30 883
Cash and cash equivalents at the beginning of the reporting period		4 205 132	8 204 230
Cash and cash equivalents at the end of the reporting period	**42**	**12 422 956**	**4 205 132**

Notes presented on pages 10–163 constitute an integral part of these Financial Statements.

EXPLANATORY NOTES TO THE FINANCIAL STATEMENTS

1. Information regarding mBank S.A.

mBank S.A. ("Bank", "mBank") was established under the name of Bank Rozwoju Eksportu S.A. by Resolution of the Council of Ministers N 99 of 20 June 1986. The Bank was registered pursuant to the legally valid decision of the District Court for the Capital City of Warsaw, 16th Economic Registration Division, on 23 December 1986 in the Business Register under the number RHB 14036. The 9th Extraordinary Meeting of Shareholders held on 4 March 1999 adopted the resolution changing the Bank's name to BRE Bank SA. The new name of the Bank was entered in the Business Register on 23 March 1999. On 11 July 2001, the District Court in Warsaw issued the decision on the entry of the Bank in the National Court Register (KRS) under number KRS 0000025237.

On 22 November 2013, the District Court for the Capital City of Warsaw, 12th Commercial Division of the National Court Register, registered the amendments to the Bank's by-laws arising from Resolutions N°26 and Resolutions N°26 of the 27th Annual General Meeting of mBank S.A., which was held on 11 April 2013. With the registration of changes in by-laws, the name of the Bank has changed from BRE Bank Spółka Akcyjna to mBank Spółka Akcyjna (abbreviated mBank S.A.).

According to the Polish Classification of Business Activities, the business of the Bank was classified as "Other monetary intermediation" under number 6419Z. According to the Stock Exchange Quotation, the Bank is classified as "Banks" sector as part of the "Finance" macro-sector.

According to the by-laws of the Bank, the scope of its business consists of providing banking services and consulting and advisory services in financial matters, as well as of conducting business activities within the scope described in its by-laws. The Bank operates within the scope of corporate, institutional and retail banking (including private banking) throughout the whole country and operates trade and investment activities as well as brokerage activities.

The Bank provides services to Polish and international corporations and individuals, both in the local currency (Polish Zloty, PLN) and in foreign currencies.

The Bank may open and maintain accounts in Polish and foreign banks, and can possess foreign exchange assets and trade in them.

The head office of the Bank is located at 18 Prosta St. in Warsaw.

The Bank conducts retail banking business in the Czech Republic and Slovakia through its foreign mBank branches in these countries.

As at 31 December 2021, the headcount of mBank S.A. amounted to 6 075 FTEs (Full Time Equivalents) (31 December 2020: 6 034 FTEs).

As at 31 December 2020, the headcount of mBank S.A. amounted to 7 088 persons (31 December 2020: 7 065 persons).

The Management Board of mBank S.A. approved these financial statements on 1 March 2022.

2. Description of relevant accounting policies

The principal accounting policies used in the preparation of these financial statements are set forth below. These accounting policies have been applied consistently in all periods presented, except for the change in accounting policy implemented since the beginning of 2021 regarding recognition of the impact of legal risk concerning indexation clauses in mortgage and housing loans in CHF. Until the end of 2020 the Bank recognised provisions for legal proceedings in accordance with IAS 37 "Provisions, Contingent Liabilities and Contingent Assets" in relation to both active and repaid loans. In view of changes in conditions, such as the growing number of court cases and the predominantly unfavourable court judgments stating the invalidity of the contract in whole or certain provisions thereof the Bank expects that it will not obtain the full amount of contractual cash flow related to these loans. Therefore in relation to active loans the Bank revised its estimates of cash flows and adjusted the gross carrying amount of these loans in accordance with IFRS 9 "Financial Instruments" paragraph B5.4.6. as the change in expected cash flows is not related to credit risk and therefore is not recognised as expected credit losses. The recognition of the impact of legal risk related to repaid loans remained unchanged.

The Bank changed its accounting policies as allowed by IAS 8 in order to provide users of financial statements with more relevant information regarding the impact of the CHF mortgage and housing loan portfolio and related legal risk on the financial position, financial performance and cash flows of the Bank. In the Bank's opinion such approach provides better reflection of value of CHF-indexed loans in the statement of financial position. The changed approach will also allow for better comparability of financial statements across financial sector as such accounting treatment constitutes the prevailing market practice in this respect. These changes are described in Note 2.30.

2.1. Accounting basis

These Financial Statements of mBank S.A. have been prepared for the 12-month period ended 31 December 2021. Comparative data presented in these financial statements relate to the period of 12 months ended on 31 December 2020.

The Financial Statements of mBank S.A. have been prepared on a historical cost basis in compliance with the International Financial Reporting Standards (IFRS) as adopted for use in the European Union, except for derivative financial instruments, other financial assets and liabilities held for trading, financial assets failing SPPI test and financial assets and liabilities designated at fair value through profit or loss (FVTPL), debt and equity instruments at fair value through other comprehensive income (FVOCI), investment properties and liabilities related to cash-settled share-based payment transactions, all of which have been measured at fair value. Non-current assets held for sale or group of these assets classified as held for sale are stated at the lower of the carrying value and fair value less costs to sell.

The data for the year 2020 presented in these financial statements was audited by the auditor.

The preparation of the financial statements in compliance with IFRS requires the application of specific accounting estimates. It also requires the Management Board to use its own judgment when applying the accounting policies adopted by the Bank. The issues in relation to which a significant professional judgement is required, more complex issues, or such issues where estimates or judgments are material to the financial statements are disclosed in Note 4.

Financial statements are prepared in compliance with materiality principle. Material omissions or misstatements of positions of financial statements are material if they could, individually or collectively, influence the economic decisions that users make on the basis of the Bank's financial statements. Materiality depends on the size and nature of the omission or misstatement of the position of financial statements or a combination of both. The Bank presents separately each material class of similar positions. The Bank presents separately positions of dissimilar nature or function unless they are immaterial.

These financial statements were prepared under the assumption that all the entities of the Group continue as a going concern in the foreseeable future, i.e. in the period of at least 12 months following the reporting date.

The Management Board, in its assessment of the appropriateness of the going concern assumption for the Bank and the Group companies, considered, inter alia, net loss incurred by the Bank in the amount of PLN 1 215 353 thousand. This loss results from the legal risk costs recognised in 2021 related to mortgage and housing loans granted to individual customers in CHF, as described in detail in Note 34.

The profitability of core business model of the Bank and the Group remained high and stable in 2021. As at 31 December 2021 and as at the date of these financial statements, the Bank and the Group complied with all regulatory requirements, including these relating to capital adequacy and liquidity. Also recovery plan indicators in the areas of liquidity, capital and assets quality demonstrate the stable and robust situation of the Bank and the Group, as described in detail in Note 3.2.6.

Therefore, as of the date of approving these statements, the Bank Management Board has not identified any events that could indicate that the continuation of the operations by the Group is endangered in the period of at least 12 months from the reporting date.

The Bank also prepares consolidated financial statements in accordance with IFRS. mBank S.A. Group Consolidated Financial Statements for the year 2021 were approved on 1 March 2022.

2.2. Interest income and expenses

All interest income on financial instruments carried at amortised cost using the effective interest rate method, as well as interest income from financial assets measured at fair value through profit or loss and measured at fair value through other comprehensive income, are recognised in the income statement.

The effective interest rate method is a method of calculation of the amortised initial value of financial assets or financial liabilities and allocation of interest income or interest expense to the proper periods. The effective interest rate is the interest rate that exactly discounts estimated future cash payments or receipts through the expected life of the financial assets or financial liability to the gross carrying amount of a financial asset or to the amortised cost of a financial liability. When calculating the effective interest rate, the Bank estimates the expected cash flows taking into account all the contractual terms of the financial instrument, but without taking into account the expected credit losses. This calculation takes into account all the fees paid or received between the parties to the contract, which constitute an integral component of the effective interest rate, as well as transaction expenses and any other premiums or discounts.

The Bank calculates interest income using the effective interest rate on the gross carrying amount of the financial asset except for the financial assets which subsequently have become credit-impaired. In case of reclassification of a financial asset or a group of similar financial assets to Stage 3, the interest income is calculated on the amortised cost (i.e. the gross carrying amount adjusted for the loss allowance) and recognised using the interest rate at which the future cash flows were discounted for the purpose of valuation of impairment.

Interest income includes interest and commissions received or due on account of loans, inter-bank deposits or investment securities recognised in the calculation of the effective interest rate.

Interest income, including interest on loans, is recognised in the income statement and on the other side in the statement of financial position as part of receivables from banks or from other customers.

The calculation of the effective interest rate takes into account the cash flows resulting from the hybrid contract as a whole containing a host that is an asset within the scope of IFRS 9.

Amounts calculated with the use of negative interest rates are qualified accordingly to interest income in case when they relate to financial liabilities, and to interest expenses when they relate to financial assets.

Income and expenses related to the interest component of the result on interest rate derivatives and resulting from current calculation of swap points on currency derivatives classified into banking book are presented in the interest results in the position Interest income/expense on derivatives classified into banking book. The banking book includes transactions, which are not concluded for trading purposes i.e. not aimed at generating a profit in a short-term period (up to 6 months) and those that do not constitute hedging a risk arising from the operations assigned into trading 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 interest result in the position Interest income/expense on derivatives under the fair value hedge.

Interest income related to the interest measurement component of derivatives concluded as hedging instruments under cash flow hedge are presented in the interest result in the position Interest income on derivatives under the cash flow hedge.

2.3. Fee and commission income

Fee and commission income is recognised in accordance with IFRS 15 using a 5-step model for revenue recognition, which consists of:

<u>Step 1: Identifying the contract with a customer</u>

The Bank accounts for a contract with a customer that is within the scope of this Standard only when all of the following criteria are met:

1. the parties to the contract have approved the contract (in writing, orally or in accordance with business practices) and are committed to perform their respective obligations;
2. the Bank can identify each party's rights regarding the goods or services to be transferred;
3. the Bank can identify the payment terms for the goods or services to be transferred;
4. the contract has commercial substance (i.e. the risk, timing or amount of the entity's future cash flows is expected to change as a result of the contract); and
5. it is probable that the Bank will collect the consideration to which it will be entitled in exchange for the goods or services that will be transferred to the customer. In evaluating whether collectability of an amount of consideration is probable, the Bank considers only the customer's ability and intention to pay that amount of consideration when it is due. The amount of consideration to which the entity will be entitled may be less than the price stated in the contract if the consideration is variable because the Bank may offer the customer a price discount.

<u>Step 2: Identifying performance obligations in the contract</u>

The performance obligation is a promise (presumed or specified) to provide the client with goods or services that are identified at the time of entering into the contract on the basis of contractual terms as well as the Bank's business practice.

At contract inception, the Bank assesses the goods or services promised in a contract with a customer and identifies as a performance obligation each promise to transfer to the customer either:

1. a good or service (or a bundle of goods or services) that is distinct; or
2. a series of distinct goods or services that are substantially the same and that have the same pattern of transfer to the customer.

A good or service that is promised to a customer is distinct if both of the following criteria are met:

1. the customer can benefit from the good or service either on its own or together with other resources that are readily available to the customer (i.e. the good or service is capable of being distinct); and
2. the Bank's promise to transfer the good or service to the customer is separately identifiable from other promises in the contract (i.e. the good or service is distinct within the context of the contract).

The Bank identifies options for purchasing additional goods or services for the customer (loyalty points) as separate obligations to provide benefits, if they give the customer relevant rights (material law, which the client would not have obtained if he did not conclude the contract).

If a third party is involved in the process of providing selected services for the client, the Bank assesses whether it acts as an agent or principal, taking into account in particular the possibility of controlling the given service before it is passed on to the client (control principle).

Step 3: Determining the transaction price

The transaction price reflects the amount of consideration that the Bank expects to be entitled to in exchange for distinct good or service transferred as provided by the terms of the contract and the Bank's business practice.

The transaction price is the amount of remuneration which, in line with the Group's expectations, will be due in exchange for transfer of promised goods or services to the client, excluding amounts collected on behalf of third parties.

Determining the transaction price can become complex where a contract includes any of the following: variable consideration, a significant financing component, non-cash consideration, consideration payable to a customer. In terms of variable remuneration (e.g. rebates from payment organizations), the Bank estimates the amount of remuneration to which it will be entitled in exchange for the transfer of promised services.

Step 4: Allocating the transaction price to the performance obligations

The transaction price is allocated to each separate performance obligation, or distinct good or service, so that revenue is recorded at an amount that depicts the amount of consideration that the Bank expects to be entitled to in exchange for transferring the promised goods or services. The transaction price is allocated to each performance obligation based on the relative fair value model.

Step 5: Recognition of revenue when (or as) the Bank satisfies a performance obligation

The Bank recognises revenue when (or as) it satisfies a performing obligation by transferring a promised good or service to a customer (which is when the customer obtains control of that good or service). The Bank recognises at a point in time the fees charged at a point in time not related directly to origination of loans and advances. Fees for services delivered over time longer than 3 months are recognised by the Bank over time. As the fee and commission income, the Bank treats also fees and commissions recognised over time on a straight line basis, related to loans and advances with not established timing of cash flows, for which effective interest rate is not possible to be determined. Straight line method for those services presents fairly the timing of transfer of services, because they are delivered evenly over time.

Accounting principles related to recognition of fee income from sale of assurance products bundled with loans and advances are described under Note 2.4.

Fees charged for granting of loans which are likely to be drawn down are deferred (together with the related direct costs) and included in the calculation of the effective interest rate charge on the loan. Fees on account of syndicated loans are recognised as income at the time of closing of the process of organisation of the respective syndicate, if the Bank has not retained any part of the credit risk on its own account or has retained a part of the risk of a similar level as other participants. Commissions and fees on account of negotiation or participation in the negotiation of a transaction on behalf of a third party, such as the acquisition of shares or other securities, or the acquisition or disposal of an enterprise, are recognised at the time of realisation of the transaction. Portfolio management fees and other fees for management, advisory and other services are recognised on the basis of service contracts, usually in proportion to the passage of time. The same principle is applied in the case of management of client assets, financial planning and custody services, which are continuously provided over an extended period of time.

Fees and commissions collected by the Bank on account of issuance, renewal and change in the limit of credit and payment cards, guarantees granted as well as opening, extension and increase of letters of credit are accounted for on a straight-line basis.

Fees and commissions collected by the Bank on account of cash management operations, keeping of customer accounts, money transfers and brokerage business activities are recognised directly in the income statement as one-off.

In addition, fee and commission income include revenue from a fee on instalment payment for premium on insurance products sold through the Internet platform. The fee on instalment payment is settled in time in accordance with the duration of the policy.

The Bank's fee and commission income comprises also income from offering insurance products of third parties. In case of selling insurance products that are not bundled with loans, the revenues are recognised as upfront income or in majority of cases settled on a monthly basis.

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

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

Revenue and expenses from sale of insurance products bundled with loans are split into interest income and fee and commission income based on the relative fair value analysis of each of these products.

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 deferred over time based on the analysis of the stage of completion of the service, in accordance with 5-step model described above.

Expenses directly linked to the sale of insurance products are recognised using the same pattern as in the case of income observing the matching concept. 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.

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 connection with entry into force of Recommendation U concerning best practices in the area of bancassurance, starting from 31 March 2015 the Bank does not receive remuneration from the sale of insurance products which would have been treated as bundled with loans.

2.5. Financial assets

The Bank classifies its financial assets to the following categories: financial assets valued at fair value through profit or loss, financial assets valued at fair value through other comprehensive income for which gains or losses may be reclassified subsequently to the income statement at derecognition, financial assets valued at fair value through other comprehensive income for which gains or losses will not be reclassified subsequently to the income statement at derecognition and financial assets valued at amortised cost. Classification of the debt financial asset to the one of the above categories takes place at its initial recognition based on business model for managing financial assets and contractual cash flow characteristics. An equity instrument is classified as a financial asset at fair value through profit or loss unless at the time of initial recognition the Bank made an irrevocable election of specific equity investments to present subsequent fair value changes in other comprehensive income.

Standardised purchases and sales of financial assets at fair value through profit or loss and measured at fair value through other comprehensive income are recognised on the settlement date – the date on which the Bank delivers or receives the asset. Changes in fair value in the period between trade and settlement date with respect to assets carried at fair value are recognised in profit or loss or in other components of equity. Loans are recognised when the funds are disbursed or made available to the borrower's account. Derivative financial instruments are recognised beginning from the date of transaction.

Derecognition of financial asset is when and only when the contractual rights to the cash flows from the financial assets expire, when the Bank transfers the financial asset and the transfer qualifies for derecognition or in case of a substantial modification of financial asset.

Financial assets measured at fair value through profit or loss

A financial asset shall be measured at fair value through profit or loss unless it is measured at amortised cost or at fair value through other comprehensive income.

Disposals of debt and equity securities held for trading are accounted according to the weighted average method.

The Bank may, at the initial recognition, irrevocably designate a financial asset at fair value through profit or loss when doing so results in more relevant information, because it eliminates or significantly reduces a measurement or recognition inconsistency (sometimes referred to as "an accounting mismatch") that would otherwise arise from measuring assets or liabilities or recognising the gains and losses on them on different bases.

As presented in this financial statements reporting periods, the Bank did not designate any financial instrument on initial recognition as financial assets at fair value through profit or loss to reduce an accounting mismatch.

Financial assets classified to this category are valued at fair value upon initial recognition.

After initial recognition, financial assets classified in this category are measured at the end of the reporting period at fair value.

Gains and losses arising from changes in the fair value of financial assets at fair value through profit or loss are recognised in the income statement in the period in which they arise.

Interest income on financial assets measured at fair value through profit or loss (Note 2.2), except for derivatives the recognition of which is discussed in Note 2.11, is recognised in net interest income. The valuation and result on disposal of financial assets measured at fair value through profit or loss is recognised in trading income for financial assets held for trading or in gains or losses on non-trading financial assets mandatorily at fair value through profit or loss.

Financial assets measured at amortised cost

Financial assets measured at amortised cost are assets that meet both of the following conditions, unless the Bank designated them to fair value through profit or loss: the financial asset is held within a business model whose objective is to hold financial assets in order to collect contractual cash flows and contractual terms of the financial asset give rise on specified dates to cash flows that are solely payments of principal and interest on the principal amount outstanding Financial assets at amortised cost are entered into books on the transaction date.

At initial recognition financial assets classified to this category are valued at fair value plus transaction costs that are directly attributable to the acquisition of the financial asset. After initial recognition, these assets are measured at amortised cost using the effective interest rate.

Financial assets measured at fair value through other comprehensive income

Financial assets measured at fair value through other comprehensive income are assets that meet both of the following conditions, unless the Bank designated them to fair value through profit or loss: the financial asset is held within a business model whose objective is achieved by both collecting contractual cash flows as well as selling financial assets and contractual terms of the financial asset give rise on specified dates to cash flows that are solely payments of principal and interest on the principal amount outstanding.

Interest income and expense from financial assets measured at fair value through other comprehensive income are presented in net interest income. Gains and losses from sale of financial assets measured at fair value through other comprehensive income are presented in gains less losses from derecognition of financial assets and liabilities not measured at fair value through profit or loss.

Financial assets measured at fair value through other comprehensive income and financial assets measured at fair value through profit or loss are valued at the end of the reporting period according to their fair value.

Gains and losses arising from changes in the fair value of debt financial assets measured at fair value through other comprehensive income are recognised in other comprehensive income until the derecognition of the respective financial asset in the statement of financial position: at such time the aggregate net gain or loss previously recognised in other comprehensive income is now recognised in the income statement. However, interest calculated using the effective interest rate is recognised in the income statement.

The fair value of quoted investments in active markets is based on current market prices. If the market for a given financial asset is not an active one, the Bank determines the fair value by applying valuation techniques. These comprise recently conducted transactions concluded according to normal market principles, reference to other instruments, discounted cash flow analysis, as well as valuation models for options and other valuation methods generally applied by market participants.

Equity instruments

Investments in equity instruments are measured at fair value through profit or loss. Upon initial recognition, the Bank may make an irrevocable election to present in other comprehensive income subsequent changes in the fair value (the option of measurement at fair value through other comprehensive income) of an investment in an equity instrument that is not held for trading and does not constitute a contingent payment recognised by the Bank as part of a business combination in accordance with IFRS 3.

In the case of the financial instruments for which the option of measurement at fair value through other comprehensive income was used all gains and losses related to change in fair value, including foreign exchange differences, are recognised in other comprehensive income. There is no possibility to reclassify them to income statement even if the instrument is derecognised. Only dividends received related to these instruments are recognised in income statement when the entity’s right to receive payment is established.

Modification of contractual terms for financial assets

The Bank settles previously recognised financial assets and re-recognises the financial assets in accordance with the requirements for initial recognition in case of substantial modification of contractual terms of financial assets. The Bank defines modification as substantial when it meets one of the following criteria:

- increase of the credit amount of more than 10%,
- prolongation of the contractual maturity of more than 12 months,
- change of currency not provided for in the terms of the contract. Change of the currency provided for in the terms of the agreement is such a change that defines both the FX rate at which it would have place and the interest rate of the loan after the change of the currency,
- change of the borrower – only if the current borrower is exempted from the debt,
- change of the cash flow criterion from 'SPPI compliance' of a financial assets to 'SPPI non-compliance' and vice versa,
- change of the financed asset in case of object finance or project finance,
- change of the legal form/ type of financial instrument.

In the event of substantial modification the deferred income and expense related to such asset is recognised in the income statement and the provision is released. At the same time there is re-recognition of financial assets in accordance with the requirements for initial recognition. Any other modifications of contractual terms that do not cause derecognition of financial assets are treated as non-substantial modifications and the gain or loss on modification is recognised. The effect of all identified non-substantial modifications of cash flows are treated as not related to credit risk and are recognised in net interest income. The result on modification is the difference between present value of the modified cash flows discounted using the old effective interest rate and the effective loan exposure. Commissions received related to minor modification are settled over time using effective interest rate. All identified substantial modifications of cash flows are treated as related to credit risk. In case of substantial modification in Stage 2, for which as a consequence, the exposure was moved to Stage 1, the adjustment to fair value of the exposure at the initial recognition, adjusts the interest result in the subsequent periods.

In the case of contract terms' modification as a result of a market-wide reform of interest rate benchmark, including the replacement of the interest rate benchmark with an alternative benchmark, when:

- the basis for determining contractual cash flows has changed in the contract and the new basis is considered economically equivalent to the old basis, such change is recognised through a change in the effective interest rate;
- changes concern other areas, or have not been considered economically equivalent, such changes are recognised on general principles, in particular they are evaluated for a substantial modification.

Purchased or originated credit impaired financial assets (POCI assets)

POCI are financial assets measured at amortised cost that at initial recognition are credit impaired. POCI are also financial assets that are credit impaired at the moment of substantial modification. At the initial recognition POCI assets are recognised at fair value. The fair value of POCI assets at the initial recognition is calculated as present value of estimated future cash flows including credit risk discounted for the risk free rate. After the initial recognition POCI assets are measured at amortised cost. With respect to these financial assets the Bank uses credit adjusted effective interest rate in order to determine the amortised cost of financial asset and the interest income generated by these assets – CEIR. In case of POCI exposures the change of the expected credit losses relative to the estimated credit losses at the date of their initial recognition is recognised as an impairment loss. Its value can both reduce the gross value of POCI exposure and increase it in the event of a decrease of expected losses relative to its value at the date of initial recognition.

Reclassification of financial assets

Debt financial assets are reclassified when, and only when, the Bank changes its business model for managing financial assets. In such a case the assets affected by the change of business model are subject to reclassification.

Financial liabilities are not subject to reclassification by the Bank.

2.6. Offsetting of financial instruments

Financial assets and financial liabilities are offset and the net amount is reported in the statement of financial position when there is a legally enforceable right to offset the recognised amounts and there is an intention to settle on a net basis, or realise the asset and settle the liability simultaneously. The conditions mentioned above are not satisfied and offsetting is inappropriate when: different financial instruments are used to emulate the features of a single financial instrument, financial assets and liabilities arise from financial instruments having the same risk exposure but involve different counterparties, financial or other assets are pledged as collaterals for non-recourse financial liabilities, financial assets are set aside in trust by a debtor for the purpose of discharging an obligation without those assets having been accepted by the creditor in the settlement of the obligation, or obligations incurred as a result of events giving rise to losses are expected to be recovered from a third party by virtue of a claim made under an insurance contract.

2.7. Impairment of financial assets

Financial instruments subject to estimation of expected credit losses are: financial assets measured at amortised cost, financial assets measured at fair value through other comprehensive income, loan commitments if not measured at fair value through profit or loss, financial guarantee contracts if not measured at fair value through profit or loss, leases under IFRS 16, contract assets under IFRS 15.

A detailed description of issues regarding the principles of estimation of expected credit losses is presented in Note 3.3.6.

How exposures are classified to Stages

The Transfer Logic is an algorithm used to classify exposures to one of the four Stages: 1, 2, 3, POCI.

- Stage 1 includes exposures for which expected credit losses are calculated on a 12-month basis.
- Stage 2 contains exposures for which, as at the reporting date, a significant deterioration in credit quality was identified compared to the date of their initial recognition – expected credit losses are calculated over a lifetime period.
- Stage 3 contains exposures identified as credit-impaired.
- Stage POCI contains assets identified as credit-impaired at initial recognition.

A detailed description of issues regarding the principles of classification of exposures to stages is presented in Note 3.3.6.1.

Significant deterioration in credit quality

A significant deterioration in credit quality is recognised for the asset concerned on the basis of quantitative and qualitative criteria, with the asset being transferred to Stage 2 once at least one of such qualitative or quantitative criteria is met.

Rebuttable presumption

The Bank's approach that involves rejection of the presumption that a significant deterioration in credit quality occurs where DPD≥31 days (rebuttable presumption) involves introducing thresholds of materiality (thresholds of activation) for any outstanding amount payable to the Bank. The DPD≥31 days criterion (one of the qualitative criteria of the Transfer Logic) is not taken into account if at least one of the following conditions is not met:

1. the past due exposure amount exceeds PLN 400 for retail exposures in Polish branch and exposures of Private Banking debtors, registered in corporate systems, CZK 2,500 for retail exposures in the foreign branch of the Bank in Czech Republic, EUR 100 for retail exposures in the foreign branch of the Bank in Slovakia and PLN 2,000 for exposures in the area of corporate and investment banking,
2. the ratio of the past due exposure amount to the total balance sheet exposure amount exceeds 1%.

A detailed description of issues regarding the significant deterioration in credit quality is presented in Note 3.3.6.1.1.

Low credit risk

According to the IFRS 9, the Bank distinguishes a category of assets with low credit risk (ang. Low Credit Risk, LCR). Assets marked as LCR are not subject to the process of identifying indications of significant deterioration of credit quality (if they are not in the default status, they are in Stage 1).

A detailed description of issues regarding the low credit risk criteria is presented in Note 3.3.6.1.2.

Impairment

The Bank applies a common default definition in all areas of credit risk management, including for the purpose of calculating expected credit losses and capital requirement. The basis for the adopted definition of default is the definition of default in the Regulation (EU) No 575/2013 of the European Parliament and of the Council of 26 June 2013 on prudential requirements for credit institutions and investment firms and amending regulation (EU) No 648/2012 ("CRR Regulation").

The customer is reclassified to the default category in case of loss event occurrence. Reclassification of at least one customer credit liability to the default category reclassifies all credit and non-credit liabilities of the customer to the default category.

A detailed description of issues regarding loss events is presented in Note 3.3.6.1.3 (corporate) and 3.3.6.1.4 (retail).

Estimating expected credit losses (ECL)

An expected loss is measured for non-zero exposures that are active at the reporting date (balance sheet and off-balance sheet). An expected credit loss is estimated separately for on and off-balance-sheet exposures. The calculation of expected credit losses uses:

- portfolio approach: concerning exposures for which no loss event was identified at the reporting date and exposures from the retail portfolio with identified loss event (excluding exposures for which an individual approach is used),
- individual approach: concerning all corporate exposures and all Private Banking customer exposures registered in corporate systems for which a loss event was identified, as well as in specific cases of retail micro company exposures for which a loss event was identified.

A detailed description of issues regarding expected credit losses estimation is presented in Note 3.3.6.2.

Loan receivable write-off

Loan receivable write-off can be partial (corporate banking) or total. In case of retail banking, writing off receivables can be done when:

1. Debt recovery procedure is not possible due to e.g.:
   a. the claim limitation,
   b. fraud – inability to identify the debtor,
   c. limitation of inheritors' liability,
   d. the claim was questioned by the debtor in court.
2. Debt is irrevocable e.g.:
   a. the enforcement proceedings have been completed and the whole debt was not recovered - then the unrecovered portion is written off,
   b. bankruptcy proceeding has been rejected or has been completed due to debtor's lack of liquidation assets to cover the costs of the proceedings,
   c. the conclusion is that a claim is irrevocable – costs of recovery are higher than recovered claim,
   d. limitation of heirs' liability for inheritance debts.

Cases that meet these criteria may also be included in the process of debt portfolio sale.

In the case of corporate portfolio, writing off receivables is carried out when all recovery options are exhausted. This happens when:

1. all options to recover the debt have been exercised:
   a. bankruptcy proceedings ended, the debtor was removed from the National Court Register and the debt was not recovered in whole,
   b. bankruptcy proceedings were discontinued on account of the debtor having no assets to cover the costs of the proceedings or having only enough assets to cover these costs,
   c. petition for bankruptcy was dismissed on account of the debtor having insufficient assets to cover the costs of the proceedings,
   d. during judicial restructuring proceedings the terms and conditions of an arrangement assuming partial cancellation of the debt were approved,
   e. enforcement proceedings were considered ineffective and discontinued on account of the debtor having no assets,
   f. the debt was considered irrecoverable as the costs of recovering it exceed the potential proceeds;

2. it is impossible to pursue the debt, e.g.:
   a. the debtor challenges the debt in court. The debt is cancelled by a court decision,
   b. the statute of limitations on the Bank's claim.

2.8. Financial guarantee contracts

The financial guarantee contract is a contract that requires the issuer to make specified payments to reimburse the holder for a loss it incurs because a specified debtor fails to make payment when due in accordance with the original or modified terms of a debt instrument.

When a financial guarantee contract is recognised initially, it is measured at the fair value. After initial recognition, an issuer of such a contract subsequently measures it at the higher of:

- the amount of the loss allowance determined in accordance with IFRS 9, the methodology is described in Note 3.3.6 Calculating expecting credit,
- the amount initially recognised less when appropriate, the cumulative amount of income recognised in accordance with the principles of IFRS 15.

2.9. Cash and cash equivalents

Cash and cash equivalents comprise items with maturities of up to three months from the date of their acquisition, including: cash in hand and cash held at the Central Bank with unlimited availability for disposal, treasury bills and other eligible bills, amounts due from other banks.

2.10. Sell and repurchase agreements

Repo and reverse-repo transactions are defined as selling and purchasing securities for which a commitment has been made to repurchase or resell them at a contractual date and for a specified contractual price and are recognised when the money is transferred.

Securities sold with a repurchase clause (repos or sell/buy back) are reclassified in the financial statements as pledged assets if the entity receiving them has the contractual or customary right to sell or pledge them as collateral security. The liability towards the counterparty is recognised as amounts due to other banks, deposits from other banks, other deposits or amounts due to customers, depending on its nature. Securities purchased together with a resale clause (reverse repos or buy/sell back) are recognised as loans and advances to other banks or other customers, depending on their nature. For assets subject to repurchase agreements, the Bank is exposed to the same risks as those associated with holding identical assets not subject to repurchase agreements.

When concluding a repo or sell/buy back or reverse repo or buy/sell back transaction, mBank sells or buys securities with a repurchase or resale clause specifying a contractual date and price. Such transactions are presented in the statement of financial position as financial assets measured at fair value through profit or loss or at fair value through other comprehensive income, and also as liabilities in the case of repo or sell/buy back transactions and as receivables in the case of reverse repo or buy/sell back transactions measured at amortised cost.

Securities borrowed by the Bank under buy/sell back transactions are not recognised in the financial statements, unless they are sold to third parties. In such case the purchase and sale transactions are recorded in the financial statements with a gain or a loss included in trading income. The obligation to return them is recorded at fair value as amounts due to customers. Securities borrowed under buy/sell back transactions and then lent under sell/buy back transactions are not recognised as financial assets.

As a result of repo or sell/buy back transactions concluded on securities held by the Bank, financial assets are transferred in such way that they do not qualify for derecognition. Thus, the Bank retains substantially all risks and rewards of ownership of the financial assets.

2.11. Derivative financial instruments and hedge accounting

Derivative financial instruments are recognised at fair value from the date of transaction. Fair value is determined based on prices of instruments listed on active markets, including recent market transactions, and on the basis of valuation techniques, including models based on discounted cash flows and options pricing models, depending on which method is appropriate in the particular case. All derivative instruments with a positive fair value are recognised in the statement of financial position as assets, those with a negative value as liabilities.

The best fair value indicator for a derivative instrument at the time of its initial recognition is the price of the transaction (i.e., the fair value of the paid or received consideration). If the fair value of the particular instrument may be determined by comparison with other current market transactions concerning the same instrument (not modified) or relying on valuation techniques based exclusively on market data that are available for observation, then the Bank recognises the respective gains or losses from the first day in accordance with the principles described under Note 2.12.

Derivative instrument embedded in the hybrid contract, the host of which is a financial asset within the scope of IFRS 9, is not separated and the hybrid contract is recognised in accordance with the requirements for classification of the financial assets.

Derivative instrument embedded in the hybrid contract, the host of which is not a financial asset within the scope of IFRS 9, is assessed for the need to separate it.

Derivative instruments, which are designated and constitute effective hedging instruments, are not classified under any of the categories specified above and are subject to the principles of hedge accounting.

In accordance with IFRS 9: (i) there is no need to separate the prepayment option from the host debt instrument for the needs of financial statements, if the option's exercise price is approximately equal on each exercise date to the amortised cost of the host debt instrument. If the prepayment option does not meet the contractual cash flow characteristic test, then the financial asset as a whole shall be classified as a financial asset measured at fair value through profit or loss; (ii) exercise price of a prepayment option reimburses the lender for an amount up to the approximate present value of lost interest for the remaining term of the host contract. Lost interest is the product of the principal amount prepaid multiplied by the interest rate differential. The interest rate differential is the excess of the effective interest rate of the host contract over the effective interest rate the entity would receive at the prepayment date if it reinvested the principal amount prepaid in a similar contract for the remaining term of the host contract.

The assessment of whether the call or put option is closely related to the host debt contract is made before separating the equity element of a host debt instrument in accordance with IAS 32.

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 either as (1) fair value hedges against a recognised asset or liability or against a binding contractual obligation (fair value hedge), or as (2) hedges against highly probable future cash flows attributable to a recognised asset or liability, or a forecasted transaction (cash flow hedge).

The Bank decided that it would continue to apply the hedge accounting requirements in accordance with IAS 39, instead of the requirements set forth in IFRS 9.

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:

- 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 shall include 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 or cash flows attributable to the hedged risk;
- the hedge is expected to be highly effective in offsetting changes in fair value or cash flows attributable to the hedged risk, consistently with the originally documented risk management strategy for that particular hedging relationship;
- for cash flow hedges, a forecast transaction that is the subject of the hedge must be highly probable and must present an exposure to variations in cash flows that could ultimately affect profit or loss;
- the effectiveness of the hedge can be reliably measured, i.e. the fair value or cash flows of the hedged item that are 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 actually 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 and cash flow 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.

Due to the split of derivatives classified into banking book and into trading book, the Bank applies a different approach to the presentation of interest income/expense for each of these groups of derivatives that is described in Note 2.2. The remaining result from fair value measurement of derivatives is recognised in "Net trading income".

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 asset or liability that are attributable to the hedged risk. Hedging gain or loss on the hedged item adjusts the carrying amount of the hedged item.

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 method is used is amortised to the income statement over the period to maturity. The adjustment to the carrying amount of the hedged equity security remains in other comprehensive income until the disposal of the equity security.

Cash flow hedges

The effective part of the fair value changes of derivative instruments designated and qualifying as cash flow hedges is recognised in other comprehensive income. The gain or loss concerning the ineffective part is recognised in the income statement of the current period.

The amounts recognised in other comprehensive income are transferred to the income statement and recognised as income or cost of the same period in which the hedged item will affect the income statement (e.g., at the time when the forecast sale that is hedged takes place).

In case the hedging instrument has expired or has been sold, or the hedge has ceased to fulfil the criteria of hedge accounting, any aggregate gains or losses recognised at such time in other comprehensive income remain in other comprehensive income until the time of recognition in the income statement of the forecast transaction. When a forecast transaction is no longer expected to occur, the aggregate gains or losses recorded in other comprehensive income are immediately transferred to the income statement.

Derivative instruments not designated to the hedge accounting

Changes of the fair value of derivative instruments that are not designated to hedge accounting are recognised in the income statement of the current period.

The Bank holds the following derivative instruments in its portfolio:

Market risk instruments:

- Futures contracts for bonds, index futures
- Options for securities and for stock-market indices
- Options for futures contracts
- Forward transactions for securities
- Commodity swaps

Interest rate risk instruments:

- Forward Rate Agreement (FRA)
- Interest Rate Swap (IRS), Overnight Index Swap (OIS)
- Interest Rate Options

Foreign exchange risk instruments:

- Currency forwards, FX swap, FX forward
- Cross Currency Interest Rate Swap (CIRS)
- Currency options.

2.12. Gains and losses on initial recognition

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

The transaction for which the fair value determined using a valuation model (where inputs are both observable and non-observable data) and the transaction price differ, the initial recognition is at the transaction price. The Bank assumes that the transaction price is the best indicator of fair value, although the value obtained from the valuation model may differ. The difference between the transaction price and the model value, commonly referred to as “day one profit or loss”, is amortised over the period of time.

The timing of recognition of deferred day one profit or loss is determined individually. It is either amortised over the life of the transaction, deferred until the instrument’s fair value can be determined using market observable data, or realised through settlement. The financial instrument is subsequently measured at fair value, adjusted for the deferred day one profit or loss. Subsequent changes in fair value are recognised immediately in the income statement without reversal of deferred day one profits and losses.

2.13. Financial liabilities measured at amortised cost

Financial liabilities measured at amortised cost include borrowings, deposits taken, debt securities issued and subordinated liabilities. These liabilities are initially recognised at fair value reduced by the incurred transaction costs. After the initial recognition, these liabilities are recorded at adjusted cost of acquisition (amortised cost using the effective interest method). Any differences between the amount received (reduced by transaction costs) and the redemption value are recognised in the income statement over the period of duration of the respective agreements according to the effective interest rate method.

2.14. Investments in subsidiaries

Investments in subsidiaries in the stand-alone financial statements are initially recognised at cost, and then measured using the equity method, whereby the carrying amount of investments in subsidiaries is increased or decreased in order to recognise the Bank's shares in the profit or loss of the subsidiary recorded after the date of acquisition. The Bank's share in the profit or loss of the subsidiary is recognised in the income statement under the item Share in profits (losses) of entities under the equity method. Received dividends reduce the carrying amount of the investment and are recognised under Dividend income. The Bank's share in other comprehensive income of the subsidiary the Bank recognises in other comprehensive income of the Bank. Unrealized gains or losses on transactions with subsidiaries accounted for using the equity method (including, for example, expected credit losses recognised in relation to loans or guarantees granted) are eliminated. Balance sheet balances such as receivables and liabilities or deposits and loans granted to subsidiaries are not eliminated in the stand-alone financial statements. If the Bank's share of losses exceeds the value of shares in a subsidiary, the Bank ceases to recognise its share of further losses. At the balance sheet date the Bank assesses whether there are any triggers indicating impairment of investments made in a subsidiary.

2.15. Intangible assets

The Bank measures intangible assets initially at cost. After initial recognition, intangible assets are recognised at their cost of acquisition adjusted by the costs of improvement (rearrangement, development, reconstruction or modernisation) less any accumulated amortization and any accumulated impairment losses. Amortization is accrued by the straight line method taking into account the expected period of economic useful life of the respective intangible assets.

Computer software

Purchased computer software licences are capitalised in the amount of costs incurred for the purchase and adaptation for use of specific computer software. These costs are amortised on the basis of the expected useful life of the software (1.5-18 years). Expenses attached to the maintenance of computer software are expensed when incurred. Expenses directly linked to the development of identifiable and unique proprietary computer programmes controlled by the Bank, which are likely to generate economic benefits in excess of such costs expected to be gained over a period exceeding one year, are recognised as intangible assets. Direct costs comprise personnel expenses directly related to the software.

Capitalised costs attached to the development of software are amortised over the period of their estimated useful life (1.5-30 years).

Computer software directly connected with the functioning of specific information technology hardware is recognised as “Tangible fixed assets”.

Intangible assets are tested in terms of possible impairment always after the occurrence of events or change of circumstances indicating that their carrying value in the statement of financial position might not be possible to be recovered.

2.16. Tangible fixed assets

Tangible fixed assets are carried at historical cost reduced by accumulated depreciation and accumulated impairment losses. Historical cost takes into account the expenses directly attached to the acquisition of the respective assets.

Subsequent costs are included in the asset’s carrying amount or are recognised as a separate asset, as appropriate, only where it is probable that future economic benefits associated with the item will flow to the Bank and the cost of the item can be measured reliably. Any other expenses incurred on repairs and maintenance are expensed to the income statement in the reporting period in which they were incurred.

Land is not depreciated. Depreciation of other fixed assets is accounted for according to the straight line method in order to spread their initial value reduced by the residual value over the period of their useful life which is estimated as follows for the particular categories of fixed assets:

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Buildings and structures	20-40 years,
Equipment	2-15 years,
Vehicles	4-5 years,
Information technology hardware	2-10 years,
Leasehold improvements	5-20 years, no longer than the period of the lease contract,
Office equipment, furniture	2-10 years.

Land and buildings consist mainly of branch outlets and offices. Residual values estimated useful life periods and depreciation method are verified at the end of the reporting period and adjusted prospectively in accordance with the arising need.

Bank assesses at the end of each reporting period whether there is any indication that tangible asset may be impaired. If any such indication exists, the Bank estimates the recoverable amount of the asset. Depreciable fixed assets are tested for impairment always whenever events or changes in circumstances indicate that the carrying value may not be recoverable. The value of a fixed asset carried in the statement of financial position is reduced to the level of its recoverable value if the carrying value in the statement of financial position exceeds the estimated recoverable amount. The recoverable value is the higher of two amounts: the fair value of the fixed asset reduced by its selling costs and the value in use.

If it is not possible to estimate the recoverable amount of the individual asset, the Bank shall determine the recoverable amount of the cash-generating unit to which the asset belongs (cash-generating unit of the asset).

The carrying amount of tangible fixed assets is derecognised on disposal or when no future economic benefits are expected from its use or disposal. The gain or loss arising from the derecognition of tangible fixed assets are included in profit or loss when the item is derecognised.

Gains and losses on account of the disposal of fixed assets are determined by comparing the proceeds from their sale against their carrying value in the statement of financial position and they are recognised in the income statement.

2.17. Investment properties

Investment properties are defined as land and buildings held for the purpose of earning rental income or because they are expected to increase in value. Investment property also includes right-of-use assets that meet the definition of investment property under IAS 40. On initial recognition investment properties are measured at cost including directly attributable transaction costs.

In subsequent measurements, investment properties are measured at fair value. The fair value of a right-of-use that meets the definition of investment property excludes the value of expected cash outflows from lease payments, which are presented separately in the Bank's statement of financial position as a lease liability in accordance with IFRS 16.

Current income and expenses are recognised in other operating income or expenses. Remeasurement changes arising from changes in fair value are also shown under other operating income or expenses in the income statement for the period. As at the date of reclassification of the property occupied by the Bank to investment property, the difference between the carrying amount of the property determined in accordance with IAS 16 or IFRS 16 and its fair value is recognised by the Bank (i) in the profit or loss account in the event of a decrease in the carrying amount or reversal of a previously recognised impairment loss on this property, or (ii) in other comprehensive income, in the event of an increase in the current value above the amount of the reversed impairment loss. On subsequent disposal of the investment property, the revaluation reserve in other comprehensive income is transferred to retained earnings. The transfer from other comprehensive income to retained earnings is not made through the income statement.

2.18. Non-current assets held for sale and discontinued operations

The Bank classifies a non-current asset (or disposal group) as held for sale if its carrying amount will be recovered principally through a sale transaction rather than through continuing use. For this to be the case, the asset (or group) must be available for immediate sale in its present condition subject only to terms that are usual and customary for sale of such assets and its sale must be highly probable, i.e., the appropriate level of management must be committed to a plan to sell the asset, and an active programme to locate a buyer and complete the plan must have been initiated. Further, the asset must be actively marketed for sale at a price that is reasonable in relation to its current fair value. In addition, the sale should be expected to qualify for recognition as a completed sale within one year from the date of classification.

Non-current assets held for sale are priced at the lower of: carrying value and fair value less costs to sell. Assets classified in this category are not depreciated.

When criteria for classification to non-current assets held for sale are not met, the Bank ceases to classify the assets as held for sale and reclassifies them into appropriate category of assets. The Bank measures a non-current asset that ceases to be classified as held for sale (or ceases to be included in a disposal group classified as held for sale) at the lower of:

- its carrying amount at a date before the asset (or disposal group) was classified as held for sale, adjusted for any depreciation, amortization or revaluations that would have been recognised had the asset (or disposal group) not been classified as held for sale, and;
- its recoverable amount at the date of the subsequent decision not to sell.

Discontinued operations are a component of the Bank that either has been disposed of or is classified as held for sale and represents a separate major line of business or geographical area of operation or is a subsidiary acquired exclusively with a view to resale.

The classification to this category takes places at the moment of sale or when the operation meets criteria of the operation classified as held for sale, if this moment took place previously. Disposal group which is to be taken out of usage may also be classified as discontinued operation.

2.19. Deferred income tax

The Bank creates a deferred income tax on the temporary difference arising between the carrying amount of an asset or liability in the statement of financial position and its tax base. A taxable net difference is recognised in liabilities as "Deferred income tax liabilities". A deductible net difference is recognised under "Deferred income tax assets". Any change in the balance of the deferred tax assets and liabilities in relation to the previous accounting period is recorded under the item "Income Tax".

Liabilities or assets for deferred income 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. Such liabilities or assets are determined by application of the tax rates in force by virtue of law or of actual obligations at the end of the reporting period. According to expectations such tax rates applied will be in force at the time of realisation of the assets or settlement of the liabilities for deferred income tax.

The main temporary differences arise on account of impairment write-offs recognised in relation to the loss of value of credits and granted guarantees of repayment of loans, amortisation of fixed assets and intangible assets, leases, revaluation of certain financial assets and liabilities, including contracts concerning derivative instruments and forward transactions, provisions for retirement benefits and other post-employment benefits, and also deductible tax losses.

The Bank reviews the carrying amount of a deferred tax assets at the end of each reporting period. The Bank reduces the carrying amount of a deferred tax asset to the extent that it is no longer probable that sufficient taxable profit will be available to allow the benefit of part or all of that deferred tax asset to be utilised. Any such reduction is reversed to the extent that it becomes probable that sufficient taxable profit will be available.

Deferred income tax assets are recognised to the extent it is probable that there will be sufficient taxable profits to allow them to recover. If the forecast amount of income determined for tax purposes does not allow the realisation of the asset for deferred income tax in full or in part, such an asset is recognised to the respective amount, accordingly. The above described principle also applies to tax losses recorded as part of the deferred tax asset.

In the case of the Bank, the deferred income tax assets and provisions are netted against each other separately for each country where the Bank conducts its business and is obliged to settle corporate income tax.

The Bank discloses separately the amount of negative temporary differences (mainly on account of unused tax losses or unutilised tax allowances) in connection with which the deferred income tax asset was not recognised in the statement of financial position, and also the amount of temporary differences attached to investments in subsidiaries and associates for which no deferred income tax provision has been formed.

Deferred income tax for the Bank is provided on assets or liabilities due to temporary differences arising from investments in subsidiaries and associates, except where, on the basis of any probable evidence, the timing of the reversal of the temporary difference is controlled by the Bank and it is possible that the difference will not reverse in the foreseeable future.

Deferred income tax on account of revaluation of financial instruments measured through other comprehensive income and of revaluation of cash flow hedging transactions is accounted for in the same way as any revaluation, directly in other comprehensive income, and it is subsequently transferred to the income statement when the respective investment or hedged item affects the income statement.

2.20. Assets repossessed for debt

Assets repossessed for debt represents financial and non-financial assets acquired by the Bank in settlement of overdue loans. The assets are initially recognised at fair value when acquired and included in premises and equipment, financial assets or other assets depending on their nature and the Bank's intention in respect of recovery of these assets. In case the fair value of repossessed collateral exceeds the receivable from the debtor, the difference constitutes a liability toward the debtor.

Repossessed assets are subsequently measured and accounted for in accordance with the accounting policies relevant for these categories of assets.

2.21. Prepayments, accruals and deferred income

Prepayments are recorded if the respective expenses concern the months succeeding the month in which they were incurred. Prepayments are presented in the statement of financial position under "Other assets".

Accruals include costs of supplies delivered to the Bank but not yet resulting in its payable liabilities. Deferred income includes received amounts of future benefits. Accruals and deferred income are presented in the statement of financial position under the item "Other liabilities".

2.22. Leasing

A contract is, or contains, a lease if the contract conveys the right to control the use of an identified asset for a period of time in exchange for consideration. The Bank shall reassess whether a contract is, or contains, a lease if the terms and conditions of the contract are changed.

Transfer of the right-of-use occurs when it concerns an identified asset, for which the lessee possesses the right to obtain substantially all of the economic benefits and it controls the use of the asset throughout the period of use.

mBank S.A. Bank as a lessee

If lease definition is fulfilled, the Bank recognises the right to use of the leased asset and a financial liability representing its obligation to make future lease payments in the amount of discounted future cash flows throughout the lease period.

The Bank as a lessee applies simplified approach and it does not apply the requirements in terms of recognition, measurement and presentation for short-term lease contracts lasting no longer than 12 months for each class of underlying asset as well as for lease contracts for which the underlying asset is of low value, i.e. less than PLN 20 000 for separate leases. Lease payments are recognised as costs using straight-line method throughout the lease period for lease contracts for which the Bank applies simplified approach.

Perpetual usufruct right is classified as a lease according to IFRS 16 due to the occurrence of future fees for the use of this right. The Bank assumed that the lease period for this type of contracts is the remaining period of the right granted since the transition to IFRS 16.

The Bank shall determine the lease term as the non-cancellable period of a lease, together with both:

- periods covered by an option to extend the lease if the Bank as a lessee is reasonably certain to exercise that option, and
- periods covered by an option to terminate the lease if the Bank as a lessee is reasonably certain not to exercise that option.

The Bank shall reassess whether it is reasonably certain to exercise an option to extend a lease, or not to exercise an option to terminate a lease. The Bank shall consider all relevant facts and circumstances that create an economic incentive for the lessee to exercise an option to extend a lease, or not to exercise an option to terminate a lease. The Bank shall reassess whether it is reasonably certain to exercise an extension option, or not to exercise a termination option, upon the occurrence of either a significant event or a significant change in circumstances that is within the control of the Bank as a lessee, and that affects whether the lessee is reasonably certain to exercise an option not previously included in its determination of the lease term, or not to exercise an option previously included in its determination of the lease term. The Bank shall revise the lease term if there is a change in the non-cancellable period of a lease.

At the commencement date, the Bank as a lessee shall measure the right-of-use asset at cost. The cost of right-of-use assets includes:

- the amount of the initial measurement of the lease liability,
- any lease payments made at or before the commencement date, less any lease incentives received,
- initial direct costs incurred by the Bank as a lessee in connection with the conclusion of the leasing contract and
- an estimate of the costs to be incurred by the Bank as a lessee in dismantling and removing the underlying asset, restoring the site on which it is located or restoring the underlying asset to the condition required by the terms and conditions of the lease, unless those costs are incurred to produce inventories.

After the commencement date, the Bank as a lessee shall measure the right-of-use asset at cost:

- less any accumulated depreciation and any accumulated impairment losses and,
- adjusted for any remeasurement of the lease liability.

The Bank applies the depreciation requirements in IAS 16 Property, Plant and Equipment in depreciating the right-of-use asset and requirements in IAS 36 Impairment of Assets to determine whether the right of use asset is impaired.

At the commencement date, the Bank shall measure the lease liability at the present value of the lease payments that are not paid at that date. At the commencement date, the lease payments included in the measurement of the lease liability comprise the following payments:

- fixed lease payments less any lease incentives,
- variable lease payments that depend on an index or a rate, initially measured using the index or rate as at the commencement date,
- amounts expected to be payable by the lessee under residual value guarantees,
- the exercise price of a purchase option if the lessee is reasonably certain to exercise that option and,
- payment of penalties for terminating the lease, if the lease term reflects the lessee exercising an option to terminate the lease.

Variable lease payments that depend on an index or a rate include, for example, payments linked to a customer price index, payments linked to a benchmark interest rate (such as LIBOR) or payments that vary to reflect changes in market rental rates.

After the commencement date, the Bank shall measure the lease liability by:

- increasing the carrying amount to reflect interest on the lease liability,
- reducing the carrying amount to reflect the lease payments made and,
- remeasuring the carrying amount to reflect any reassessment or lease modifications or to reflect revised in-substance fixed lease payments.

Bank discounts lease payments using the interest rate of lease if this rate can be easily determined. Otherwise, the Bank applies the marginal interest rate of lessee. As the lessee the Bank estimates the discount rate taking into account the duration and the currency of the contract.

The discount rates calculated by the Group were:

- for contracts in PLN: 1.95%,
- for contracts in EUR: 0.02%,
- for contracts in USD: 2.93%,
- for contracts in CZK: 2.19%.

All right-of-use assets are classified in tangible fixed assets (Note 26).

Lease liabilities are presented as financial liabilities measured at amortised cost (Note 29).

Cash payments of lease liabilities are classified in statement of cash flows within financial activities. Short term lease payments, payments for leases of low-value assets and variable lease payments not included in the measurement of the lease liability are classified in statement of cash flows within operating activities.

mBank S.A. Bank as a lessor

Operating lease

Bank recognises the lease payments from operating leases as income on a straight-line basis or in another systematic manner. Bank recognises costs, including depreciation, incurred in order to obtain benefits from leasing. Bank adds the initial direct costs incurred in order to obtain operating leasing to the carrying value of the underlying asset and it recognises these costs as expenses incurred throughout the lease period on the same basis as lease revenues. The method of depreciation of leased out depreciable assets should be the same as that foreseen by the normal depreciation rules adopted by the Bank with regard to similar assets, and the depreciation charges should be calculated in accordance with IAS 16 and IAS 38. In order to determine whether there has been any impairment of the object of the lease, the Bank applies IAS 36.

2.23. Provisions

Loan commitments and financial guarantee contracts are subject to loan loss provisions requirements according to IFRS 9 Financial Instruments.

According to IAS 37, provisions are recognised when Bank has a present legal or constructive obligation as a result of past events, it is more likely that an outflow of resources will be required to settle the obligation and the amount has been reliably estimated.

2.24. Post-employment employee benefits and other employee benefits

Post-employment employee benefits

The Group forms provisions against future liabilities on account of post-employment benefits determined on the basis of an estimation of liabilities of that type, using an actuarial model. The Group uses a principle of recognition of actuarial gains or losses from the measurement of post-employment benefits related to changes in actuarial assumptions in other comprehensive income that will not be reclassified to the income statement. The Group recognises service cost and net interest on the net defined benefit liability in the "Overhead cost" and in other interest expenses, respectively.

Equity-settled share-based payment transactions

The Group runs programmes of remuneration based on and settled in own shares. Equity-settled share-based payment transactions are accounted for in compliance with IFRS 2 Share-based Payment. In case of the part of the programme settled in shares, the fair value of the service rendered by employees in return for options and shares granted increases the costs of the respective period corresponding to own equity. The total amount which needs to be expensed over the period when the outstanding rights of the employees for their options and shares to become exercisable are vested is determined on the basis of the fair value of the granted options and shares. There are no market vesting conditions that shall be taken into account when estimating the fair value of share options and shares at the measurement date. Non-market vesting conditions are not taken into account when estimating the fair value of share options and shares but they are taken into account through adjustment on the number of equity instruments. At the end of each reporting period, the Group revises its estimates of the number of options and shares that are expected to become exercised. In accordance with IFRS 2 it is not necessary to recognise the change in fair value of the share-based payment over the term of the programmes.

2.25. Equity

Equity consists of capital and own funds created in compliance with the respective provisions of the law, i.e., the appropriate legislative acts, the Bank by-laws.

Registered share capital

Share capital is presented at its nominal value, in accordance with the by-laws and with the entry in the business register.

Own shares

In the case of acquisition of shares in the Bank by the Bank the amount paid reduces the value of equity as own shares until the time when they are cancelled. In the case of sale or reallocation of such shares, the payment received in return is recognised in equity.

Share premium

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

Costs directly connected with the issue of new shares and options reduce the proceeds from the issue recognised in equity. Moreover, share premium takes into account the settlements related to incentive programs based on Bank's shares.

Retained earnings

Retained earnings include:

- other supplementary capital,
- other reserve capital,
- general risk reserve,
- undistributed profit from previous years,
- net profit (loss) for the current year.

Other supplementary capital, other reserve capital and general risk reserve are formed from allocations of profit and they are assigned to purposes specified in the by-laws or other regulations of the law.

Moreover, other reserve capital comprises valuation of incentive programs based on Bank's shares.

Dividends for a given year, which have been approved by the General Meeting but not distributed at the end of the reporting period, are shown under the liabilities due to dividends payable under "Other liabilities".

Other components of equity

Other components of equity result from:

- valuation of financial assets at fair value through other comprehensive income,
- exchange differences on translation of foreign operations,
- actuarial gains and losses relating to post-employment benefits,
- valuation of derivative financial instruments held for cash flow hedging in relation to the effective portion of the hedge,
- the Bank's shares of other comprehensive income of entities under the equity method,
- fair value measurement of assets reclassified to investment property.

2.26. Valuation of items denominated in foreign currencies

Functional currency and presentation currency

The items contained in financial reports of particular entities of the Bank, including foreign branches of the Bank, are valued in the currency of the basic economic environment in which the given entity conducts its business activities ("functional currency"). The financial statements are presented in the Polish zloty, which is the presentation currency of the Bank.

Transactions and balances

Transactions denominated in foreign currencies are converted to the functional currency at the exchange rate in force at the transaction date. Foreign exchange gains and losses on such transactions as well as balance sheet revaluation of monetary assets and liabilities denominated in foreign currency are recognised in the income statement.

Foreign exchange differences arising on account of such monetary items as financial assets measured at fair value through profit or loss are recognised under gains or losses arising in connection with changes of fair value. Foreign exchange differences arising on account of such monetary items as equity instruments measured at fair value through other comprehensive income are recognised in other comprehensive income.

At the end of each reporting period non-monetary items that are measured in terms of historical cost in a foreign currency are translated using the exchange rate at the date of the transaction, and non-monetary items that are measured at fair value in a foreign currency are translated using the exchange rates at the date when the fair value was measured.

When a gain or loss on a non-monetary item is recognised in other comprehensive income, any exchange differences component of that gain or loss is recognised in other comprehensive income. Conversely, when a gain or loss on a non-monetary item is recognised in profit or loss, any exchange differences component of that gain or loss is recognised in profit or loss.

Changes in fair value of monetary items valued through other comprehensive income cover foreign exchange differences arising from valuation at amortised cost, which are recognised in the income statement.

Items of the statement of financial position of foreign branches are converted from functional currency to the presentation currency with the application of the average exchange rate as at the end of the reporting period. Income statement items of these entities are converted to presentation currency with the application of the arithmetical mean of average exchange rates quoted by the National Bank of Poland on the last day of each month of the reporting period. Foreign exchange differences so arisen are recognised in other comprehensive income.

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2.27. Trust and fiduciary activities

mBank S.A. operates trust and fiduciary activities including domestic and foreign securities and services provided to investment and pension funds.

The Bank provides custody, trustee, corporate administration, investment management and advisory services to third parties. Fee and commission income from trust and fiduciary activities is recognised in accordance with IFRS 15 using a 5-step model for revenue recognition, described in the Note 2.3. In connection with these, the Bank makes decisions concerning the allocation, purchase and sale of a wide variety of financial instruments. Assets held in a fiduciary capacity are not included in these financial statements because as they do not belong to the Bank.

2.28. New standards, interpretations and amendments to published standards

These financial statements include the requirements of all the International Accounting Standards, International Financial Reporting Standards and related interpretations as endorsed by the European Union which have been issued and are binding for annual periods starting on 1 January 2021

Standards and interpretations endorsed by the European Union

Published Standards and Interpretations which have been issued and binding for the first time in the reporting period covered by the financial statements

Standards and interpretations	Description of changes	Beginning of the binding periods	Impact on the Bank's financial statements in the period of their initial application
Amendments to IFRS 4 Extension of the Temporary Exemption from Applying IFRS 9	Amendments to IFRS 4 extend the temporary exemption from application of the IFRS 9 so that insurers will be required to apply IFRS 9 for annual periods beginning on or after 1 January 2023. The extension maintains the alignment between the expiry date of the temporary exemption and the effective date of IFRS 17, which replaces IFRS 4.	1 January 2021	The application of the amended standard will have no significant impact on the financial statements.
Amendments to IFRS 9, IAS 39, IFRS 7, IFRS 4 and IFRS 16 Interest Rate Benchmark Reform – Phase 2	Amendments to IFRS 9, IAS 39, IFRS 7, IFRS 4 and IFRS 16 Interest Rate Benchmark Reform – Phase 2 relate to the modification of financial assets, financial liabilities and lease liabilities, specific hedge accounting requirements, and disclosure requirements applying IFRS 7 resulting from the implementation of IBOR reform. The amendments to the standards require that in the case of a modification of the base for calculating cash flows, which is equivalent to the previous base and is the result of the implementation of the reform, the modification should be recognised as a result from a change in the variable interest rate. Regarding hedge accounting, amendments allow for the continuation of the existing relationships that were modified as a result of the IBOR reform, after appropriate modification of the documentation of the hedging relationship. Specific disclosures are also required in order to allow users to understand the nature and extent of risks arising from the IBOR reform to which the entity is exposed to and how the entity manages those risks as well as the entity's progress in transitioning from IBORs to alternative benchmark rates. IFRS 4 was also amended to require insurers that apply the temporary exemption from IFRS 9 to apply the amendments in accounting for modifications directly required by the IBOR reform.	1 January 2021	In 2021, the Bank worked on the implementation of IBOR reform. As a result, financial instruments based on the reference rates covered by reform were modified by replacing the IBOR with alternative benchmark rates. In order to correctly recognise the changes described above, in accordance with the requirements of the amended standards, the Bank assessed the economic equivalence of the changes introduced and recognised them in the books in accordance with the results of this assessment. The bank also modified the documentation of hedging relationships to reflect the changes resulting from the reform. The amendments did not have significant impact on the balance sheet of the modified instruments or on the interest income resulting from these instruments. The detailed information regarding the IBOR reform is provided below in this note.

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

Standards and interpretations	Description of changes	Beginning of the binding periods	Impact on the Bank's financial statements in the period of their initial application
Annual Improvements to IFRS Standards 2018-2020	Annual Improvements include changes to IFRS 1 First-time Adoption of International Financial Reporting Standards, IFRS 9 Financial Instruments, Illustrative Examples accompanying IFRS 16 Leases and IAS 41 Agriculture. The amendment to IFRS 9 clarifies which fees the entity includes when it applies the '10 per cent test' in assessing whether to derecognise a financial liability. The amendment to IFRS 16 removes the illustration of payments from the lessor relating to leasehold improvements.	1 January 2022	The application of the amended standard will have no significant impact on the financial statements.
Amendments to IAS 16 Property, Plant and Equipment: Proceeds before Intended Use	Amendments to IAS 16 prohibit a company from deducting from the cost of property, plant and equipment amounts received from selling items produced while the company is preparing the asset for its intended use. Instead, a company will recognise such sales proceeds and related cost in profit or loss.	1 January 2022	The application of the amended standard will have no significant impact on the financial statements.
Amendments to IAS 37 Onerous contracts – Cost of Fulfilling the Contract	Amendments to IAS 37 specifies which costs to include in estimating the cost of fulfilling a contract for the purpose of assessing whether the contract is onerous.	1 January 2022	The application of the amended standard will have no significant impact on the financial statements.
Amendments to IFRS 3 Reference to the Conceptual Framework	Amendments to IFRS 3 replaced references to the Framework with references to the 2018 Conceptual Framework. They also added a requirement that, for transactions and other events within the scope of IAS 37 or IFRIC 21, an acquirer applies IAS 37 or IFRIC 21 (instead of conceptual framework) to identify the liabilities it has assumed in business combination. Moreover, the standard added an explicit statement that an acquirer does not recognise contingent asset acquired in a business combination.	1 January 2022	The application of the amended standard will have no significant impact on the financial statements.
Amendments to IFRS 16, COVID-19-related Rent Concessions beyond 30 June 2021	In amendment to IFRS 16 COVID-19-related Rent Concessions beyond 30 June 2021 (the 2021 amendment) the Board extended the availability of the practical expedient that permits lessees not to assess whether rent concessions that occur as a direct consequence of the COVID-19 pandemic and meet specified conditions are lease modifications by one year.	1 April 2021	The application of the amended standard will have no significant impact on the financial statements.
IFRS 17, Insurance contracts	IFRS 17 defines a new approach to the recognition, valuation, presentation and disclosure of insurance contracts. The main purpose of IFRS 17 is to guarantee the transparency and comparability of insurers' financial statements. IFRS 17 introduces a number of significant changes in relation to the existing requirements of IFRS 4. They concern, among others: methods for the valuation of insurance liabilities, recognition a revenues and result from insurance contract.	1 January 2023	The application of the amended standard will have no significant impact on the financial statements.
Amendments to IFRS 17, Insurance contracts	Amendments to IFRS 17 include a two-year deferral of the effective date and the fixed expiry date of the temporary exemption from applying IFRS 9 granted to insurers meeting certain criteria. Preparers of financial statements are no longer required to apply IFRS 17 to certain credit cards and similar arrangements, and loans that provide insurance coverage.	1 June 2023	The application of the amended standard will have no significant impact on the financial statements.

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Standards and interpretations not yet endorsed by the European Union

These financial statements do not include standards and interpretations listed below which await endorsement of the European Union.

Standards and interpretations	Description of changes	Beginning of the binding periods	Impact on the Bank's financial statements in the period of their initial application
Amendments to IAS 12, Deferred tax related to assets and liabilities arising from a single transaction	The amendments to the standards require that the entities recognise in the financial statements deferred tax assets and liabilities resulting from transactions, other than business combinations, in which equal amounts of deductible and taxable temporary differences arise on initial recognition.	1 January 2023	The application of the amended standard will have no significant impact on the financial statements.
Amendments to IAS 1, Classification of liabilities as current or non-current	Amendments to IAS 1 affect the requirements for the presentation of liabilities in the financial statements. In particular, they explain one of the criteria for classifying liabilities as non-current.	1 January 2023	The application of the amended standard will have no significant impact on the financial statements.
Amendment to IAS 8, Definition of Accounting Estimates	In amendment to IAS 8, the definition of a change in accounting estimates was replaced with a definition of accounting estimates. Under the new definition, accounting estimates are monetary amounts in financial statements that are subject to measurement uncertainty. The introduction of a definition of accounting estimates and other amendments to IAS 8 was aimed to help entities distinguish changes in accounting policies from changes in accounting estimates.	1 January 2023	The application of the amended standard will have no significant impact on the financial statements.
Amendments to IAS 1 and IFRS Practice Statement 2 Disclosure of Accounting Policies	Amendments to IAS 1 and IFRS Practice Statement 2 are intended to help preparers in deciding which accounting policies to disclose in their financial statements. The amendments introduce the requirement to disclose material accounting policy information instead of significant accounting policies with some clarifications and examples how an entity can identify material accounting policy information.	1 January 2023	The application of the amended standard will have no significant impact on the financial statements.
IFRS 17, Insurance contracts and IFRS 9	The amendment to the standards introduces optional facilities to minimize the accounting mismatch between financial assets and liabilities presented in the comparative data of the financial statements of entities applying IFRS 17 and IFRS 9 for the first time.	1 January 2023	The application of the amended standard will have no significant impact on the financial statements.

IBOR reform

In 2021, mBank continued efforts to implement the reform of reference rates initiated by Regulation 2016/1011 of The European Parliament and of the Council of 8 June 2016 on indices used as benchmarks in financial instruments and financial contracts or to measure the performance of investment funds and amending Directives 2008/48/EC and 2014/17/EU and Regulation (EU) No 596/2014 (further "BMR") which resulted, inter alia, in the Financial Conduct Authority's (further "FCA") decision to cease quoting or lose representativeness of LIBOR rates (hereinafter IBOR reform). In order to effectively implement the changes resulting from the IBOR reform, a project has already been launched at mBank in 2020 involving mBank's units responsible for risk management, treasury, retail and corporate banking, financial markets, IT, accounting, reporting and compliance areas. The implementation of the project is supervised by the Steering Committee and the Capital, Asset and Liability Management Committee of mBank.

The key risks faced by the Bank in relation to the IBOR reform identified and managed under the project are:

- risks resulting from lack of established market practices and uncertainty related to transition of the contracts to new alternative reference rates, which could lead to deterioration of the risk profile of these contracts,
- risk of customers not cooperating with the Bank in the process of introducing IBOR reform required contractual changes and the resulting uncertainty concerning the appropriate basis to calculate the contractual cashflows after cessation of or losing representativeness of LIBOR indexes,
- risk of delayed implementation of required IT changes which could hinder correct interest calculation or financial asset and liabilities valuation,
- operational risks related to the number of contracts that require amending as a result of the IBOR reform, including risks related to mass processing of client's personal data required to implement changes to client contracts.

As a result of the project, the Bank updated and implemented changes to its action plan in the event of material changes or discontinuation of an index or benchmark, developed and started the process of introducing fallback clauses in its customer contracts.

WIBOR and EURIBOR indices, as a result of actions of Polish and European regulators, were reformed and brought in line with the BMR regulation, which significantly reduced the risk of reform in their scope and limited the necessary changes to the implementation of emergency clauses in case of discontinuation of quoting these rates in the future.

On 19th January 2021 the European Parliament amended the BMR regulation granting the European Commission the power to designate an alternative reference index for indices in scope of the IBOR reform. Such by law replaces all references to the index that ceases to be published in all contracts and financial instruments whose provisions do not provide for solutions in the event of permanent cessation of the index publication. On October 14, 2021, the European Commission issued Regulation (EU) 2021/1847 on the designation of a statutory replacement for certain settings of CHF LIBOR and designated an alternative reference rate. This decision significantly reduced the risks related to cessation of publishing of this reference index.

In order to mitigate the risks related to other reference indices, mBank participated in works of the working groups established by Polish Bank Association and took advantage of the solutions developed consultation process led by International Swaps and Derivatives Association (ISDA) and other international organisations.

In the fourth quarter 2021 the Bank has intensified activities related to implementing required changes to contracts with retail and corporate customers based on reference indices for European Commission had not designated alternative reference rates. Particular emphasis, in order to maximise the percentage of annexed agreements was placed on effective and transparent communication of the required changes and training of the banks' staff to prepare for implementation of the new contract clauses. As a result of these actions, according to Banks estimation, as at the end of 2021, over 40% of mortgage loans based on LIBOR EUR were successfully amended to include the required clauses.

In addition, with exception for single cases, all loan agreements from the corporate segment based on LIBOR family indices include fallback clauses addressing events of change or cessation of reference rates.

Derivative instruments based on LIBOR rates (except for LIBOR USD) were converted to instruments based on alternative reference rates by clearing houses or in case of derivatives not cleared centrally in accordance with methodology developed by ISDA in the course of market consultations.

Bank has also adjusted risk models to the new reference rates and implemented IT changes to properly handle the new reference rates as well as business relevant products and instruments based on those rates. Due to complexity of the IT systems, further changes in this area will continue in 2022.

As result of the action taken by the Bank, at year end 2021, the Bank has significantly mitigated the risks associated with the IBOR reform described above.

The table below presents the Bank's exposure as at 31 December 2021 to material reference rates in scope of the IBOR reform for which the transition to the alternative reference rates was yet not completed.

(PLN million)	The contractual amount of non-derivative financial asset	The contractual amount of non-derivative financial liabilities	Nominal amount of derivatives as a net amount of receivables and liabilities for derivative transactions
EUR LIBOR	2 977	18	-
USD LIBOR	1 047	4	108
CHF LIBOR	12 190	1 779	(8 804)
GBP LIBOR	69	-	-
JPY LIBOR	5	-	-
Other	3	-	-

As WIBOR, EURIBOR and PRIBOR rates have been recognised as compliant with the BMR Regulation, exposures based on these rates are not presented in the above table as at 31 December 2021. If in the future it turns out that these rates no longer comply with the requirements of the BMR Regulation, mBank will activate the appropriate procedures provided for in such a case by the action plan.

The amounts of assets, liabilities and derivative instruments based on CHF LIBOR reference rate after the end of the current interest rate period, that is until the end of first quarter 2022, will expire or be converted either to SARON Compound rate adjusted for appropriate tenor related spread, in line with the European Commission Regulation dated 14 October 2021 mentioned above, or to other reference agreed in the contract.

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In case of LIBOR USD based contracts, both loans and derivatives, mBank will continue efforts to introduce to contracts with customers relevant fallback clauses and alternative reference rate based on those clauses. However, taking into account the mBank's limited exposure and that by the end of 2021 fallback clauses were already implemented to corporate loan portfolio, the bank does not perceive any significant risks related to this process.

In case of LIBOR EUR based contracts, approximately half of the Bank's exposure will be converted to EURIBOR in first quarter of 2022. The rest of the portfolio, in cases where customers did not respond or refused to signed contract annexes introducing the alternative reference rate, the contractual interest will be calculated based on the interest rate valid for the previous interest period. The Bank does not exclude the possibility of signing an appropriate annex at a later date at the initiative of the customer. Bank currently is not offering any products based on BMR non-compliant reference rates.

The impact of the IBOR reform is presented in Note 19.

2.29. Business segments

Data concerning business segments was presented in the Consolidated Financial Statements of mBank S.A. Group for the year 2021, prepared in compliance with the International Financial Reporting Standards and published on 1 March 2022.

2.30. Comparative data

- Impact of the legal risk related to court cases concerning indexation clauses in mortgage and housing loans

Starting from 2021, the Bank changed the accounting policy for recognizing the impact of the legal risk related to court cases concerning indexation clauses in mortgage and housing loans in CHF. Until the end of 2020 the Bank recognised provisions for legal proceedings in accordance with IAS 37 "Provisions, Contingent Liabilities and Contingent Assets" in relation to both active and repaid loans. In view of changes in conditions, such as the growing number of court cases and the predominantly unfavourable court judgments stating the invalidity of the contract in whole or certain provisions thereof the Bank expects that it will not obtain the full amount of contractual cash flow. Therefore in relation to active loans the Bank revised its estimates of cash flows and adjusted the gross carrying amount of those loans in accordance with IFRS 9 "Financial Instruments" paragraph B5.4.6. as the change in expected cash flows is not related to credit risk and therefore is not recognised as expected credit losses. The comparative data as at 1 January 2020 and 31 December 2020 and for the period from 1 January to 30 December 2020 have been restated accordingly. The recognition of the impact of legal risk related to repaid loans remained unchanged. The above change did not affect the equity and the income statements of the Bank in the comparative periods presented in this report. The data on capital ratios for comparative periods remained unchanged. The impact of the introduced adjustments on the comparative data is presented in the following tables.

Restatements in statement of financial position at 1 January 2020

ASSETS	01.01.2020 before restatement	restatement	01.01.2020 after restatement
Financial assets at amortised cost, including:	101 310 293	(367 555)	100 942 738
Debt securities	*11 234 873*	-	*11 234 873*
Loans and advances to banks	*7 337 703*	-	*7 337 703*
Loans and advances to customers	*82 737 717*	*(367 555)*	*82 370 162*
Other assets	47 917 980	-	47 917 980
TOTAL ASSETS	**149 228 273**	**(367 555)**	**148 860 718**

LIABILITIES AND EQUITY	01.01.2020 before restatement	restatement	01.01.2020 after restatement
Provisions	737 167	(367 555)	369 612
Other liabilities	132 376 099	-	132 376 099
TOTAL LIABILITIES	**133 113 266**	**(367 555)**	**132 745 711**
TOTAL EQUITY	**16 115 007**	**-**	**16 115 007**
TOTAL LIABILITIES AND EQUITY	**149 228 273**	**(367 555)**	**148 860 718**

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Restatements in statement of financial position at 31 December 2020

ASSETS	31.12.2020 before restatement	restatement	31.12.2020 after restatement
Financial assets at amortised cost, including:	110 792 043	(1 264 677)	109 527 366
Debt securities	*15 952 501*	-	*15 952 501*
Loans and advances to banks	*10 845 844*	-	*10 845 844*
Loans and advances to customers	*83 993 698*	*(1 264 677)*	*82 729 021*
Other assets	61 217 641	-	61 217 641
TOTAL ASSETS	**172 009 684**	**(1 264 677)**	**170 745 007**

LIABILITIES AND EQUITY	31.12.2020 before restatement	restatement	31.12.2020 after restatement
Provisions	1 779 888	(1 264 677)	515 211
Other liabilities	153 762 104	-	153 762 104
TOTAL LIABILITIES	**155 541 992**	**(1 264 677)**	**154 277 315**
TOTAL EQUITY	**16 467 692**	**-**	**16 467 692**
TOTAL LIABILITIES AND EQUITY	**172 009 684**	**(1 264 677)**	**170 745 007**

Restatements in statement of cash flows for the period from 1 January to 31 December 2020

	Period from 01.01.2020 to 31.12.2020 before restatement	restatement	Period from 01.01.2020 to 31.12.2020 after restatement
Profit (loss) before income tax	**572 996**	**-**	**572 996**
Adjustments, including:	***(3 309 182)***	**-**	***(3 309 182)***
Changes in financial assets and liabilities held for trading and hedging derivatives	(5 149 823)	897 122	(4 252 701)
Changes in loans and advances to customers	1 042 721	(897 122)	145 599
Changes in provisions	797 920	-	797 920
Other adjustments	**(2 736 186)**	**-**	**(2 736 186)**
A. Cash flows from operating activities	**(278 830)**		**(278 830)**
B. Cash flows from investing activities	**(1 014 965)**		**(1 014 965)**
C. Cash flows from financing activities	**(4 029 981)**	**-**	**(4 029 981)**
Net increase / decrease in cash and cash equivalents (A+B+C)	30 883	-	30 883
Effects of exchange rate changes on cash and cash equivalents	8 204 230	-	8 204 230
Cash and cash equivalents at the beginning of the reporting period	**4 205 132**	**-**	**4 205 132**

The changes in the comparative data, as described above, has been included in these financial statements in all the notes to which these change referred.

3. Risk Management

mBank S.A. manages risks on the basis of regulatory requirements and best market practice, by developing risk management strategies, policies and guidelines. The risk management functions and roles are released on all of the levels of the organizational structure, starting at the level of the Supervisory Board down to each business unit of the Bank. Risk management is streamlined in unified process run by specialized organizational units, and analyses are carried out at the level of mBank.

3.1. mBank risk management in 2021 – external environment

The Bank is taking steps to achieve full compliance with regulatory requirements.

CRR/CRD IV regulatory package

The Bank has implemented changes to the CRR/CRD IV regulatory package, in particular:

- Regulation (EU) 2019/876 of the European Parliament and of the Council of 20 May 2019 amending Regulation (EU) No 575/2013 as regards the leverage ratio, the net stable funding ratio, requirements for own funds and eligible liabilities, counterparty credit risk, market risk, exposures to central counterparties, exposures to collective investment undertakings, large exposures, reporting and disclosure requirements, and Regulation (EU) No 648/2012,
- Directive (EU) 2019/878 of the European Parliament and of the Council of 20 May 2019 amending Directive 2013/36/EU as regards exempted entities, financial holding companies, mixed financial holding companies, remuneration, supervisory measures and powers and capital conservation measures,

most of which, were binding starting from 28 June 2021.

The altered provisions of the Directive have already been transposed into the Polish law by amendments to the Banking Law Act and other acts, as well as secondary legislation. The Bank is also adapting its processes and systems on an ongoing basis with regard to changes in mandatory reporting and Pillar III disclosures.

Regulatory changes resulting from the work of the Basel Committee on Banking Supervision

The Bank monitors regulatory developments arising resulting from the work of the Basel Committee on Banking Supervision. In particular, these related to the review of the methodologies for calculating capital requirements (the so-called Basel 4). 27 October 2021. The European Commission adopted a draft amendment to the EU banking legislation (CRR/CRD IV), which aims to implement the updated Basel standards into EU legislation, primarily with regard to the calculation of capital requirements for individual risks. The new requirements would be effective from 2025. The Bank analyses the proposed regulatory changes and assesses their impact in preparation for their implementation. It also follows the legislative work in this area, as the published draft amendments have not yet been finally approved in the EU and may still change during the legislative work.

Directive BRRD2

The provisions of Directive BRRD2 [Directive (EU) 2019/879 of the European Parliament and of the Council of 20 May 2019 amending Directive 2014/59/EU as regards loss absorption capacity and recapitalisation of credit institutions and investment firms and Directive 98/26/EC] have also been transposed into the Polish legal order as part of the amendment of the Act on the Bank Guarantee Fund, deposit guarantee scheme and compulsory restructuring and certain other acts. The aforementioned legal acts introduced changes to the rules for calculating and maintaining the MREL requirement. This in turn has necessitated modification of the Fund's previous approach to determining the MREL requirement for banks. The first binding inerim MREL target should be fulfilled by 31 December 2021 and the mBank has met this requirement, however the final target should be met by 31 December 2023.

AIRB models

In 2016 - 2021 the EBA published documents, as part of a broader regulatory initiative concerning revision of the Internal Ratings Based Approach (AIRB), which include:

- draft Regulatory Technical Standards on assessment methodology for IRB approach,
- guidelines on PD estimation, LGD estimation and treatment of defaulted assets,
- guidelines and regulatory technical standard on estimation and identification of an economic downturn in IRB modelling (with regard to LGD parameter),
- guidelines on Credit Risk Mitigation for institutions applying the IRB approach with own estimates of LGDs,
- Commission delegated regulation (EU) 2021/598 of 14 December 2020 supplementing Regulation (EU) No 575/2013 of the European Parliament and of the Council with regard to regulatory technical standards for assigning risk weights to specialized lending exposures.

In June 2021 Bank submitted the application for approval of material changes in all PD, CCF and LGD parameters models in portfolios covered by AIRB approach to banking supervisory authorities. The implementation of AIRB models adapted to the aforementioned guidelines is planned for 2022, immediately after the approval of the banking supervisory authorities.

The Bank adjusted the CRE dedicated model to Regulation 2021/598, which will apply from April 2022. As part of this process, the Bank submitted notification addressing the model adjustment to the banking supervisory authorities in February 2022. The model adjustment will not be classified as significant change according to the criteria specified in RTS 529/2014.

PFSA recommendations

In order to update good practices binding on banks, including in the context of new guidelines and requirements defined by the European supervisory authorities, taking into account regulatory solutions and practices applied in other countries, PFSA regularly works on updating recommendations addressed to banks. Work is currently underway on:

- updating Recommendation G concerning interest rate risk management. Work on the amendment has been temporarily suspended;
- updating Recommendation A related to derivatives activities, which will replace the current Recommendation A issued in 2010. Further consultations with the banking sector are currently underway.

In 2021, PFSA issued an updated Recommendation R on the principles of credit risk management and recognition of expected credit losses. Recommendation R entered into force on 1 January 2022. Works on the implementation of the requirements of Recommendation R are continued by the Bank in 2022. The most important changes resulting from the implementation of Recommendation R in the area of the definition of default and expected credit losses are described in Note 3.3.6.2.4.

IBOR reform

The Bank is carrying out a project which is aimed at preparing for the cessation of LIBOR rates announced by FCA (Financial Conduct Authority) on 5 March 2021. LIBOR reference rates are used both in products offered to retail and corporate clients and in financial markets instruments. At the same time, the Bank continues to carry out project work addressing further changes to the publication or changes to the calculation rules for other benchmarks used in financial products and instruments.

EBA guidelines and standards on interest rate risk in the banking book

In December 2021 EBA launched consultations specifying technical aspects of the revised framework regarding interest rate risks for banking book (IRRBB):

- project of Guidelines on IRRBB and credit spread risk arising from the banking book (CSRBB),
- project of RTS on the IRRBB standardised approach,
- project of RTS on IRRBB supervisory outlier tests.

These regulations contain detailed provisions and requirements for the management of interest rate risk in the banking book that will apply to banks in the context of the regulatory changes that have taken place in CRD IV with regard to interest rate risk in the banking book. Consultations with the banking sector are currently underway.

Regulations in the area of sustainable development

From June 18, 2020, Regulation 2020/852 of the European Parliament and of the Council on the establishment of a framework to facilitate sustainable investments (Regulation on the EU Taxonomy), is in force. This regulation is a key element of the EU Action Plan, the so-called Green Deal for financing sustainable economic growth. The plan is to redirect capital flows towards sustainable investments and ensure market transparency. The taxonomy introduces a single EU classification system for activities for sustainable development. It is a tool to support entrepreneurs and investors in sustainable investment decisions. 4 June 2021 EU Commission issued Delegated Regulation no 2021/2139 establishing the technical criteria that define sustainable economic activities making a significant contribution to climate change mitigation or climate change adaptation.

The act specifying the provisions of Article 8 of the Taxonomy is the EU Commission Delegated Regulation No 2021/2178 of 6 July 2021, which precisely defines the scope of information on sustainable economic activity disclosed by large non-financial enterprises and credit institutions. It specifies in detail the content and presentation of the information disclosed and the deadlines for mandatory disclosures. The act establishes a transitional period (from 1 January 2022 to 31 December 2023) for financial institutions regarding the disclosure of information. During the transitional period, financial institutions shall only disclose information about exposures to Taxonomy eligible.

Regulation (EU) 2019/2088 of the European Parliament and of the Council on sustainability-related disclosures in the financial services sector (SFDR) has been in force since 10 March 2021. The regulation defines the scope of disclosures, including information about:

- the adopted strategy regarding risks related to sustainable development for investment decisions,
- negative impact of investment decisions on the factors of sustainable development,
- ensuring consistency of the remuneration policy with the introduction of risks to sustainable development into the business.

In June 2021, the European Banking Authority (EBA) published a report on the management and supervision of environmental, social and governance (ESG) risks for credit institutions and investment firms. The document presents:

- a common definition of ESG-related risks,
- review of assessment methods that are necessary for effective risk management,
- recommendations related to the recognition of ESG-related risks in the business strategy, bank management rules and the risk management process.

Detailed information on how mBank S.A. addresses sustainability issues is described in chapter 12 of the Management Board Report on Performance of mBank S.A. (regarding taxonomy in subchapter 6).

3.2. Principles of risk management

In 2021, in connection with the persistent COVID-19 pandemic and its impact on the economic situation, the Bank monitored their development and adjusted risk management policies and processes on an ongoing basis. This especially refers to the credit risk.

Bank, in the corporate banking area, on regular basis, adapted credit risk policies and the credit risk management process to the economic situation, taking into account the impact of the coronavirus pandemic.

An important element of risk management is the consideration of the environmental, social and corporate governance impacts on credit development, and in particular the incorporation of ESG considerations into credit risk processes and policies. The ESG risk assessment is one of the elements of the customer's credit risk assessment. If a high ESG risk is identified, the Bank conducts an in-depth analysis of the customer's business model, assesses the impact of this risk on the customer's financial results and its ability to settle future liabilities, and also assesses the impact of the customer's ESG risk on the reputation risk of the Bank. The result of the ESG risk analysis is taken into account in the credit decision to provide financing and annually in the renewal of the customer's PD-rating.

In retail area Bank adapted its current credit policy for ML and NML segment to expected economic downturn caused by COVID-19 pandemic. Changes in credit policy address most probable risks:

- decrease in account turnover,
- increased unemployment rate,
- permanent or temporary deterioration of financial standing in particular sectors particularly exposed, in opinion of the Bank, to the negative effect of the pandemic.

Additionally, in the mortgage segment, the Bank takes into account the potential reduction in borrower salaries.

Due to the transition to remote work by the majority of employees, Bank constantly monitored - through operational risk tools - the processes functioning during the pandemic and defined corrective action plans aimed at improving the methods of working in that mode.

3.2.1. Risk management culture

The foundations of the risk culture implemented in the Bank and the mBank Group have been specified in the Risk Management Strategy of mBank Group and strategies for managing individual types of risk (concentration risk, retail and corporate portfolio credit risk, market risk, liquidity risk, operational risk, reputational risk) approved by the Management Board and the Supervisory Board of mBank.

Risk management roles and responsibilities in the mBank Group are organised around the three lines of defence scheme:

- The first line of defence consists of Business (business lines) whose task is to take risk and capital aspects into consideration when making all business decisions within the risk appetite set for the Group.
- The second line of defence, mainly the organizational units of the risk management area, Security and Compliance function, determines framework and guidelines for managing individual risks, supports and supervises Business in their implementation and independently analyses and assesses the risk.

To ensure that the Business is supported and supervised in an objective manner, the second line functions act independently of the Business.

- The third line of defence is Internal Audit, ensuring independent assessment of activities connected with risk management performed by the first and the second line of defence.

3.2.2. Division of responsibilities in the risk management process

Supervisory Board supervises the Bank's operations in the area of the risk management system. This includes approving the Risk Management Strategy of the mBank Group and supervising its implementation.

Risk Committee of the Supervisory Board exercises constant supervision over the risk, in particular issues recommendations regarding approval of risk management strategies, including the Risk Management Strategy of mBank Group, by the Supervisory Board.

Management Board of the Bank designs, implements and ensures the operation of the risk management system. In particular the Management Board defines and implements the Risk Management Strategy of the Group and is responsible for defining and implementing the principles of managing individual risk types and for their consistency with the Strategy. The Management Board establishes the organisational structure of the Bank and allocates tasks and responsibilities to individual organizational units, ensuring the appropriate distribution of roles in the risk management. The Management Board is also responsible for developing, implementing, effectiveness and updating written strategies, policies and procedures for: risk management system, internal capital adequacy assessment process, capital management and capital planning, and internal control system.

Chief Risk Officer is responsible for integrated risk and capital management of the Bank and the Group in the scope of: defining strategies and policies, measuring, controlling and independent reporting on all risk types (in particular credit risk, market risk, liquidity risk, non-financial risk including operational risk), approving limits (in accordance with internal regulations), and for processes of managing the risk of the retail credit portfolio and corporate portfolio.

Committees:

- **The Committees of the Business and Risk Forum of mBank Group** (Retail Banking Risk Committee – KRD, Corporate and Investment Banking Risk Committee – KRK, Financial Markets Risk Committee – KRF) are a platform for making decisions and dialogue for organizational units in particular business lines and the risk management area in mBank as well as between the Bank and the Group subsidiaries. In particular, the Committees take decisions and make recommendations concerning i.a.: risk policies, risk assessment processes and tools, risk limit system, assessment of the quality and profitability of the portfolio of exposures to clients, approval of introducing new products to the offer.
- **Model Risk Committee** is responsible for supervising the model risk management process, performing an informative, discussion, decision-making and legislative function in this respect.
- **Capital, Assets and Liabilities Committee** is responsible for the systematic monitoring of the balance sheet structure and capital, and the allocation of funds within acceptable risks. Its purpose is to optimize financial result, as well as to shape and allocate capital in a way that maximizes return on equity of the mBank Group.
- **Sustainable Development Committee of mBank Group** is a platform for making decisions and issuing recommendations, and dialogue on sustainable development. The Committee shapes, promotes and monitors sustainable development in the mBank Group.
- **Credit Committee of the mBank Group** is responsible, in particular, for the supervision of concentration risk and large exposures at the Group level by taken decisions and made recommendations. The Committee shall also take credit decisions as well as decisions on debt conversion into shares, stocks, and on taking over properties in return for debts (applies to the Bank).
- **Investment Banking Committee** is responsible, in particular, for the control and management of risks (including market, credit, reputational and operational) of the Brokerage House transactions and making decisions regarding the execution of these transactions.
- **Foreign Branch Supervision Committee of mBank S.A.** is responsible, among others, for issuing recommendations on approval of the operational strategy and the rules for stable and prudent management of a particular foreign branch of the Bank, especially with reference to credit risk.

The function of management at the strategic level and the function of control of credit, market, liquidity and operational risks and risk of models used to quantify the aforesaid risk types are performed in the risk management area supervised by the Deputy Chairman of the Management Board, Chief Risk Officer.

3.2.3 Internal capital and liquidity adequacy assessment process (ICAAP/ILAAP)

The mBank Group applies the internal capital adequacy assessment process (ICAAP) aimed at maintaining own funds at the level adequate to the profile and the level of risk in its operations. The ICAAP includes:

- risk inventory in the mBank Group,
- calculation of internal capital and own funds requirements for coverage of risk,
- capital aggregation,
- stress tests,
- setting limits on the utilization of capital resources,
- capital planning and allocation,
- monitoring consisting in a permanent identification of risk involved in mBank Group operations and analysis of the level of capital for risk coverage.

The liquidity adequacy assessment process (ILAAP) implemented in mBank Group plays a key role in maintaining the Bank's and the Group's business continuity by ensuring an appropriate liquidity and financial position. ILAAP comprises of:

- Group's liquidity and funding risk inventory,
- calculation of liquidity measures, including modelling of selected banking products,
- balance sheet planning and setting limits in line with the risk appetite,
- management, taking into account the stress tests, risk measures, contingency plan, early warning indicators (EWI), recovery indicators (RI) and limits monitoring,
- process review and assessment,
- Funds Transfer Pricing (FTP) system,
- model validation.

The ICAAP and ILAAP are reviewed by the Bank's Management Board on a regular basis. Reviews of these processes are supervised by the Supervisory Board of the Bank.

<u>Material risks in mBank Group's operations</u>

The Management Board is taking activities for ensuring that the Bank manages all material risks arising from the implementation of adopted business strategy. Therefore, the mBank Group carries out an annual process of identifying and assessing risk materiality. All material types of risk are included in the Risk Management Strategy of mBank Group, in particular in the process of risk bearing capacity management.

The following risks were recognised as material for the Group as of 31 December 2021: credit risk, market risk, operational risk, business risk (including strategic risk), liquidity risk, compliance risk, reputational risk, model risk, capital risk (including risk of excessive leverage), tax risk and FX loans portfolio risk.

3.2.4. Risk appetite

Risk appetite is defined within the mBank Group as the maximum risk, in terms of both amount and structure, which the Bank is willing and able to incur in pursuing its business objectives under going concern scenario.

<u>Capital and liquidity buffers</u>

Risk appetite is determined below the available resources determined by the minimum supervisory requirements on capital adequacy and liquidity, set in the European and Polish regulations, in order to ensure that the Group is functioning in an uninterrupted manner in the case of negative changes in the Group or in its environment, thereby providing the ability to assure risk bearing capacity. Funding sources and capital position of the Group, both in the regulatory and economic perspective, are taken into consideration while defining the risk capacity and risk appetite. The Bank maintains capital and liquid assets on the levels ensuring to meet regulatory requirements under normal and realistic stress conditions. To determine the appropriate volume of the liquidity buffer, a minimum level of LCR above the regulatory requirement has been established.

mBank Group's risk appetite covers all significant risks and key risk concentrations embedded in its business strategy by setting appropriate capital buffers necessary in case of materialization of selected risk factors related to existing portfolios and planned business, and addressing new regulatory requirements and potential negative macroeconomic changes.

As a result of internal discussion on risk appetite, the target capital ratios and internal liquidity buffers for the mBank Group are determined.

Risk Bearing Capacity

Risk bearing capacity is expressed in terms of capital and funding resources available for allocation so as to ensure safety in normal scenario and risk scenario. The maximum risk that mBank Group is willing and able to incur, while accepting threats resulting from mBank Group business strategy, is subject to the following conditions:

- adequate risk bearing capacity must be ensured (limits must be ensured in normal conditions) in accordance with ICAAP principles,
- internal targets set for regulatory capital ratios must be observed,
- financial liquidity and adequate structural liquidity of the Group must be ensured at all times in accordance with ILAAP principles.

The approach of mBank Group to the assessment and control of mBank Group risk bearing capacity covers internal and regulatory requirements.

Risk limit system

The mBank applies a risk limit system in order to ensure effective allocation of risk appetite. The structure of limits translates the risk appetite into specific constraints on risks occurring in the Bank's activity. In addition to the limits, monitoring action triggers and early warning indicators are also used to ensure the safe operation of the Bank.

3.2.5. Stress tests within ICAAP and ILAAP

Stress tests are used in the management and capital and liquidity planning of the Bank. Stress tests allow an assessment of the Bank's resistance in the context of adverse, yet plausible scenarios of external and internal events.

The stress tests are conducted assuming scenario of unfavourable economic conditions that may adversely affect the Bank's financial and liquidity position.

As part of ICAAP, the Bank carries out stress tests using various scenarios, including historical scenarios, macroeconomic scenarios for economic downturn, scenarios that take into account idiosyncratic events, in the context of specific risk concentrations in the Bank. Such analyses take into account different levels of severity of the scenarios, which are characterised by different probability levels regarding their realisation.

The ILAAP scenarios include negative idiosyncratic events, events concerning the entire market and combined scenarios. These scenarios are supplemented by a reverse scenario that identifies risk factors. In addition, an integrated scenario is carried out, which also takes into account the impact of factors derived from other types of risk.

The analysed macroeconomic scenarios allow for a comprehensive analysis of: all significant risk types and scenarios' impact on the capital adequacy and liquidity of the Bank.

Bank carries out so called reverse stress tests, the goal of which is to identify events potentially leading to unviability of the Bank. Reverse stress tests are used for making strategic decisions concerning the acceptable risk profile of the Bank.

3.2.6. Financial results of mBank and mBank Group in the context of regulatory requirements

Bank monitors the recovery plan indicators in the areas of liquidity, capital, profitability and assets quality in accordance with the governance stipulated in the Recovery Plan for mBank Group.

In line with the guidelines of European Banking Authority (EBA/GL/2015/02) on the minimum list of qualitative and quantitative recovery plan indicators, profitability indicators should capture any institution's income-related aspect that could lead to a rapid deterioration in the institution's financial position through lowered retained earnings (or losses) impacting own funds of the institution.

The profitability of core business model of the Bank remained high and stable in 2021. The results for 2021 were influenced by extraordinary events, independent from the core business of the Bank i.e. recognizing in 2021 costs of legal risk related to the currency loan portfolio in the amount of PLN 2 758 079 thousand.

It should be emphasized that despite the consolidated net loss in 2021 in the amount of PLN 1 178 813 thousand, in accordance with the applicable provisions regarding recovery plans, in particular Article 142(2) of the Banking Law, the prerequisite related to significant deterioration of the financial situation of the Bank and the Group has not been met.

Recovery plan indicators in the areas of liquidity, capital and assets quality demonstrate the stable and robust situation of the Bank and the Group.

3.3. Credit risk

3.3.1. Organization of risk management

The mBank Group actively manages credit risk in order to optimise the level of profit in terms of return on risk. Analysis of the risk in the Group operations is continuous. For the purpose of identification and monitoring of credit risk, uniform credit risk management rules are applied across the Bank's structure and its subsidiaries; they are based, among others, on separation of the credit risk assessment function and the sales function at all levels up to the Management Board. A similar approach is applied to administration of credit risk exposures as this function is performed in the risk area and the operating area and is independent from sales functions. The model of Group-wide risk management assumes participation in the process of the Bank's risk management area organizational units as well as the Credit Committee of the mBank Group (KKG).

<u>Decision-making for credit exposures in the corporate area</u>

Credit decisions are consistent with the accepted internal rules. Levels of decision-making competences are determined by a decision-making matrix. The determination of level of decision-making authority for credit decision is based on EL-rating and total exposure on client/group of affiliated entities. The total exposure includes also exposures on the client/group of affiliated entities in the mBank Group subsidiaries.

<u>Decision-making for credit exposures in the retail banking area</u>

Due to a profile of retail banking clients, the accepted amount of exposure per client and standardisation of products offered to those clients, the credit decision-making process differs from that applied to corporate clients. The decision-making process is automated to a large extent, both in terms of acquiring data on the borrower from internal and external data sources, and in terms of risk assessment by means of scoring techniques and standardised decision-making criteria. The tasks, which are not automated concern mainly the verification of credit documentation and potential derogations when a decision is made with the escalation to the decision-making level in accordance with the applicable rules. In addition, in case of mortgage loans, the value of the collateral is established (standard applications evaluated internally, other with the use of external appraisal report which is additionally evaluated internally).

3.3.2. Credit Policy

Bank manages credit risk based on supervisory requirements, market best practices, bank's own experiences and expertise. Credit policies, established separately for retail banking and corporate banking, play the key role in the credit risk management process. Credit policies include e.g.:

- target customer groups,
- acceptable ratings' levels defined by the expected loss value,
- criteria for acceptance of financed subjects and collaterals,
- rules for mitigating concentration risk,
- rules for selected industries and customers segments.

3.3.3. Collateral accepted

<u>Collateral accepted in the process of granting credit products</u>

The collateral is an important part of the credit policy. The primary role of collateral is to reduce the credit risk of the transaction and provide the Bank with a realistic opportunity to repay receivables. In making a decision about granting a credit risk bearing product, the Bank strives to obtain collateral adequate to the accepted risk. The Bank accepts collateral only upon its assessment and provided it meets the condition of no significant correlation between the credibility of the debtor and the collateral value. Specific types of collateral that are required depend on the risk bearing product, the tenor of the transaction and the risk of the client. The most common collateral accepted are:

- mortgage on real estate,
- registered pledge,
- transfer of receivables (cession of rights),
- monetary deposit,
- guarantees and warranties,
- guarantee deposit or cash blocked,
- transfer of ownership to vehicle.

The value of fixed assets taken as collateral (other than vehicles) is determined on the basis of a valuation prepared by a licensed expert. Valuations submitted to the Bank is verified by a team of specialists located in the risk management area, that verifies the correctness of the market value assumptions and assesses the liquidity of the collateral. Carefully selected, most liquid flats securing retail credits can be valuated using automatically based on historical transactional data.

Each collateral is monitored. Frequency of monitoring depends on the type of collateral and is specified in internal regulations.

In the corporate banking area, in the case of collateral on fixed assets or financial assets, the final value of collateral is brought to a most realistic value (MRV) using Empirical Coverage Factor (ECF), which reflects the pessimistic variant of debt recovery from the collateral through forced sale. Personal collateral is assessed taking into account the financial standing of provider. The Bank assigns the risk parameter PSW (which is an equivalent of Most Realistic Value for fixed assets collateral). In cases when PD parameter of the collateral provider is equal or worse than PD parameter of the debtor, then PSW parameter is zero.

The Bank has a dedicated collateral policy in the area of corporate banking. The most important elements of this policy are:

- indication of collateral preferred and unrecommended,
- recommendations regarding the requirements of collateral in specific situations,
- frequency of collateral monitoring,
- Bank's approach to collateral with MRV parameter equal to zero.

Collateral accepted for transactions in derivative instruments

The Bank manages the risk of derivative instruments. Credit exposures arising from concluded derivative transactions are managed as a part of clients' general credit limits, taking into account potential impact of changes in market parameters on the value of the exposure. Existing master agreements with contractors obligate the Bank to monitor the value of exposure to the client on a daily basis and provide for additional collateral against the exposure to be contributed by the client or mBank in accordance with signed agreements. At the same time, the master agreements provide for early settlement of the transaction with the client in the event of breach of contract. mBank applies an Early Warning Process in order to monitor the usage of limits on derivatives and the Bank's ability to respond to the client when the exposure due to open derivative transactions nears the maximum limit. Moreover, taking into consideration credit risk related to a derivative limit granted to a specific client, the Bank may apply additional collaterals from standard catalogue of collaterals of credit risk-bearing products.

3.3.4. Rating system

The rating system is a key element of the credit risk management process in the corporate banking area. It consists of two main elements:

- customer rating (PD-rating) – describing the probability of default (PD);
- Loss Given Default (LGD) model for non-default portfolio (for default portfolio individual method of estimating recoveries is used). Model consists of components: recoveries from unsecured part of the credit (based on contractual and customer factors, information from financial statement), recoveries from secured part of exposure (based on collateral factors);
- Exposure at Default (EAD) model, which includes Credit Conversion Factor (CCF) model and Limit Utilization (LU) model. The components are based on contract and customer characteristics;
- credit rating (EL-rating) – describing expected loss (EL) and taking into consideration both customer risk (PD) and transaction risk (LGD, Loss Given Default – loss resulting from default). EL can be described as PD*LGD. EL indicator is used mainly at the credit decision-making stage.

The rating produces relative credit risk measures, both as percentages (PD%, EL%) and on a conventional scale from 1.0 to 6.5 (PD-rating, EL-rating) for corporations (sales over PLN 50 million) and SMEs (sales up to and including PLN 50 million). PD rating calculation is a strictly defined process, which comprises seven steps including: financial analysis of annual reports, financial analysis of interim figures, assessment of timeliness of presenting financial statements, analysis of qualitative risks, warning indicators, level of integration of the debtor's group, and additional discretionary criteria. Credit rating based on expected loss (EL) is created by combining customer risk rating and transaction risk rating, which results from the value of exposure (EAD, Exposure at Default) and the character and coverage with collateral for transactions concluded with the client (LGD). LGD, described as % of EAD, is a function of possibly executed value of tangible and financial collateral and depends on the type and the value of the collateral, the type of transaction and the ratio of recovery from sources other than collateral.

The rating system generates the borrower's probability of default directly in the form of a PD ratio, expressed as a percentage (continuous scale). Rating classes are calculated on the basis of procedures of dividing percentage PD into groups based on geometric stepladder. In external reporting, the Bank maps the internal PD rating scale onto external ratings. The table below presents the mapping system.

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Sub-portfolio	1				2			3		4		5			6	7	8	
PD rating	1.0 – 1.2	1.4	1.6	1.8	2	2.2	2.4 – 2.6	2.8	3	3.2 – 3.4	3.6 – 3.8	4	4.2 – 4.6	4.8	5	5.2 – 5.8	No rating	6.1 – 6.5
S&P	AAA	AA+	AA, AA-	A+, A	A-	BBB+	BBB	BBB-	BB+	BB	BB-	B+	B	B-	B-	CCC+ do C	Not applicable	D
	Investment Grade								Sub-investment Grade			Non-investment Grade						Default

The following models comprised by the rating system are used in the retail banking area:

- Loss Given Default (LGD) model, which covers the entire retail portfolio. The ultimate loss level is determined basing on integration of three components:
  - recovery rate for cured cases (based on mean recoveries achieved for cured defaults),
  - recovery rate for non-cured cases (based on contractual factors, bank-client relations and collateral characteristic),
  - probability of cure (based on socio-demographic factors and full product structure of contract owner).

  Estimation of loss level takes place in homogenous segments, taking into account the type of product and the type of collateral. Separate models are in place for non-default and default portfolio;

- Exposure at Default (EAD) model, which includes Credit Conversion Factor (CCF) model, Limit Utilization (LU) model and Prepayments model. The components are based on contract and customer characteristics,
- PD model with a modular structure, which integrates results of scoring cards dedicated to the retail area:
  - application scoring cards (based on socio-demographic factors, factors describing the characteristics of business activity and factors related to the specificity of applied credit products),
  - behavioural scoring cards (based on information on the history of credit and deposit relation with the Bank),
  - internal scoring card based on Credit Information Bureau data (regarding the data about liabilities held outside the Bank).

3.3.5. Monitoring and validation of models

All models of risk parameters applied in mBank, including, i.a. PD models (with all components), LGD models and CCF models are subject to detailed and annual monitoring by modelling units. Moreover, the models are cyclically validated by mBank's independent Validation Unit.

The monitoring includes tests to check discriminatory power of individual models or their components, stability over time, the materiality of individual deviations of empirical values from theoretical values and the impact on portfolio parameters. The modelling unit recalibrates the respective models, i.a. in case of identification of some mismatches. Reports on the performed monitoring/back tests are presented to the model users and the independent Validation Unit.

Validation

Validation is an internal, complex process of independent and objective assessment of model operation, which is consistent with the Recommendation W requirements and - in case of the AIRB method - meets the supervisory guidelines set out in the CRR. The validation rules are set out in general in the Model Management Policy and described in detail in other mBank's internal regulations. The validated models are those that are directly or indirectly used in the assessment of capital adequacy under the AIRB approach, those directly or indirectly used in the process of calculation of provisions under IFRS 9 and others listed in the Bank's List of Models PZM.

In case of AIRB models there is assured an independence of Validation Unit in the organizational structures of the Bank or the Group's subsidiary in relation to the units involved in the model's construction/maintenance, i.e. the model owner and users. The Validation Unit is responsible for the validation in mBank.

The scope of validation performed by the Validation Unit covers the assessment of models, model implementation and their application process.

Depending on the materiality and complexity of the model, as well as the type of validation task to be performed, the validation may be advanced (covers both quantitative and qualitative elements) or basic (mainly focused on the quantitative analyses and selected qualitative elements). The validation results are documented in the validation report containing, in particular, an assessment used for the purpose of approving the model, and recommendations, if any, in the form of precautionary and remedial actions, about the irregularities found.

Validation tasks are performed in accordance with the annual validation plan. Both validation plan and the results of performed validation tasks are approved by the Model Risk Committee.

IRB Method Change Policy

The Bank implemented the IRB Method Change Policy approved by the Management Board. The Policy contains internal rules for the change management within the IRB approach, based on the supervisory guidelines and taking into account the organizational specifics of the Bank. The Policy specifies the stages of the change management process, defines roles and responsibilities, describes in detail the rules of classification of changes, in particular classification criteria based on the guidelines published by the European Central Bank.

3.3.6. Calculating expected credit losses

The method of calculating expected credit losses is consistent with the International Financial Reporting Standards. All the rules and definitions implemented in the Bank that are used in this section are in accordance with Polish banking law and requirements of Polish Financial Supervision Authority.

3.3.6.1 How exposures are classified to stages

The Bank, by implementing International Financial Reporting Standards, classifies credit exposures to stages:

- Stage 1 – exposures for which the risk did not increase significantly since the initial recognition in the loan portfolio,
- Stage 2 – exposures for which, as at the reporting date, a significant deterioration in credit quality was identified compared to the date of their initial recognition,
- Stage 3 – exposures for which impairment triggers were identified during its lifetime in portfolio,
- POCI (purchased or originated credit-impaired asset) – assets identified as credit-impaired at initial recognition.

In the Bank the assignment of exposure to Stage 2 takes place according to the Transfer Logic algorithm, which defines the qualitative and quantitative criteria indicating a significant increase of credit risk, while the classification exposure to the Stage 3 is determined by loss-events.

Once the quantitative or qualitative criteria that were used to classify the exposure in Stage 2 at the reporting date are no longer met (the client and the exposure assigned to him or her no longer meet any of the Transfer Logic qualitative criteria or quantitative criteria), the exposure will be moved from Stage 2 to Stage 1. In case of exposures classified as forborne, the additional condition for reclassification to Stage 1 is the 24-month probation period during which the loan has a performing status.

The exposure may also be transferred from Stage 3 to Stage 2 or to Stage 1 if for each loss-events assigned to debtor, probation period has elapsed and, additionally in case of corporate clients, debtor's assessment carried out after probation period, has not shown that the debtor is unlikely to fully repay its obligations without recourse to realizing security.

Probation period refers to the period in which debtor properly fulfils its obligations, calculated from the moment event leading to loss-event ceases.

Probation period is calculated separately for each loss-event. Probation period is also maintained when the exposure due to which loss-event has occurred has been repaid, written off or sold. Probation period equals:

1. for distressed restructuring – 12 months,
2. for other loss-events – 3 months.

During probation period, the Bank assesses debtor's credit behaviour, and the exit from probation period depends on proper service.

3.3.6.1.1. Significant deterioration of credit quality (classification to Stage 2)

A significant deterioration in credit quality is recognised for the asset concerned on the basis of quantitative and qualitative criteria, with the asset being transferred to Stage 2 once at least one of such qualitative or quantitative criteria is met.

Qualitative criteria are:

1. the number of days of delay in paying the amount due is greater than or equal to 31 days, taking into account materiality thresholds:
    a. the absolute threshold refers to the past due exposure amount and amounts to PLN 400 for retail exposures in polish branch and exposures of Private Banking debtors, registered in corporate systems, CZK 2,500 for retail exposures in the foreign branch of the Bank in Czech Republic,

   b. EUR 100 for retail exposures in the foreign branch of the Bank in Slovakia and PLN 2,000 for exposures in the area of corporate and investment banking,
   c. the relative threshold refers to the ratio of the past due exposure amount to the total balance sheet exposure amount and amounts to 1%,
2. the number of days of delay in paying the amount due od exposure is greater than or equal to 91 days (without materiality thresholds),
3. occurrence of the Forborne performing flag (the client status shows that he or she is experiencing difficulties in repaying the loan commitment, as defined by the Bank),
4. occurrence of the Watch List flag (the Bank's internal process designed to identify corporate clients who are subject to increased monitoring in terms of changes in credit quality, in accordance with the Watch List classification rules adopted by the Bank),
5. deterioration of the risk profile of the entire exposure portfolio, due to the type of product, industry or distribution channel. (for retail customers).

The quantitative criterion of the Transfer Logic is based on a significant deterioration in credit quality, which is assessed on the basis of relative and absolute long-term change in Probability of Default (PD), specified for the exposure at the reporting date, relative to the long-term PD specified on initial recognition. This factor is determined separately for the retail and corporate portfolio within the homogeneous segments in terms of probability of default events and exposure characteristics. Where relative and absolute change in long-term PD exceeds "the transition thresholds", the exposure is moved to Stage 2. An important issue in the process of calculating the credit quality deterioration is initial date recognition consistent in the entire Bank, against which the deterioration of credit quality is examined. Initial date re-recognition is determined for the exposures for which substantial modification of contractual terms took place. Each change of initial recognition date results in recalculation taking into account the new exposure characteristics, initial PD parameter at the new initial recognition date, against which the credit quality deterioration is examined.

3.3.6.1.2. Low credit risk criteria

For exposures whose characteristics are indicative of low credit risks (LCR), expected credit losses are always determined on a 12-month basis. Exposures designated as LCR may not be transferred from Stage 1 to Stage 2, although they can be moved from Stage 1 to Stage 3 upon being recognised as credit-impaired. The Bank applies the LCR criterion to clients from the government and central bank segment with investment grade ratings. The LCR criterion is also applied to clients from segments such as: Banks, Local Government Units and NBFI (Non-Banking Financial Institution). The LCR criteria is not used in the retail banking segment.

3.3.6.1.3. Impairment triggers - corporate portfolio

The list of definite loss events in corporate portfolio:

1. the number of days past due of the principal, interest or fees is over 90 days (in the case of exposures to Banks over 14 days). Number of days past due is calculated at the debtor level and commences when both absolute and relative materiality thresholds have been exceeded, where:
   a. absolute threshold refers to the sum of all overdue amounts related to the debtor's liabilities towards the Bank and amounts to PLN 2,000 for corporate and investment banking debtors and PLN 400 for Private Banking debtors registered in corporate systems;
   b. relative threshold refers to the ratio of all overdue amounts related to the debtor's liabilities towards the Bank to the sum of balance sheet exposures related to given debtor and amounts to 1%;
2. Bank's sale of the credit obligation with material economic loss related to change in creditworthiness of the debtor;
3. the Bank performed distressed restructuring (the materiality threshold from which the Bank considers a diminished financial obligation to be defaulted is 1%);
4. filing by the debtor or filing by the Bank, the parent or subsidiary entity of the Bank a bankruptcy motion against debtor or filing similar motion in respect of credit obligations of the debtor towards the Bank, the parent or subsidiary entity of the Bank;
5. bankruptcy of debtor or acquiring by him a similar legal protection resulting in his evasion of or delay in repayment of credit obligations towards the Bank, the parent or subsidiary entity of the Bank;
6. termination of part or whole credit agreement by the Bank or the beginning of restructuring/collection procedures;
7. fraud (embezzlement) of the debtor;
8. Bank expecting suffering a loss on the client;
9. occurrence of cross default (till 31.12.2021 inclusive the cross default rationale was preceded by an expert assessment by analysts).

In addition Bank identifies loss-events specific to individual categories of entities, and so-called 'soft' loss events, introduced in order to signal situations, which may result in the loss of the debtor's ability to repay loan to the Bank. In the event of their occurrence, an in-depth analysis (taking into account the specificity of the entity's operations) is performed and individual decision on the classification of the exposure to one of the stages is made.

3.3.6.1.4. Impairment triggers - retail receivables

The list of definite loss events in retail portfolio:

1. 1. the number of days past due of the principal, interest or fees is over 90 days. Number of days past due is calculated at the debtor level and commences when both absolute and relative materiality thresholds have been exceeded, where:
   a. absolute threshold refers to the sum of all overdue amounts related to the debtor's liabilities towards the Bank and amounts to PLN 400 for polish branch, CZK 2,500 for the foreign branch of the Bank in Czech Republic and EUR 100 for the foreign branch of the Bank in Slovakia
   b. relative threshold refers to the ratio of all overdue amounts related to the debtor's liabilities towards the Bank to the sum of balance sheet exposures related to given debtor and amounts to 1%;
2. the Bank performed distressed restructuring (the materiality threshold from which the Bank considers a diminished financial obligation to be defaulted is 1%);
3. termination of the agreement by the Bank in the event of breach of the loan agreement by the debtor;
4. obtaining information on the submission of a petition for consumer bankruptcy by the debtor, conducting court proceedings in this matter or a judgment by the court of consumer bankruptcy;
5. obtaining information about the submission of an application by the debtor to initiate or to conduct bankruptcy / restructuring proceedings against the debtor, which, in the Bank's opinion, may result in delay or failure to repay the liability;
6. recognition of the contract as fraudulent;
7. Bank's sale of the credit obligation with material economic loss related to change in creditworthiness of the debtor;
8. uncollectable status of debt;
9. pay out of low down payment insurance;
10. occurrence of cross default.

3.3.6.2. Calculation of expected credit losses

Expected credit losses (ECL) are measured at the level of a single contract or exposure (agreement). In the portfolio approach, expected credit losses are the multiplication of individual for each exposure estimated value of PD, LGD and EAD and the final value of expected credit losses is the sum of expected credit losses in particular periods discounted with the effective interest rate. The calculation of expected credit losses does not use a collective approach (assigning one parameter value to selected portfolios).

If on the reporting date the exposure credit risk did not increase significantly since the initial recognition, expected credit losses are calculated in 12-month horizon (12m ECL) or, in the case of the retail portfolio, the minimum horizon of 12-month horizon and horizon to maturity. If the exposure credit risk increased significantly since the initial recognition (exposure is in the Stage 2), the Bank calculates expected credit losses in the life-time horizon (Lt ECL). The parameters used to calculate an expected credit loss in Stage 1 are identical to those used to calculate a long-term credit loss in Stage 2 for t=1, where 't' stands for the first year of the forecast.

The individual approach concerns all balance sheet and off-balance sheet credit exposures with an impairment in the corporate loan portfolio and Private Banking loan portfolio, which is registered in corporate systems, as well as selected credit exposures with an impairment in the retail micro company loan portfolio (used in the case of exposures with mortgage collateral with a debt balance over PLN 300 thousand and arrears over 1 year). The expected credit losses are calculated as a difference between the value of exposure and the present value of the estimated future cash flows discounted with the effective interest rate, including the costs of debt collection and collateral enforcement. The method of calculating the expected recoveries takes place in scenarios and depends on the Bank's chosen strategy for the client. In case of restructuring strategy, considered scenarios are developed for exposures and assume a significant share of recoveries from the customer's own payments. In case of debt collection strategy, the scenarios are developed for each recovery source (collateral) separately. Bank identifies scenarios per exposure/recovery source, minimum 2 are considered obligatory, provided one of them reflects a partial loss on exposure/recovery source. Weight of scenario results from an expert assessment of the likelihood of scenarios based on the relevant facts of the case, in particular, on existing security and their type, client's financial situation, client's willingness to cooperate, the risks that may occur in the case and micro- and macroeconomic factors.

For the valuation of expected credit losses the Bank uses data contained in the Bank's transaction systems and dedicated tools implemented for the purposes of IFRS 9.

3.3.6.2.1. Use of macroeconomics scenarios in ECL estimation

The Bank is required to set an expected credit loss in a way which meets the expectations for various forward-looking macroeconomic scenarios. In case of portfolio estimation of ECL, the non-linearity factor (NLF) is set in order to adjust the value of an expected credit loss (calculated every month). The values of NLF are used as scaling factors for individual ECLs. The NLF factor is determined separately for retail and corporate segments at least once a year. NLFs are used as scaling factors for individual ECLs that are determined at the level of individual exposures in each segment. NLFs are calculated based on results from three simulation calculations at the same reporting date, which result from relevant macroeconomic scenarios. In particular, NLF for a given segment is calculated as:

1. probability-weighted average of the expected loss from three macroeconomic scenarios ('average estimation') comprising: baseline scenario, optimistic scenario, pessimistic scenario. The weights of scenarios are consistent with probabilities of realization each scenario – 60% for base, 20% for optimistic and 20% for pessimistic,
2. the expected loss determined under baseline scenario (reference estimate).

Simulation calculations, whose results are used to calculate NLF, are carried out on the basis of the same input data on exposure characteristics, but involve different risk parameter vectors, if the macroeconomic expectations defined in the scenarios are such as to affect the value of these parameters.

Additionally, the inclusion of forward-looking information takes place in the models of all three credit risk parameters estimated in the lifetime horizon (Lt PD, Lt EAD, Lt LGD). In the estimates the Bank uses, among others, generally available macroeconomic and financial indicators (GDP, employment in the enterprise sector, unemployment rate, level of export/import, salaries, monetary financial institutions receivables from households), expectations regarding interest rates and exchange rates, as well as changes in property prices, separately for residential and commercial properties.

In case of individual estimation of ECL, the assumed recovery scenarios take into account various macroeconomic and general factors having an impact to the time and amount of recoveries.

3.3.6.2.2. Significant model changes

In 2021 the following significant modifications were introduced to the models used for determination of expected credit losses:

1. update of macroeconomic variables utilized in models accompanied by recalibration of lifetime PD and transfer logic models, especially taking into account the new recommendation R released by The Polish Financial Supervision Authority (regulations have become effective since 01.01.2022). The total impact of these changes, in the context of the expected credit loss amounted to PLN 53 million (positive impact). Additionally, the impact on fair value valuation of non-mortgage loans portfolio was estimated at PLN 7.5 million (positive impact),
2. implementation of dedicated PD lifetime and LGD lifetime models for specialized lending portfolio as well as modifications in the transfer logic algorithm. The implementation of the above mentioned models led to the enlargement of the expected credit loss by PLN 92 million.

3.3.6.2.3. EBA Guidelines on the application of the definition of default (EBA/GL/2016/07)

Starting from 1 January 2021, Group has implemented the definition of default in line with the EBA guidelines from 18 January 2017 (EBA/GL/2016/07).

The Group maintained its current application of the definition of default at the client level, also for retail banking exposures.

The new definition of default is used consistently both for the purposes of the own funds requirements calculation and for estimating impairment and expected credit loss. In line with supervisory expectations, it also plays a meaningful role in internal credit risk management processes.

On the implementation date of the EBA/GL/2016/07 guidelines, the share of NPL exposure in the loan portfolio decreased. On an individual basis the NPL_{REG} ratio (ratio calculated according to EBA guideline) decreased by 0.1 pp (from 3.62% as of 31 December 2020 to 3.52% as of 1 January 2021).

The observed direction of changes is a consequence of introducing for mortgage loans portfolio the obligations from paragraphs 95 – 105 EBA guidelines, concerning the treatment of joint credit obligations. The positive effect of using the above-mentioned regulations is balanced with the negative effect of introducing a continuous method of calculating days past due and by lowering the materiality threshold to PLN 400.

In case of the corporate and investment banking portfolio, no material impact of changes to the EBA/GL/2016/07 guidelines on the NPL level. This is due to the fact that the corporate area in the assessment of the default status is mostly based on an expert judgment approach, that identifies probability of default much earlier than being past due more than 90 days. Thus, changes in the calculation of days past due introduced by the guidelines, had an immaterial impact on the level of NPL in the corporate area.

The impact of the implementation of the EBA/GL/2016/07 guidelines on the costs of credit risk, recognised by the Bank in the income statement amounted to PLN 32.5 million as of 1 January 2021 (negative impact).

In addition, from 1 January 2022, a change in the method of marking the cross default loss event in the area of corporate banking was implemented - there was a switch to automatic marking (expert assessment of analysts was excluded). The change did not have a significant impact on the level of the default portfolio

3.3.6.2.4 The most important changes resulting from the implementation of Recommendation R

On 15 April 2021, the Polish Financial Supervision Authority (KNF) issued Recommendation R on the principles of credit exposure classification, estimation and recognition of expected credit losses and credit risk management, which entered into force on 1 January 2022.

The revised Recommendation R is a set of best practices regarding the classification of credit exposures, estimation and recognition of expected credit losses, in accordance with the accounting and credit risk management policies adopted and applicable at banks. The most important adjustments resulting from the content of the Recommendation covered the following areas:

- definition of default - no need to change the definition of default was identified as part of the adaptation to Recommendation R. The rules of the recommendation influenced the specification of some loss events and the modification of the debt collection process;
- classification into Stages - adjusting the catalogue of criteria of the Transfer Logic algorithm:
  - in terms of quality criteria, the following two elements have been added to the previously used criteria:
    - deterioration of the risk profile of the entire exposure portfolio, due to the type of product, industry or distribution channel – applies to retail banking,
    - a delay in repayment for a given exposure exceeding 90 days from the maturity of a loan / loan instalment - principal or interest or fees, in a situation where the materiality criteria of an overdue credit obligation are not met for a given exposure - applies to retail and corporate banking;
  - in terms of the quantitative criterion, the following changes were made:
    - adjusting the definition of the relative and absolute change of the long-term PD to the requirements of Recommendation R,
    - updating the thresholds of the Transfer Logic, taking into account the long-term perspective (departure from cyclical recalibration of the thresholds based on the current portfolio data; ensuring the constancy of the thresholds expected by the supervisor throughout the life of the contract by determining the threshold based on a long – term sample of data),
    - taking into account the model segmentation compliant with the cross-sections suggested in the R recommendation;
- process changes:
  - extending the approval process of expected credit losses to include the Vice President of the Management Board for Risk Management (CRO),
  - increasing the frequency of back tests of expected credit losses and risk parameters up to quarterly

The most important changes implemented in the scope of expected credit losses and their impact are presented in Note 3.3.6.2.2. The Bank does not expect any significant impacts from the changes in 2022.

3.3.6.3. Credit risk costs coverage of individual sub-portfolios

The tables below show the percentage of the Bank's balance sheet and off-balance sheet items relating to loans and advances, guarantees and letters of credit to individuals, corporate entities a public sector and the coverage of the exposure with credit risk costs for each of the Bank's internal rating categories (the description of rating model is included in Note 3.3.4).

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Portfolio measured at amortised cost

Sub - portfolio	31.12.2021		31.12.2020	
	Exposure (%)	Provision coverage (%)	Exposure (%)	Provision coverage (%)
1	13.24	0.00	12.18	0.01
2	29.09	0.05	36.41	0.09
3	24.07	0.24	12.10	0.23
4	17.77	0.66	27.26	0.59
5	10.25	2.16	6.25	2.80
6	0.41	5.68	0.32	7.36
7	1.67	10.42	1.60	9.27
8	0.78	0.07	0.70	0.18
default	2.72	62.65	3.18	64.11
Total	**100.00**	**2.31**	**100.00**	**2.61**

As at 31 December 2021, 42.33% of the loans and advances portfolio for balance sheet and off-balance sheet exposures is categorised in the top two grades of the internal rating system (31 December 2020: 48.59%).

Portfolio measured at fair value through other comprehensive income

Sub - portfolio	31.12.2021		31.12.2020	
	Exposure (%)	Provision coverage (%)	Exposure (%)	Provision coverage (%)
1	58.32	0.01	47.81	0.02
2	36.15	0.02	45.38	0.07
3	3.35	0.07	4.07	0.27
4	1.30	0.21	1.83	0.77
5	0.35	0.83	0.51	2.36
6	0.06	2.02	0.06	4.44
7	0.29	4.95	0.20	7.32
default	0.18	28.05	0.14	26.42
Total	**100.00**	**0.08**	**100.00**	**0.13**

As at 31 December 2021, 94.47% of the loans and advances is categorized in the top two grades of the internal rating system (31 December 2020: 93.19%).

3.3.7. Fair value for credit assets

If the conditions for the measurement of a credit asset at amortised cost (IFRS 9, par. 4.1.2) are not met, then it is measured at fair value through profit or loss or at fair value through other comprehensive income.

3.3.7.1. Fair value valuation of non-impaired credit assets

The valuation for non-impaired exposure is based on its discounted estimated future cash flows.

Future cash flows are determined taking into account:

- repayment schedule, and in the absence of a schedule (revolving products) - based on a statistical estimation of the annual credit limit utilization in expected behavioural exposure period,
- time value of money, based on risk-free interest rates set in the process of forecasting interest flows,
- cash flows amount and their schedule fluctuations stemming from the option of prepayment (early partial or full repayment of the principal) included in the loan agreement by application of prepayment factors,
- uncertainty of cash flows resulting from credit risk throughout the forecasted lifetime of the exposure by modification of contract flows using multi-year credit risk parameters Lt PD and Lt LGD,
- other factors that would be taken into consideration by the potential exposure buyer (overhead costs and the profit margin expected by market participants) during the process of calibration of the discount rate used in the valuation process.

Due to requirements of IFRS 13 for the exposures for which there are no quotes on an active market, the Bank calibrates the discount rate based on fair value at the date of the initial recognition (i.e. the cost price of exposure). Calibration margin reflects market valuation of costs related to maintaining exposures in the portfolio and market expectations about profit margin realized on similar exposures.

3.3.7.2. Fair value valuation of impaired credit assets

Impaired credit assets are valuated based on expected recoveries. In case of retail exposures the valuation is reflected by LGD parameters, and in case of corporate exposures it refers to individual recovery scenarios.

3.3.8. Repossessed collateral

The Bank classifies repossessed collaterals as assets repossessed for debts and measures them in accordance with the adopted accounting policies described in paragraph 2.20. Assets repossessed for debts classified as assets held for sale shall be put up for sale on an appropriate market and sold at the soonest possible date. The process of selling collaterals repossessed by the Bank is arranged in line with the policies and procedures specified for individual types of repossessed collaterals. In 2021 and 2010, the Bank did not have any repossessed collaterals that were difficult to sell.

3.3.9. Bank Forbearance Policy

<u>Definition</u>

The Bank's forbearance policy is a set of activities relating to renegotiation and restructuring of terms of loan agreements which is defined by internal regulations.

The Bank offers forbearance to assist customers, who are temporarily or permanently 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 contract. These actions may be initiated by the customer or the Bank.

The type of concession offered should be appropriate to the nature and the expected duration of the customer’s financial distress. The Bank’s belief in the customer’s willingness and ability to repay the loan is necessary to conclude an agreement. Prior to granting a concession, an assessment of its impact on improving customer’s ability to repay the loan is carried out.

The Bank renegotiates loan agreements with customers in financial difficulties to maximise possibility of receivables repayment and minimise the risk of default (situation when client fails to fulfil his contractual obligation).

Exposures with modified terms and conditions under forbearance policy (hereinafter - forborne exposures) are subject to regulatory and internal reporting.

<u>Instruments used</u>

The Bank maintains open communication with borrowers in order to detect any financial difficulties as early as possible and to know the reasons of such difficulties. In case of retail borrowers with temporary financial difficulties forbearance solutions focus on temporary reductions of contractual payments among others in form of capital repayments suspension with only interest repayments kept.

For borrowers under long term financial distress extension of contractual repayment schedule may be offered which can include instalments reduction.

For the corporate borrowers in financial distress, as part of the business support process, the mBank offers concessions, starting from participating in debt standstills and concluding on debt restructuring agreements. Debt restructuring agreements may improve Bank’s collateral position by replacing open financing (overdraft) with factoring or invoice discount. Restructuring agreements and they can waive or ease covenants included in the primary agreement (additional conditions included in the primary agreement), if it represents optimal strategy for borrower’s business continuity.

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

- maturity extension/extension of loan duration,
- restructuring (medium or long term refinancing),
- capitalization of interest,
- interest deferrals,
- principal deferrals,
- covenant waiver,
- standstills.

In the year 2021, the Bank continued to offer its clients assistance tools aimed at supporting them in a difficult situation resulting from the ongoing COVID-19 epidemic. The purpose of these tools was to help maintain the financial liquidity of customers by reducing the financial burden in the short term. A detailed description of the support tools, as well as the rules and scale of application can be found in the Note 4.

Risk management

Forbearance measures have been an integral part of mBank's risk management area for many years. Forborne portfolios are subject to regular review and reporting to the area management. The effectiveness of undertaken actions, regularity of restructured transactions' service in respect of types of product and borrower's segment are subject to assessment. The risk analysis of retail forborne portfolio is based on portfolio approach and corporate portfolio analysis is based on individual approach.

In corporate banking, every bank's exposure to borrowers with recognised loss event is classified as default and impairment test is required to be carried out. Every exposure classified as default is being taken over by the specialised unit dedicated to restructuring and debt collection, which defines and implements the Bank's optimal strategy towards the client from the point of view of minimizing losses, i.e. restructuring or debt collection. All exposures to borrowers in financial difficulties with granted concessions (incl. classified as default) have the forborne status. Non-default debtors in financial difficulties, i.e. without recognised loss event, who received the concession (forbearance measures), are subject to close monitoring (Watch List – WL) by all units involved in the loan granting process. Their financial situation is subject to close monitoring and they are under constant review to establish whether any of impairment indicators had materialised.

Bank does not use dedicated models to determine level of portfolio provision and special-purpose provision for forborne portfolio.

Forborne exit conditions – corporate banking area

The Bank ceases to recognise the exposure as forborne if all of the following conditions are met:

- debtor financial situation's analysis showed improvement and the exposure has been recognised as performing and it was reclassified from the nonperforming category,
- at least two years after exposure had been recognised as performing have passed (probation period),
- for the last 12 months of probation period, significant and regular capital or interest payments have been made by the borrower (overdue not exceeding 30 days),
- none of the debtor exposures is overdue more than 30 days at the end of probation period.

Forborne exit conditions – retail banking area

The Bank ceases to recognise the contract as forborne when all of the following conditions are met:

- the contract is recognised as performing,
- at least two years (probation period) have passed since the exposure was recognised as performing,
- at least from the middle of the abovementioned probation period regular capital or interest payments were made (lack of significant delays in repayment longer than 30 days),
- none of the debtor's exposures are overdue more than 30 days and at the same time the due amount does not exceed material threshold defined in internal regulations of the Bank at the end of the 2-year probation period.

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Portfolio characteristic

	31.12.2021			31.12.2020		
	Gross carrying amount	Accumulated impairment	Net value / Fair value	Gross carrying amount	Accumulated impairment	Net value / Fair value
Loans and advances from customers measured at amortised cost	**89 100 112**	**(2 600 966)**	**86 499 146**	**85 760 468**	**(3 031 447)**	**82 729 021**
of which: forborne exposures	1 551 367	(347 027)	1 204 340	1 975 597	(435 714)	1 539 883
of which: defaulted	*750 383*	*(315 400)*	*434 983*	*822 881*	*(395 490)*	*427 391*
Loans and advances from customers measured at fair value through other comprehensive income	**18 206 495**	**(15 241)**	**18 191 254**	**12 531 167**	**(16 154)**	**12 515 013**
of which: forborne exposures	79 618	(2 099)	77 519	33 648	(916)	32 732
of which: defaulted	*6 986*	*(1 533)*	*5 453*	*2 133*	*(500)*	*1 633*
Loans and advances from customers measured at fair value through profit and loss			**991 469**			**1 372 481**
of which: forborne exposures			4 905			102 229
of which: defaulted			*1 703*			*91 266*
Forborne exposures, total			**1 286 764**			**1 674 844**
of which: defaulted			*442 139*			*520 290*

Change of carrying value of forborne exposures	31.12.2021	31.12.2020
As at the beginning of the period	**1 674 844**	**1 415 413**
Outflow from forborne exposures	(830 013)	(304 346)
Inflow to forborne exposures	538 772	680 753
Changes in existing forborne exposures	(96 839)	(116 976)
As at the end of the period	**1 286 764**	**1 674 844**

The analysis carried out for the above reporting periods showed a negligible share of exposures that leave the forbearance status within one year and then return to it.

Forborne exposures by client segment	31.12.2021	31.12.2020
Loans and advances to customers, including:		
Individual customers:	828 659	785 908
of which: housing and mortgage loans to natural persons	*529 098*	*558 642*
Corporate customers	458 105	888 936
Public sector customers	-	-
Total	**1 286 764**	**1 674 844**

Forborne exposures by the type of concession	31.12.2021	31.12.2020
Refinancing	121 464	90 436
Modification of terms and conditions	1 165 300	1 584 408
Total	**1 286 764**	**1 674 844**

Forborne exposures by geographical breakdown	31.12.2021	31.12.2020
Poland	1 228 754	1 626 996
Other countries	58 010	47 848
Total	**1 286 764**	**1 674 844**

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Forborne exposures by days past due	31.12.2021	31.12.2020
Not past due	-	319 960
Past due less than 30 days	966 112	1 118 388
Past due 31 – 90 days	106 106	53 612
Past due over 90 days	214 546	182 884
Total	**1 286 764**	**1 674 844**

Forborne exposures by industry	31.12.2021	31.12.2020
Individual customers	828 659	785 657
Scientific and technical activities	97 022	25 680
Food sector	79 374	101 992
Wood, furniture and paper products	55 699	54 931
Construction	29 091	360 132
Motorisation	28 013	38 384
Real estate	26 983	77 686
Construction materials	23 468	15 846
Other manufacturing	20 870	713
Culture, sport and entertainment	17 787	8 691
Other	79 798	205 132
Total	**1 286 764**	**1 674 844**

3.3.10. Counterparty risk that arises from derivatives transactions

The credit exposure on mBank portfolio to derivative transactions is calculated as the sum of the replacement cost of each transaction (which is its current net present value - NPV) and its estimated future potential exposure (Add-on). Moreover the bank uses credit mitigation techniques such as netting and collateralization. The former is implemented if close-out netting agreement is signed, whereas the latter requires prior Credit Supported Annex (CSA) or suitable clauses in the framework agreement concluded in order to collateralize the exposure. CSA states that the variation margin may be called if current valuation of the portfolio exceeds the predefined level (threshold). Moreover as far as existing agreements are concerned, additional collateral (initial margin, etc.) may also be exchanged. Credit exposure to the derivatives portfolio is adjusted appropriately depending on the collateral being paid or received in accordance with the binding agreements. For the purpose of the counterparty risk calculation only positive NPV at the derivative portfolio level is taken into account.

Credit exposure control is performed through an integrated system in real time. In particular the level of the allocated credit exposure limit usage is monitored on a daily basis. In addition, compliance with restrictions resulting from credit decisions, supervisory regulations and business decisions is controlled. Credit exposure limits are subject to limit decomposition into different products and maturities.

The decomposition of mBank credit exposure of the derivatives portfolio based on the counterparty type is as follows:

- 36.28% banks,
- 12.35% central counterparties (CCP),
- 8.34% financial institutions,
- 43.03% corporates, private banking and others.

The decomposition of mBank credit exposure of the derivatives portfolio based on client type is as follows:

Client type	Credit exposure 2021 (PLN m)	Credit exposure 2020 (PLN m)
Banks CSA	1 444	1 479
Banks uncollateralized	-	-
CCP	491	354
Corporations with limit	1 712	1 890
Non-Bank Financial Institution	332	302
Private Banking	-	(1)
Corporations collateralized and other	1	(13)

** negative exposure means overcollateralization*

Positive NPV (netting included) and inflows and outflows of the collateral for mBank of the derivatives portfolio is depicted below:

(PLN m)	Banks*		CCP*		Corporates and others			
					CSA	w/o CSA**	CSA	w/o CSA**
	2021	2020	2021	2020	2021		2020	
NPV***	22.46	86.95	2.07	29.91	11.62	332.08	57.01	345.70
Collateral received (including collateral posted to custodian)	528.85	275.31	-	-	-	100.52	-	67.60
Collateral posed (including collateral posted to custodian)	463.80	175.35	583.31	307.24	-	-	-	-

** collateral excluding variation margin and default fund (collateral posted to the CCP lest one of its participants defaults)*
*** collateral based on NPV and its estimated future potential exposure,*
**** NPV with variation margin adjustment for banks, CCPs and corporates with CSA*

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

Geographic concentration risk

In order to actively manage the risk of concentration by country, the Bank:

- complies with the formal procedures aimed at identifying, measurement and monitoring this risk,
- complies with the formal limits mitigating the risk by country and the procedures to be followed when the limits are exceeded,
- uses a management reporting system, which enables monitoring the risk level by country and supports the decision-making process related to management,
- maintains contacts with a selected group of the largest banks with good ratings, which are active in handling foreign transactions. On some markets, where the risk is difficult to estimate, the Bank uses the services of its foreign correspondent banks, e.g. Commerzbank, and insurance of the Export Credit Insurance Corporation ("KUKE"), which covers the economic and political risk.

As at 31 December 2021 and as at 31 December 2020 there was no substantial level of geographical concentration in the credit portfolio of mBank. In terms of exposure relating to countries other than Poland there was no substantial share of impaired exposures.

Sector concentration risk

The Bank analyses the sector concentration risk in order to build its corporate portfolio in a safe and effective way and manages industrial concentration risk determining industrial limits.

Limiting covers the sectors in which the Bank's exposure is at least 5% of the total amount of exposures in corporate portfolio at the end of a given reporting period, and sectors indicated by the Corporate and Investment Banking Risk Committee (KRK).

The Bank set industrial limits on a level not higher than:

- 12% of the gross loan corporate portfolio for low risk sectors but not higher than 60% of Tier I;
- 10% of the gross loan corporate portfolio for medium risk sectors but not higher than 50% of Tier I;
- 7% of the gross loan corporate portfolio for high risk sectors but not higher than 35% of Tier I.

In the case when the utilisation of the limit exceeds 90%, activities preventing the exceeding of the limit are implemented; decision in this regard shall be taken by the KRK.

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The table below presents the structure of concentration of mBank S.A. exposures in particular sectors according to the sector division based on the chain value concept, where under one single sector have been focused entities operating activities related to a given market (suppliers, manufacturers, vendors).

The table below presents loans and advances measured at amortised cost, loans measured at fair value through profit or loss, or at fair value through other comprehensive income are not included.

The structure of concentration of carrying amounts of exposure of mBank S.A.

No.	Sectors	Gross value 31.12.2021	%	Gross value 31.12.2020	%
1.	Individual customers	45 192 934	50.72%	44 097 253	51.42%
2.	Rental and leasing activities	12 709 116	14.26%	12 108 583	14.12%
3.	Financial activities	4 198 618	4.71%	3 134 156	3.65%
4.	Real estate	3 891 773	4.37%	4 256 049	4.96%
5.	Construction	2 836 359	3.18%	2 876 417	3.35%
6.	Food sector	2 371 179	2.66%	2 271 547	2.65%
7.	Power and heating distribution	1 574 779	1.77%	1 287 756	1.50%
8.	Construction materials	1 514 260	1.70%	1 395 667	1.63%
9.	Metals	1 493 125	1.68%	1 342 377	1.57%
10.	Chemicals and plastic products	1 476 041	1.66%	1 401 420	1.63%
11.	Motorisation	1 442 714	1.62%	1 328 915	1.55%
12.	Wholesale trade	1 185 696	1.33%	897 279	1.05%
13.	Transport and logistics	1 178 782	1.32%	765 086	0.89%
14.	Retail trade	981 705	1.10%	993 944	1.16%
15.	Wood, furniture and paper products	699 158	0.78%	1 219 083	1.42%
16.	Scientific and technical activities	614 712	0.69%	432 946	0.50%
17.	Fuel	577 381	0.65%	424 659	0.50%
18.	Pharmacy	566 460	0.64%	721 578	0.84%
19.	Agriculture, forestry and fishing	513 602	0.58%	371 280	0.43%
20.	Information and communication	465 497	0.52%	640 110	0.75%

Total Bank's engagement as at 31 December 2021 in sectors described above (apart from natural persons) amounts to 45.22% (31 December 2020: 44.15%).

The risk of investing in sectors being limited by the Bank, i.e. sectors where the Bank's exposures is at least 5% of the corporate portfolio was estimated in line with the principles of classification sectors to limitation, accepted by the KRK in May 2019 and amended in 2021.

The table below presents the risk of limited sectors as at the end of 2021 and 2020

No.	Sectors	31.12.2021	31.12.2020
1.	Financial sector	low	low
2.	Fuels	n/a*	medium
3.	Food sector	medium	medium
4.	Construction	high	high
5.	Motorisation	n/a*	n/a*
6.	Metals	medium	high
7.	Chemistry and materials	n/a*	n/a*
8.	Power	medium	medium

*n/a distincts cases when mBank's exposure is below 5% of corporate portfolio thus sector is not limited

Large exposures concentration risk

The purpose of management of the large exposures' concentration risk is an ongoing monitoring of the level of limits set by the CRR Regulation. In order to ensure safety against the risk of exceeding the regulatory limits in the Bank:

- internal limits, lower than those specified in the CRR Regulation, are set,
- daily monitoring of large exposures is carried out and the participants of the lending and investment processes are immediately informed in the case of internal limits exceeding.

These activities have a direct impact on the Bank's decisions concerning new exposures and the increase of existing exposures.

mBank pays particular attention to the correct identification of the scale of risk of significant credit exposures defined in the Bank's internal regulations. In the case of exceeding specified amount of exposure/limit to a customer/group of affiliated customers identified as bulk risk, the financing requires additional decision of the Bank's Management Board irrespective of the PD-rating and the decision-making level.

Bank monitors large exposures that are subject to exposure limit i.e. exposures after taking into account the effect of the credit risk mitigation (in accordance with art. 401-403 CRR Regulation) and exemptions (art. 390 paragraph 6, Art. 400, Art. 493, paragraph 3 of CRR Regulation), which are equal or exceed 10% of the eligible capital. At the end of 2021 there were no exposure exceeding large exposures limit.

3.5. Market risk

In its operations, the Bank is exposed to market risk, which is defined as a risk resulting from unfavourable change of the current valuation of financial instruments in the Bank's portfolios due to changes of the market risk factors, in particular:

- interest rates;
- foreign exchange rates;
- stock share prices and indices;
- implied volatilities of relevant options;
- credit spreads (to the extent reflecting market fluctuations of debt instruments prices, reflecting credit spread for corporate bonds, and spread between government yield curve and swap curve - for government bonds).

In terms of the banking book, the Bank distinguishes the interest rate risk, which defines as the risk of an adverse change in both the current valuation of the banking book position and the net interest income as a result of changes in interest rates.

3.5.1. Organisation of risk management

In the process of organisation of the market risk management, the Bank follows requirements resulting from the law and supervisory recommendations, in particular the PFSA Recommendations (among others A, C, G and I) and the EBA guidelines, concerning market risk management.

The fundamental principle applied in the organisation of the market risk management in mBank is the separation of the market risk control and monitoring functions from the functions related to opening and keeping open market risk positions.

3.5.2. Tools and measures

For the purpose of internal management, the Bank quantifies exposure to market risk, both for banking and trading book, by measuring:

- the Value at Risk (VaR);
- expected loss under condition that this loss exceeds Value at Risk (ES – Expected Shortfall);
- the Value at Risk in stressed conditions (Stressed VaR);
- economic capital to cover market risk;
- stress tests scenario values;
- portfolio sensitivities to changes of market prices or market parameters (IR BPV – Interest Rate Basis Point Value, CS BPV – Credit Spread Basis Point Value).

The Bank allocates market risk to positions in the banking book, irrespective of the method of presentation of the financial result on those positions used for financial accounting purposes. Market risk measures for interest rate positions in the banking books are determined on the basis of Net Present Value (NPV).

The Bank monitors market risk on a daily basis. For selected risk measures, the measurement is conducted on a weekly basis (Stressed VaR, CS BPV by rating classes) or monthly (economic capital).

For the banking book, the Bank also uses the following measures (described in more detail in the chapter on interest rate risk):

- sensitivity of the economic value of equity (delta EVE);
- sensitivity of net interest income (delta NII);
- repricing gap.

The Value at Risk (VaR) is calculated for each risk factor using the historical method for a 1-day and a 10-day holding period and a 95%, 97.5% and 99% confidence level, assuming a static portfolio. In this method, historical data concerning risk factors for last 254 business days are taken into consideration.

The expected loss under condition that it exceeds Value at Risk (ES) is calculated on the basis of VaR calculation as the average of six worst losses.

The Value at Risk in stressed conditions is a measure of the potential portfolio loss under adverse market conditions that deviate from typical market behaviour. The calculation is analogous to the Value at Risk calculation, the only difference being the period of occurrence of stressed conditions, which is determined on the basis of series of Value at Risk based on successive 12-month windows of risk factors changes since 2007.

The amount of economic capital for market risk in 2021 was determined mainly by the adjustment of the bank’s position to changes in market interest rates. The reversal of the interest rate profile and the shortening of the average maturity of the treasury bonds portfolio resulted in a decrease in this measure, which was offset by the increase of the volatility on the financial markets.

Stress tests are additional measures of market risk, supplementing the measurement of the Value at Risk. They show the hypothetical changes in the current valuation of the Bank's portfolios, which would take place as a result of realisation of the so-called stress scenarios, i.e. market situations at which the risk factors would reach specified extreme values, assuming a static portfolio.

Stress tests consist of two parts: standard stress tests designated for standard risk factors (foreign exchange rates, interest rates, stock prices and their volatility), as well as stress tests, which involve changes in credit spreads. In this way, there was addressed among others, the need for covering in stress tests analysis the independent effect of basis risk (the spread between government yield curve and swap curve), which the Bank is exposed to, due to maintaining the portfolio of Treasury bonds.

IR BPV is a sensitivity measure of the current valuation of the portfolios to an increase in interest rates by 1 basis point, and CS BPV to an increase in credit spread by 1 basis point.

In order to reflect the interest rate risk of the retail and corporate banking products with unspecified interest revaluation dates or rates administered by mBank, the Bank uses the so-called replicating portfolio models. The approach to current accounts takes into account the division of the stable part into the parts sensitive and insensitive to changes in interest rates. The tenor structure adopted for stable parts of the capital and current accounts, insensitive to changes in interest rates, reflects the approved bank’s strategy to stabilise the net interest income. The tenor structure for the stable part of savings accounts is modelled.

The VaR and IR BPV measurement results presented later in the report show the perspective including modelling of stable parts of capital and non-maturity products (NMD products).

The measurement methodology is subject to initial and periodic validation carried out by the Validation Unit and control by the Internal Audit Department.

In order to mitigate market risk exposure the limits are established on:

- VaR at 975% confidence level for a 1-day holding period;
- stress tests results;
- sensitivity measures IR BPV and CS BPV.

Decisions regarding the values of market risk limits are taken by:

- the Supervisory Board (with respect to mBank Group’s portfolio);
- the Management Board (with respect to mBank’s portfolio);
- the Financial Markets Risk Committee (with respect to the business units’ portfolios.

3.5.3. Market risk profile

Value at Risk

In 2021, the market risk exposure, as measured by the Value at Risk (VaR for a 1-day holding period, at 97.5% confidence level), was in relation to the established limits on moderate level.

The table below presents VaR and Stressed VaR for the mBank's portfolio:

PLN thousand	2021		2020	
	31.12.2021	Mean	31.12.2020	Mean
VaR IR	15 825	11 024	11 091	9 365
VaR FX	2 095	3 276	2 196	1 390
VaR EQ	-	-	-	-
VaR CS	85 154	61 846	76 296	52 497
VaR	**79 934**	**59 744**	**66 191**	**46 512**
Stressed VaR	**136 733**	**153 259**	**152 842**	**130 963**

VaR IR – interest rate risk (without separate credit spread)
VaR FX – currency risk
VaR EQ – equity risk
VaR CS – credit spread risk

The measurement results are presented taking into the account the estimation of stable parts of capital and current accounts, invulnerable to interest rate fluctuation.

The Value at Risk (VaR) was largely influenced by the portfolios of instruments sensitive to the interest rates and the separate credit spread - mainly the portfolios of the treasury bonds (in the banking and trading books) and positions resulting from interest rate swap transactions. The increase of VaR value was caused by increased volatility on the financial markets.

Sensitivity measures

The table presents the values of IR BPV and CS BPV (+1 b.p.) for the mBank's portfolio, broken down into the banking and trading books:

PLN thousand	IR BPV		CS BPV	
	31.12.2021	31.12.2020	31.12.2021	31.12.2020
Banking book	1 302	(1 195)	(11 499)	(13 739)
Trading book	112	(2)	(209)	(205)
Total	**1 414**	**(1 197)**	**(11 708)**	**(13 944)**

The credit spread sensitivity (CS BPV) for mBank's banking book, results in ca. 50% from the positions in debt securities valued at amortised cost. Changes in market price have no impact on the revaluation reserve or the income statement for these positions.

Economic capital for market risk

The Bank calculates economic capital to cover market risk with taking into account the modelling of stable parts of capital and current accounts. As of the end of 2021 economic capital for market risk for mBank amounted to PLN 1 238.7 million (at the end of 2020: PLN 1 202.8 million).

The amount of economic capital for market risk in 2021 was determined mainly by the change in the interest rate position. Reversing the interest rate profile and shortening the average maturity of the treasury bonds portfolio resulted in a decrease of this measure, which was neutralized by the increase of the volatility on the financial markets.

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3.6. Currency risk

The Bank is exposed to changes in currency exchange rates due to its financial assets and liabilities other than PLN. The following tables present the exposure of bank to currency risk as at 31 December 2021 and 31 December 2020.

The tables below present assets and liabilities of the Bank at balance sheet carrying amount for each currency.

31.12.2021	PLN	EUR	USD	CHF	CZK	OTHER	TOTAL
ASSETS							
Cash and cash balances with central banks	8 357 978	3 356 377	75 411	1 029	285 356	11 457	12 087 608
Financial assets held for trading and hedging derivatives	1 362 403	1 200 628	16 052	2	1 719	370	2 581 174
Non-trading financial assets mandatorily at fair value through profit or loss, including:	1 118 195	1 786	100 782	-	300	-	1 221 063
Equity instruments	*146 380*	*1 786*	-	-	*300*	-	*148 466*
Debt securities	-	-	*81 128*	-	-	-	*81 128*
Loans and advances to customers	*971 815*	-	*19 654*	-	-	-	*991 469*
Financial assets at fair value through other comprehensive income	53 565 145	289 926	288 845	-	18 741	-	54 162 657
Financial assets at amortised cost	73 896 734	17 099 218	1 307 199	9 386 383	12 510 502	126 941	114 326 977
Debt securities	*16 632 915*	-	-	-	-	-	*16 632 915*
Loans and advances to banks	*3 778 784*	*1 413 867*	*209 785*	*1 727*	*5 758 863*	*31 890*	*11 194 916*
Loans and advances to customers	*53 485 035*	*15 685 351*	*1 097 414*	*9 384 656*	*6 751 639*	*95 051*	*86 499 146*
Fair value changes of the hedged items in portfolio hedge of interest rate risk	1 055 478	-	-	-	-	-	1 055 478
Investments in associates	2 357 068	-	-	-	-	-	2 357 068
Non-current assets and disposal groups classified as held for sale	31 247	-	-	-	-	-	31 247
Intangible assets	1 110 175	12	-	-	1 292	-	1 111 479
Tangible assets	1 169 804	9 090	-	-	25 786	-	1 204 680
Investment properties	127 510	-	-	-	-	-	127 510
Current income tax assets	-	-	-	-	28 077	-	28 077
Deferred income tax assets	719 446	-	-	-	1 878	-	721 324
Other assets	645 923	143 657	2 306	3 716	61 875	-	857 477
TOTAL ASSETS	**145 517 106**	**22 100 694**	**1 790 595**	**9 391 130**	**12 935 526**	**138 768**	**191 873 819**
LIABILITIES							
Financial liabilities held for trading and hedging derivatives	821 951	1 208 277	14 055	-	-	318	2 044 601
Financial liabilities measured at amortised cost, including:	123 444 184	25 869 036	4 928 451	6 472 682	11 062 474	857 244	172 634 071
Amounts due to banks	*2 296 390*	*426 383*	*30 132*	*667 062*	-	*34*	*3 420 001*
Amounts due to customers	*119 611 000*	*21 039 287*	*4 898 319*	*2 437 701*	*11 062 474*	*857 210*	*159 905 991*
Debt securities issued	*25 047*	*4 403 366*	-	*2 255 210*	-	-	*6 683 623*
Subordinated liabilities	*1 511 747*	-	-	*1 112 709*	-	-	*2 624 456*
Fair value changes of the hedged items in portfolio hedge of interest rate risk	-	-	-	-	110 033	-	110 033
Liabilities classified as held for sale	7 425	-	-	-	-	-	7 425
Provisions	701 091	31 627	880	105 110	985	5	839 698
Current income tax liabilities	25 845	1 840	-	-	26 782	-	54 467
Deferred income tax liabilities	-	89	-	-	-	-	89
Other liabilities	2 315 210	164 635	200 073	7 621	75 885	38 188	2 801 612
TOTAL LIABILITIES	**127 315 706**	**27 275 504**	**5 143 459**	**6 585 413**	**11 276 159**	**895 755**	**178 491 996**
Net on-balance sheet position							
Loan commitments and other commitments	**18 201 400**	**(5 174 810)**	**(3 352 864)**	**2 805 717**	**1 659 367**	**(756 987)**	**13 381 823**
Guarantees, banker's acceptances, documentary and commercial letters of credit	27 996 744	2 145 537	284 189	3	638 255	2 538	**31 067 266**
Financial liabilities held for trading and hedging derivatives	5 050 743	1 977 365	493 112	146	1 839	33 201	**7 556 406**

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31.12.2020	PLN	EUR	USD	CHF	CZK	OTHER	TOTAL
ASSETS							
Cash and cash balances with central banks	3 399 601	291 572	53 085	3 244	178 384	13 412	3 939 298
Financial assets held for trading and hedging derivatives	1 915 648	444 566	67 746	57 654	3 718	4 203	2 493 535
Non-trading financial assets mandatorily at fair value through profit or loss, including:	1 400 227	89 965	94 837	-	-	-	1 585 029
Equity instruments	*135 289*	*1 191*	-	-	-	-	*136 480*
Debt securities	-	-	*76 068*	-	-	-	*76 068*
Loans and advances to customers	*1 264 938*	*88 774*	*18 769*	-	-	-	*1 372 481*
Financial assets at fair value through other comprehensive income	46 953 709	462 708	114 762	-	200 433	-	47 731 612
Financial assets at amortised cost	68 410 889	15 909 479	954 504	12 663 013	11 461 886	127 595	109 527 366
Debt securities	*15 952 501*	-	-	-	-	-	*15 952 501*
Loans and advances to banks	*3 249 289*	*1 091 745*	*151 508*	*1 455*	*6 311 745*	*40 102*	*10 845 844*
Loans and advances to customers	*49 209 099*	*14 817 734*	*802 996*	*12 661 558*	*5 150 141*	*87 493*	*82 729 021*
Investments in associates	2 202 524	2 398	-	-	-	-	2 204 922
Intangible assets	1 013 586	25	-	-	135	-	1 013 746
Tangible assets	1 215 682	6 183	-	-	24 631	-	1 246 496
Current income tax assets	-	-	-	-	22 826	-	22 826
Deferred income tax assets	204 352	-	-	-	2 572	-	206 924
Other assets	647 078	39 611	4 837	345	63 229	18 153	773 253
TOTAL ASSETS	**127 363 296**	**17 246 507**	**1 289 771**	**12 724 256**	**11 957 814**	**163 363**	**170 745 007**
LIABILITIES							
Financial liabilities held for trading and hedging derivatives	885 097	489 900	35 062	-	-	4 315	1 414 374
Financial liabilities measured at amortised cost, including:	104 636 057	23 334 613	4 871 216	6 169 619	9 614 564	689 743	149 315 812
Amounts due to banks	*1 100 838*	*842 827*	*40 829*	*639 714*	-	*78*	*2 624 286*
Amounts due to customers	*101 988 481*	*18 362 618*	*4 830 387*	*2 292 319*	*9 614 564*	*689 665*	*137 778 034*
Debt securities issued	*35 016*	*4 129 168*	-	*2 170 981*	-	-	*6 335 165*
Subordinated liabilities	*1 511 722*	-	-	*1 066 605*	-	-	*2 578 327*
Fair value changes of the hedged items in portfolio hedge of interest rate risk	48 638	-	-	-	10 986	-	59 624
Provisions	467 758	43 365	1 972	883	1 152	81	515 211
Current income tax liabilities	199 085	-	-	-	25 944	-	225 029
Deferred income tax liabilities	-	89	-	-	-	-	89
Other liabilities	2 201 758	161 170	291 812	1 946	75 882	14 608	2 747 176
TOTAL LIABILITIES	**108 438 393**	**24 029 137**	**5 200 062**	**6 172 448**	**9 728 528**	**708 747**	**154 277 315**
Net on-balance sheet position	**18 924 903**	**(6 782 630)**	**(3 910 291)**	**6 551 808**	**2 229 286**	**(545 384)**	**16 467 692**
Loan commitments and other commitments	27 882 533	2 327 450	261 282	2	592 029	24	**31 063 320**
Guarantees, banker's acceptances, documentary and commercial letters of credit	5 694 104	1 866 706	468 673	20	1 893	41 579	**8 072 975**

3.7. Interest rate risk

In the process of management of interest rate risk in the banking book Bank ensures independence of risk identification, measurement, monitoring and control functions from activity related to risk-taking functions.

Interest rate risk of the banking book is the risk resulting from the exposure of the Bank's interest income and capital to the adverse impact of interest rates movements. Following recommendations of the Polish Financial Supervisory Authority (PFSA), in particular Recommendation G, and EBA guidelines (EBA/GL/2018/02) the Bank monitors the banking book structure in terms of repricing risk, basis risk, yield curve risk and customer option risk.

The basic measures of interest rate risk in the banking book are:

- the repricing gap (the difference between assets, liabilities and off-balance sheet banking book positions, measured in defined repricing buckets, based on repricing date of the interest rate sensitive products);
- sensitivity of net interest income (delta NII), i.e. the difference of net interest income between the base and alternative scenarios, assuming different possibilities of shifting the profitability curve and changes in the balance sheet structure;
- sensitivity of the economic value of equity (delta EVE), i.e. the difference in the present value of cash flows between the base scenario and the alternative scenario, assuming various shifts in the profitability curve, including those in line with the EBA guidelines on the regulatory outlier test (SOT).

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The interest rate risk on the banking portfolio is hedged and managed based on the repricing gap limits for the entire portfolio, including separately for significant currencies, dNII limit, SOT, limits for market risk – imposed on Value at Risk (VaR), stress tests as well as IR BPV and CS BPV. Reports on the above measures are prepared on a daily basis.

The Bank calculates on monthly basis and reports quarterly the level of sensitivity of net interest income calculated for 22 scenarios of interest rate changes, taking into account changes in the level of the yield curve (including parallel curve shift, its steepening and flattening) and the base risk, both in static, dynamic and outflow balance over a 5-year horizon. The main assumptions used to calculate the measure are:

- the use of customer rates, decomposed into a trade margin and market rate;
- for products without a specific maturity date, assigning repricing dates based on the replicating portfolio model;
- limits applied to the level of lower and upper clients interest rate, resulting from legal provisions;
- behavioural options including deposit termination and loan prepayments are calculated on the basis of the historical average.

In addition, the Bank calculates on a monthly basis and reports quarterly the sensitivity of the economic value of capital for 14 scenarios (including regulatory shock scenarios described in the EBA guidelines) taking into account changes in the level and slope of the yield curve as well as currency and credit spreads, broken down into values in currencies together and separately for material currencies based on the following assumptions:

- taking into account cash flows from interest rate sensitive assets and liabilities, including commercial margins;
- use of risk-free curves, except for debt securities, in the case of which the curve includes credit spread;
- exclusion of capital from liabilities;
- run-off balance sheet.

In the case of calculated sensitivity measures of net interest income the Bank takes into account the risk of partial or total early repayment of the loan before its maturity/ withdrawal of funds from term accounts before their maturity. The prepayment/withdrawal algorithm used is based on the historical average and its result is the annual prepayment rate/deposits withdrawal rate by major currencies (PLN, CHF, EUR, CZK) and the portfolio of retail and corporate clients. As at 31 December 2021, the percentage annual prepayments estimated for the purposes of the above-mentioned risk measures were as follows: retail clients (8%), corporate clients (10%) as at 31 December 2020: 9% and 18% respectively). The Bank aims at stabilisation of the net interest income (NII), optimisation of income statement and EVE changes within the accepted risk appetite.

As at 31 December 2021 and 31 December 2020, the sensitivity of net interest income (based on a static balance sheet over a 12-month horizon) and the economic value of capital (for the outflow balance) in shock scenarios for interest rate risk are presented in the table below:

	Δ NII		Δ EVE	
	31.12.2021	31.12.2020	31.12.2021	31.12.2020
Sudden parallel up by 200 bp	598 194	284 008	(378 318)	(880 873)
Sudden parallel down by 200 bp	(1 371 483)	(862 460)	404 786	974 577
Parallel shock up	575 424	279 017	(487 238)	(893 384)
Parallel shock down	(1 728 614)	(1 054 944)	524 708	986 934
Steepened shock	(1 123 731)	(565 329)	80 861	33 025
Flattener shock	166 404	(156 800)	(175 404)	(181 862)
Short rates shock up	324 095	(67 690)	(328 980)	(439 965)
Short rates shock down	(2 026 454)	(969 131)	343 495	174 392
Maximum	(2 026 454)	(1 054 944)	(487 238)	(893 384)
Tier I Capital	13 529 356	15 049 829	13 529 356	15 049 829

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	Δ NII*	
	31.12.2021	31.12.2020
Parallel up by 100 bp	**351 795**	**153 348**
PLN	192 007	37 971
USD	33 153	1 375
EUR	78 538	80 871
CHF	14 439	15 810
CZK	33 528	17 143
others	130	178
Parallel down by 100 bp	**(715 290)**	**(537 950)**
PLN	(509 030)	(384 436)
USD	(38 009)	(9 662)
EUR	(112 241)	(107 288)
CHF	2 389	18 254
CZK	(51 239)	(54 034)
others	(7 160)	(784)

The increase in delta NII and the decrease in delta EVE in most scenarios result from the adjustment of the Bank's position to the market situation. Taking into account the expected growth of the inflation, the interest rate increases planned by the Monetary Policy Council and the expected market interest rates, at the end of 2021 the Bank kept a much larger part of its assets in instruments with a variable interest rate. Moreover, the sensitivity of delta NII was influenced by the updated assumptions concerning the pricing policy of deposit accounts. This measure is calculated taking into account specific methodological assumptions, including balance sheet stability, historical margins for rolled products, price elasticity, adequate in a given market situation, which means that measure should not be treated as a forecast of the net interest income, but a sensitivity measure for a given moment in certain conditions.

Changes of delta NII and delta EVE were caused also by increase of balance sheet total which was observed between 2020 and 2021.

mBank S.A. interest rate risk

The following tables present the Bank’s exposure to interest rate risk. The tables present the Bank’s financial instruments at carrying amounts, categorised by the earlier of: contractual repricing or maturity dates.

31.12.2021	Up to 1 month	1-3 months	3-12 months	1-5 years	More than 5 years	Non-interest bearing	Total
Assets							
Cash and balances with the Central Bank	3 244 327	-	-	-	-	8 843 281	**12 087 608**
Loans and advances to banks	8 667 895	2 412 519	114 497	-	-	5	**11 194 916**
Debt and equity securities and investments in subsidiaries	10 573 823	1 911 593	12 848 084	22 503 610	5 522 422	2 505 533	**55 865 065**
Loans and advances to customers	62 158 195	32 672 177	2 444 642	7 588 013	459 283	399 985	**105 722 295**
Other assets and derivative financial instruments	107 871	58 547	63 589	78 458	9 360	2 406 315	**2 724 140**
Total assets	**84 752 111**	**37 054 836**	**15 470 812**	**30 170 081**	**5 991 065**	**14 155 119**	**187 594 024**
Liabilities							
Amounts due to banks	2 686 368	559 921	170 353	-	-	3 359	**3 420 001**
Amounts due to customers	151 181 421	3 320 520	1 710 124	2 654 947	1 627	1 037 352	**159 905 991**
Debt securities issued	25 047	-	2 936 007	1 450 742	2 271 827	-	**6 683 623**
Subordinated liabilities	758 076	1 112 710	753 670	-	-	-	**2 624 456**
Other liabilities and derivative financial instruments	81 384	146 529	127 133	135 706	19 190	4 251 497	**4 761 439**
Total liabilities	**154 732 296**	**5 139 680**	**5 697 287**	**4 241 395**	**2 292 644**	**5 292 208**	**177 395 510**
Total interest repricing gap	**(69 980 185)**	**31 915 156**	**9 773 525**	**25 928 686**	**3 698 421**		

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31.12.2020	Up to 1 month	1-3 months	3-12 months	1-5 years	More than 5 years	Non-interest bearing	Total
Assets							
Cash and balances with the Central Bank	854 901	-	-	-	-	3 084 397	**3 939 298**
Loans and advances to banks	8 592 250	2 157 549	17 884	65 060	-	13 101	**10 845 844**
Debt and equity securities and investments in subsidiaries	4 651 567	3 344 171	18 629 374	18 485 456	6 758 200	2 417 470	**54 286 238**
Loans and advances to customers	64 567 809	24 943 283	1 764 249	4 932 247	289 261	307 568	**96 804 417**
Other assets and derivative financial instruments	198 361	173 579	186 740	272 601	28 646	1 519 291	**2 379 218**
Total assets	**78 864 888**	**30 618 582**	**20 598 247**	**23 755 364**	**7 076 107**	**7 341 827**	**168 255 015**
Liabilities							
Amounts due to banks	2 619 676	-	-	-	-	4 610	**2 624 286**
Amounts due to customers	126 548 447	5 171 351	3 516 294	1 085 820	591 984	864 138	**137 778 034**
Debt securities issued	-	35 017	1 977 493	4 322 655	-	-	**6 335 165**
Subordinated liabilities	758 184	1 066 605	753 538	-	-	-	**2 578 327**
Other liabilities and derivative financial instruments	100 210	172 186	220 697	198 722	23 891	3 445 844	**4 161 550**
Total liabilities	**130 026 517**	**6 445 159**	**6 468 022**	**5 607 197**	**615 875**	**4 314 592**	**153 477 362**
Total interest repricing gap	**(51 161 629)**	**24 173 423**	**14 130 225**	**18 148 167**	**6 460 232**		

3.8. Liquidity risk

Sources of liquidity risk

The liquidity risk is understood as the risk of failure to fund assets and meet payment obligations arising from balance sheet and off-balance sheet items owed by the Bank in a timely manner and at a market price.

The reasons for liquidity risk may appear with respect to assets, liabilities and can also arise from off-balance sheet commitments.

As regards assets, their main sources of liquidity risk are market liquidity risk and untimely repayments of loans. Market liquidity risk is a threat of complete or partial impossibility of liquidating the assets held, or the possibility of selling these assets only at an unfavourable price.

As regards liabilities, the risks posed by funding and withdrawal of funds by the clients are the most common source of the liquidity risk. The former is a type of risk in terms of which, should the crisis occur, funding can be acquired only at a higher price, and in an extreme situation, it is not possible to acquire funding or renew existing. The latter is a type of threat associated with uncertainty as to the behaviour of clients whose decisions (for instance, about withdrawal of deposited funds) may weaken the Bank's ability to service its current financial obligations.

A source of risk for off-balance sheet liabilities is a risk posed by clients' behaviour and unexpected drawdown of granted lines. It also concerns the use of intraday and overdraft lines by custody and corporate clients. Materialisation of such a risk may be experienced as severe especially in the case of high concentration of commitments. In respect of derivative transactions concluded with CSA agreements (Credit Support Annex) or settled by CCP, liquidity risk can materialize in consequence of adverse and severe changes in market conditions resulting in sudden decrease in valuation of derivative instruments and related to necessity of pledging the collateral.

Daily operations of the Bank require settlements of various payment operations. Such activity generates high level of liquidity needs during a business day.

Taking into account the mBank Group the liquidity risk is also identified as a possibility of unexpected growth in significant liquidity needs of subsidiaries of mBank. A centralised approach to the management of the Group's financing was introduced in order to increase the effectiveness of the used liquidity resources and to ensure better tenor match of financing with assets.

Liquidity risk may appear as a result of usage of inappropriate models in liquidity analysis (e.g. deposit base stable part model), which may lead to underestimation of liquidity risk. It is monitored by verification and back-testing models pursuant to the Model Management Policy.

Organization of risk management

In order to ensure that the liquidity risk management process is effective, the Management Board of the Bank lies down an adequate organizational structure and delegates powers to dedicated units and Committees. Liquidity risk management is conducted based on three lines of defence.

Liquidity risk management aims at ensuring and maintaining the Bank's and the Group's ability to fulfil both current and future liabilities taking into account the cost of liquidity. The liquidity management process consists of procedures that aim at identification, measurement, controlling, monitoring, reducing and defining the acceptable level of exposure to risks. This process can be divided into two main elements in the operational sense: the part involving all forms of liquidity management and the part of controlling and monitoring liquidity risk.

The objective of liquidity risk management is to ensure and maintain the Bank's ability to fulfil both current and future commitments. The Bank achieves this objective by diversifying stable funding sources in terms of client's groups (from whom it acquires deposits), products and currencies, and at the same time, maintains liquidity buffer and optimizes its balance sheet in terms of profitability. Long-term activities of mBank in this scope are carried out taking into account conditions on funding capacity and business profitability.

In 2021, the liquidity situation was monitored and Bank`s liquidity remained on a very high level. This year was a continuation of the year 2020 in terms of economic conditions (COVID-19 pandemic), which resulted in a significant increase in balances on customer accounts with a twice lower increase in the dynamics of lending. This situation had a direct impact on the strengthening of the liquidity position.

The internal liquidity adequacy assessment process (ILAAP)

In order to review the liquidity risk management system in the Bank and the Group, the ILAAP process was developed. As part of this process all elements of the liquidity risk management system are subject to review including:

- liquidity risk management strategy;
- stress tests;
- liquidity contingency plan;
- liquidity buffer;
- intraday liquidity risk management;
- early warning system;
- identification and measurement of liquidity risk;
- reporting system.

The review is performed annually. The conclusions of the conducted review serve for further improvement and development of the liquidity risk management.

Tools and measures used in measuring liquidity risk

As part of liquidity risk management, a range of risk measures are being analysed. The basic measure is mismatch gap. It covers all the assets, liabilities and off-balance sheet items of the Bank in all the currencies and time-bands set by the Bank. In 2021, the Bank held liquidity surplus, adequate to the Bank's business activity and current market situation, in the form of a portfolio of liquid treasury and money market securities that may be pledged or sold at any time without any considerable loss in value.

In accordance with PFSA Resolution No. 386/2008 on establishing liquidity measures binding on banks and in accordance with Commission Delegated Regulation (EU) No 2015/61 of 10 October 2014 amended by the Commission Delegated Regulation (EU) 2018/1620 of 13 July 2018, effective since 30 April 2020 and Commission Implementing Regulation (EU) 2021/451 of 17 December 2020 the Bank calculates the supervisory liquidity measures. As in 2020, in 2021 the supervisory limits were not exceeded. Moreover the Bank conducts an in-depth analysis of long-term liquidity and sets internal limits (management action triggers) on involvement in long-term assets. Internal limits and appropriate buffers are also imposed on supervisory measures. Relevant analysis of the stability and structure of the funding sources, including the core and concentration level of term deposits and current accounts are performed. Additionally, the Bank analyses the volatility of balance sheet and off-balance sheet items, in particular open credit line facilities and current accounts and overdrafts limits utilisation.

The ongoing analysis covers liquidity under normal and stress conditions, but also on the assumption of a potential liquidity loss. In order to determine the Bank's resistance to major unfavourable events, the Bank conducts scenario analyses covering extreme assumptions on the operation of financial markets and/or behavioural events relative to the Bank's clients. For this purpose stress test scenarios are regularly calculated in the short- and long-term, in the bank stress, market stress and combined scenarios. In addition a reverse stress test for liquidity risk is performed in the Bank on annual basis and an intraday liquidity crisis scenario on a monthly basis. Liquidity stress tests are used in the Bank for operational management of liquidity risk.

The Bank has also adequate procedures in case mBank is threatened with financial liquidity loss. Base on severity of risk factors and the degree of the threat of financial loss relevant actions are defined either in the Contingency Plan in case of a threat of losing financial liquidity by mBank Group (Contingency Plan) or in the Recovery Plan mBank Group (Recovery Plan). Scenarios used in both plans are consistent with the above stress tests.

Execution of the strategy of ensuring liquidity of the Bank consists in active management of balance sheet structure of future cash flows and keeping liquidity reserves adequate to the liquidity needs, resulting from the activity and structure of the balance sheet of the Bank, obligations to subsidiaries and the current market situation as well as the demand for liquid assets, resulting from the conducted stress tests. For this purpose the Bank keeps a surplus of liquid and unencumbered assets constituting the liquidity reserves, for which there is a possibility of pledging, transaction on repo market or selling at any time without significant loss in value. Liquidity reserves were composed mainly of the Polish government debt securities in PLN and EUR, Polish government bills, bills issued by the National Bank of Poland in PLN, the Czech Republic's Government debt securities in CZK, bills issued by Czech National Bank in CZK and debt securities issued by European Investment Bank in PLN. Values of these reserves amounted to:

Value of liquidity reserves (in PLN million)	
31.12.2021	31.12.2020
54 097	51 088

In order to support the process of liquidity risk management, a system of early warnings indicators and recovery indicators was developed in the Bank. It is composed of indicators monitoring the level of regulatory and internal limits and additionally, indicators monitoring significant changes of market factors, as well as changes in the Bank's balance sheet structure. Exceedance of thresholds by defined indicators may be a trigger for the launch of the Contingency Plan or the Recovery Plan.

Due to the use by the Bank of FX swap and CIRS instruments to convert surpluses in local currencies into foreign currencies, internal limits are in place on the use of these instruments. Moreover, in order to limit the concentration in FX swaps, the amounts obtained in such transactions are monitored in monthly time bands up to 1 year.

Other measures of liquidity risk are calculated and reported in the Bank as follows:

- concentration of funding sources;
- stability of deposit base;
- early withdrawals of deposits;
- ratio of long-term funding for the real estate market;
- liquidity risk concentration within off-balance sheet positions related to related to financial and guarantee liabilities.

The Bank includes product's liquidity in its liquidity risk management framework. It is reflected in terms of measuring market liquidity of Treasury bonds, which make up liquidity reserves. The analysis is performed on monthly basis and takes account of market liquidity determinants such as: market turnover, order book depth, purchase/sale transaction spread and issue volume. The measurement of market liquidity is reflected in internal liquidity measures, where the scenario's structure provides for liquidating Treasury bonds held by the Bank in line with market trading in particular series of bonds. A similar check is carried out in the context of the market potential of pledging particular bond series.

The measurement, limiting and reporting the liquidity risk

At the Bank, there is a reporting process of liquidity risk. It covers both daily information delivery to entities engaged in operational management of liquidity risk and entities controlling liquidity risk management on operational level, as well as regular reporting to higher management levels for the purpose of making strategic decisions on liquidity risk.

Daily reporting covers:

- regulatory measures;
- liquidity gaps for mBank, the mBank Group and the material subsidiaries from liquidity risk perspective with the utilization of limits imposed on these measures;
- intraday liquidity;
- other internal liquidity risk measures.

The following measures are reported weekly:

- early warnings indicators (EWI),
- recovery indicators.

Monthly reporting covers:

- regulatory measures and internal liquidity measures to the Management Board members and Financial Markets Risk Committee (KRF);
- regulatory measures, internal liquidity measures and forecasts of liquidity measures based on business development forecasts to the Capital, Assets and Liabilities Committee of the mBank Group (CALCO).

Regulatory measures and internal liquidity measures are reported on a quarterly basis to the Bank's Supervisory Board.

For the purpose of current monitoring of liquidity, the Bank establishes values of realistic, cumulated gap of cash flows. The realistic gap is calculated on the basis of contractual cash flows (Note 3.8.1). Mainly cash flows in portfolios of non-banking customers' deposits, overdrafts and term loans are amended. In the calculation of the liquidity measures the Bank takes into account the possibilities of raising the funds by selling or pledging the debt securities from the Bank's liquidity reserves.

In the LAB methodology, the LAB Base Case measure is the primary management measure and it is also used for limiting the liquidity gap in particular foreign currencies.

Value of realistic cumulative gap of cash flows mismatch (in PLN million)				
Time bucket	LAB Base Case - 31.12.2021		LAB Base Case - 31.12.2020	
	bucket	cumulative	bucket	cumulative
up to 1 working day	33 864	33 864	22 968	22 968
up to 3 working days	2 267	36 132	3 038	26 006
up to 7 calendar days	515	36 647	(124)	25 882
up to 15 calendar days	(1 476)	35 171	398	26 280
up to 1 month	(1 795)	33 376	1 294	27 574
up to 2 months	(775)	32 600	3 021	30 595
up to 3 months	(502)	32 099	(184)	30 411
up to 4 months	(158)	31 940	195	30 606
up to 5 months	(531)	31 410	195	30 801
up to 6 months	(264)	31 146	(91)	30 710
up to 7 months	(260)	30 887	60	30 770
up to 8 months	(475)	30 412	265	31 035
up to 9 months	(2 462)	27 950	(117)	30 918
up to 10 months	(850)	27 101	(196)	30 722
up to 11 months	(987)	26 114	(528)	30 194
up to 12 months	(1 148)	24 965	(2 608)	27 586

The above values should be interpreted as liquidity surplus/deficit in relevant time buckets. The dynamics of the development of non-bank term deposits and current accounts had a positive impact on the change in the liquidity gap in the amount of PLN 22.1 billion calculated with the exchange rate of 31 December 2021 had a positive impact on the level of liquidity gap, exceeding the dynamics of the development of lending activities in the amount of PLN 7 billion calculated with the exchange rate of 31 December 2021 (in 2020, respectively: PLN 20.4 billion and PLN 3.2 billion, calculated with the exchange rate of 31 December 2020).

The Bank has a limited number of transactions with rating downgrade trigger clauses, which require the Bank to provide additional security or prepay outstanding obligations if Banks's credit rating deteriorates. The amount of the maximum liability resulting therefrom, in the event that the Bank's rating is downgraded to BB+ or lower by two rating agencies, as at the 31 of December 2021, amounts to CHF 314 million (CHF 314 million as of 31 December 2020). However, this potential liability is not unconditional. Contract clauses do not preclude the parties from agreeing the amount, form and timing of additional security on a case-by-case basis.

In 2021 the Bank's liquidity remained at a high and safe level which was reflected in surplus of liquid assets over short-term liabilities according to LAB in various scenarios and supervisory liquidity measures.

LAB cash flows gaps mismatch in terms up to 1 month and up to 1 year within 2020 and values of regulatory measures LCR and NSFR at the end of 2021 and 2020 are presented in the following table:

	31.12.2021	31.12.2020
LAB Base Case 1M	33 375	27 574
LAB Base Case 1Y	24 963	27 586
LCR	203%	202%
NSFR	152%	-

** LAB measures are shown in PLN million; LCR and NSFR are relative measures presented as a decimal.*

The LCR and NSFR measures remained on safe level, significantly exceeding 100%.

Funding sources

The strategic assumptions concerning the diversification of funding sources and profitable structure of the balance sheet are reflected in the financial plan of mBank defined by selected measures, e.g. L/D ratio (Loans to Deposits). It measures a specific relation of loans to deposits in order to maintain a stable structure of its balance sheet. In 2021, L/D ratio slightly changed from 70.3% at the end of 2020 to 66.3% at the end of 2021. The Bank aims at building a stable deposit base by offering to clients deposit and investment products, regular and specific-purpose savings offerings. Funds acquired from the Bank’s clients constitute the major funding source for the business activity along with the portfolio of long-term loans from banks (with maturities over 1 year) and issuance of debt securities (Note 29). The loans and issuances together with subordinated loans (Note 29) are the core funding source for the portfolio of mortgage loans in CHF. According to the suspension of granting new mortgage loans in CHF, the Bank’s receivables in this currency have been decreasing successively along with loans repayments.

In the third quarter of 2021, Bank has issued green senior nonpreferred bonds (NPS) of nominal worth EUR 500 million, qualifying for the MREL index, refinancing maturing unsecured bonds of EUR 428 million, which the bank redeemed on the 26th of November 2021.

Moreover, in order to acquire funding (also in foreign currencies) the Bank uses mid-term and long-term instruments, including credit line facilities on the international markets, unsecured issuances, bilateral loans as well as FX swap and CIRS transactions.

When making funding-related decisions, in order to match the term structure of its funding sources with the structure of long-term assets optimally, the Bank takes into consideration the supervisory liquidity measures and limits, as well as the internal liquidity risk limits.

The Financing Strategy is based on the following assumptions:

- diversifying sources and timing of financing,
- maintaining safe regulatory levels and internal liquidity measures,
- stable increase in transaction deposits,
- incurring liabilities eligible for the MREL indicator,
- maintaining the issuing capacity of mBank Hipoteczny, but with the Bank's greater involvement in financing the subsidiary by purchasing its covered bonds,
- increasing financial independence from the majority shareholder.

3.8.1. Cash flows from transactions in non-derivative financial instruments

The table below shows cash flows the Bank is required to settle, resulting from financial liabilities. The cash flows have been presented as at the year-end date, categorised by the remaining contractual maturities. The amounts denominated in foreign currencies were converted to Polish zloty at the average rate of exchange announced by the National Bank of Poland at the year-end date. The amounts disclosed in maturity dates analysis are undiscounted contractual cash flows.

31.12.2021	Up to 1 month	1-3 months	3-12 months	1-5 years	Over 5 years	Total
Amounts due to banks	2 691 107	561 539	171 634	5	-	**3 424 285**
Amounts due to customers	152 364 840	3 566 669	1 843 809	1 580 923	619 253	**159 975 494**
Debt securities issued	5 962	123	2 931 994	3 848 604	-	**6 786 683**
Subordinated liabilities	21 385	5 479	41 832	948 576	1 931 767	**2 949 039**
Other liabilities	2 049 814	154	136	224	-	**2 050 328**
Total liabilities	**157 133 108**	**4 133 964**	**4 989 405**	**6 378 332**	**2 551 020**	**175 185 829**
Total assets	**34 197 948**	**8 985 458**	**29 467 950**	**79 793 582**	**66 902 535**	**219 347 473**
Net liquidity gap	**(122 935 160)**	**4 851 494**	**24 478 545**	**73 415 250**	**64 351 515**	**44 161 644**

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31.12.2020	Up to 1 month	1-3 months	3-12 months	1-5 years	Over 5 years	Total
Amounts due to banks	2 624 368	-	-	-	-	**2 624 368**
Amounts due to customers	127 356 736	4 346 413	2 591 407	2 983 417	593 163	**137 871 136**
Debt securities issued	56 439	31 343	2 052 142	4 368 767	-	**6 508 691**
Subordinated liabilities	21 433	5 274	40 540	960 314	1 919 682	**2 947 243**
Other liabilities	2 066 066	34	265	372	-	**2 066 737**
Total liabilities	**132 125 042**	**4 383 064**	**4 684 354**	**8 312 870**	**2 512 845**	**152 018 175**
Total assets	**19 703 500**	**9 090 181**	**30 606 003**	**70 533 421**	**54 047 139**	**183 980 244**
Net liquidity gap	**(112 421 542)**	**4 707 117**	**25 921 649**	**62 220 551**	**51 534 294**	**31 962 069**

The assets which ensure the payment of all the liabilities and lending commitments comprise cash in hand, cash at the Central Bank, cash in transit and treasury bonds and other eligible bonds, amounts due from banks, loans and advances to customers.

In the normal course of business, some of the loans granted to customers with the contractual repayment date falling due within the year, will be prolonged. Moreover, a part of debt securities, were pledged as collateral for liabilities. The Bank could ensure cash for unexpected net outflows by selling securities and availing itself of other sources of financing, such as the market of securities secured with assets.

Lease liabilities by maturity dates (undiscounted) are presented in the note 29.

Remaining contractual maturities for guarantees issued are presented in the note 35.

3.8.2. Cash flows from derivatives

Derivatives settled in a net basis

Derivative financial instruments settled in net amounts by the Bank comprise:

- forward Rate Agreements (FRA),
- options,
- warrants,
- interest rate swaps (IRS),
- overnight index swap (OIS),
- cross currency interest rate swaps (CIRS),
- commodity swaps
- bonds forwards,
- commodity forwards,
- CO_2 emission forwards.

Financial instruments for commodities are concluded in bank back-to-back and till 2019 were insignificant from the liquidity risk perspective.

The table below shows derivative financial liabilities of the Bank, which valuation as of end of 2021 and 2020 was negative, grouped by appropriate remaining maturities as at the balance sheet date and are presented as contractual maturities apart from Other up to 1 month and Futures contracts which are presented as net present value (NPV). The amounts denominated in foreign currencies were converted to Polish zloty at the average rate of exchange announced by the National Bank of Poland at the balance sheet date.

31.12.2021	Up to 1 month	1-3 months	3-12 months	1-5 years	Over 5 years	Total
Forward Rate Agreements (FRA)	10 523	9 284	23 322	687	-	**43 816**
Overnight Index Swap (OIS)	944	5 243	(14 568)	(7 110)	4 004	**(11 487)**
Interest Rate Swaps (IRS)	33 614	200 403	1 852 398	6 001 212	350 887	**8 438 514**
Cross Currency Interest Rate Swaps (CIRS)	(3 532)	(1 612)	26 245	5 116	1 087	**27 304**
Options	32	336	(14 192)	(10 391)	(448)	**(24 663)**
Other	2 495	26 753	25 247	2 446	-	**56 941**
Total derivatives settled on a net basis	**44 076**	**240 407**	**1 898 452**	**5 991 960**	**355 530**	**8 530 425**

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31.12.2020	Up to 1 month	1-3 months	3-12 months	1-5 years	Over 5 years	Total
Forward Rate Agreements (FRA)	1 590	1 861	214	-	-	**3 665**
Interest Rate Swaps (IRS)	206 259	353 477	1 155 508	2 744 196	180 774	**4 640 214**
Cross Currency Interest Rate Swaps (CIRS)	(923)	(5 713)	13 899	34 479	(364)	**41 378**
Options	(770)	1 754	(7 340)	(8 841)	13	**(15 184)**
Other	2 789	10 093	18 387	661	-	**31 930**
Total derivatives settled on a net basis	**208 945**	**361 472**	**1 180 668**	**2 770 495**	**180 423**	**4 702 003**

Derivative financial instruments settled in gross amounts

Derivative financial instruments settled in gross amounts by the Bank comprise foreign exchange derivatives: currency forwards and currency swaps.

The table below presents derivative financial liabilities/assets of the Bank, which will be settled on a gross basis, grouped by appropriate remaining maturities as at the balance sheet date. The amounts denominated in foreign currencies were converted to Polish zloty at the average rate of exchange announced by the National Bank of Poland at the balance sheet date.

31.12.2021	Up to 1 month	1-3 months	3-12 months	1-5 years	Over 5 years	Total
Currency derivatives						
- outflows	21 386 922	10 415 286	9 102 203	3 040 668	-	**43 945 079**
- inflows	21 364 429	10 400 405	9 151 753	3 030 248	-	**43 946 835**

31.12.2020	Up to 1 month	1-3 months	3-12 months	1-5 years	Over 5 years	Total
Currency derivatives						
- outflows	23 898 127	10 203 748	7 334 439	4 189 193	-	**45 625 507**
- inflows	24 005 802	10 136 207	7 330 734	4 174 794	-	**45 647 537**

The amounts disclosed in the table are undiscounted contractual outflows/inflows.

The amounts presented in the table above are nominal cash flows of currency derivatives, which have not been settled, while Note 19 shows nominal values of all open derivative transactions.

Detailed data concerning liquidity risk related to off-balance sheet items are presented in the Note 35.

3.9. Operational risk

Operational risk is understood as the possibility of a loss resulting from inadequate or failed internal processes, people and systems or from external events, including also legal risk.

It is comprehensive in nature, which may have a significant impact on the Bank's operations and standing. Apart from the environment and external events, its source may be the Bank itself. Due to their dynamic nature, external and internal factors influencing operational risk are subject to constant analysis.

According to the Risk Catalogue, operational risk includes in particular:

- legal risk,
- conduct risk ("conduct risk"),
- IT risk,
- risk of cyber threats,
- risk of external fraud,
- risk of internal fraud,
- outsourcing risk,
- personnel and organizational risk,
- physical security risk,
- the risk of errors in implementation, delivery and process management.

Operational risk does not include reputational risk; however materialisation of operational risk may increase reputational risk.

Operational risk management is performed in mBank and, at the consolidated level, in mBank Group. While organising the operational risk management process, the Bank takes into account regulatory requirements, which are the starting point for preparation of framework for the operational risk control and management system in the Bank and the Group.

The aim of operational risk management in the Bank is to reduce the causes of operational events, the probability of their occurrence and the severity of potential consequences. When deciding on the acceptable level of operational risk, the following analysis is considered: costs vs. benefits.

Due to the dynamics of changes in factors affecting operational risk, the key elements of the risk management process are: identification, assessment, control and monitoring of the effectiveness of risk reduction, counteracting the materialisation of operational risk and reporting.

The basic tools used to identify, assess and monitor risk include:

1. Self-Assessment of Operational Risk Management Effectiveness, which is performed by organizational units of the Bank and the Group companies. The purpose of this process is to ensure the risk identification and assessment and appropriate modifications. In addition, it supports the communication process about the need to change and improve control processes.
2. The Register of Operating Losses is a database of losses resulting from operational events. mBank also uses access to external databases on operational losses and uses them to analyse operational risk and potential threats to which institutions operating in the financial sector are exposed.
3. The key risk indicators KRI and risk indicators RI support the ongoing monitoring of risk. The process makes it possible to predict in advance the occurrence of an increased level of operational risk and to react appropriately by organizational units in order to avoid the occurrence of operational events and losses.
4. Operational risk scenarios that describe the risks associated with the occurrence of rare but potentially very severe operational risk events.
5. Providing opinions on products before the implementation of a new or modified product offer and the impact of the outsourcing agreement on the operational risk profile.

Some tools support several stages of the operational risk management process.

The bank has a system of regular monitoring of operational events and warning signals coming from the tools, which enables the monitoring of the operational risk profile and ensures regular remedial actions, at the level of the Management Board and Supervisory Board.

Regular monitoring allows Bank to quickly detect weaknesses in the risk management system. Thanks to the identification and analysis of the circumstances related to the recorded event and the operational loss, we can better understand the reasons for the occurrence of an operational event and adequately prevent their repetition also in other areas of the organization.

The bank also places great emphasis on monitoring operational risk and reacting appropriately to emerging potential threats. Timely monitoring of processes is to help early identify negative trends that may lead to significant material losses in the bank.

Operational losses

In 2021, as part of operational risk management, Bank faced in particular losses related to legal risk related to the foreign currency loan portfolio, cyber threats, external fraud.

The vast majority of the Group's operational losses refers to the following business lines: commercial banking and retail banking (separated in accordance with the CRR Regulation).

In terms of losses by risk category, the Group incurs the highest losses in two categories of operational risk: (i) external fraud; (ii) clients, products and business practices.

The following table presents the distribution of actual gross losses by operational risk category, incurred by the mBank in 2020 and 2021:

Operational event category	Total gross losses (in PLN thousand)	
	31.12.2021	31.12.2020
External fraud	5 144	5 051
Clients, Products and Business Practices for foreign currency loans	2 781 503	1 021 714
Clients, Products and Business Practices, excluding foreign currency loans	62 652	44 144
Execution, delivery and process management	4 283	9 727
Other	6 338	13 976
Total	**2 859 920**	**1 094 612**

The high share of losses in the "Customers, products and business practices" category in 2021 was primarily due to the costs of legal risk related to loans in CHF. For more information, see Note 34.

The level of operational risk losses is monitored on an ongoing basis and regularly reported to the Bank's Management Board, the Bank's Supervisory Board and to the committees of the Business and Risk Forum. There are escalation mechanisms in the mBank Group when the operational loss thresholds are exceeded.

They ensure an appropriate analysis of operational events and trigger corrective actions. Information on an event for which the effect or the sum of realized or unrealized effects in the amount the amount of PLN 1 million and higher is reported to: Vice President of the Management Board for Risk Management and Internal Audit Department (DAW).

3.9.1. Compliance risk

Compliance risk management is realized in mBank, in particular, in accordance with the provisions of the Compliance Policy at mBank S.A. The Policy sets forth general rules for ensuring compliance of operations pursued by the Bank with provisions of law, internal regulations and market standards.

Compliance risk is the risk posed by consequences of failure to observe the law, internal regulations and market standards in processes executed in the bank. The objective of compliance risk management is the minimisation of this risk. Noncompliance of the bank's operations with the law is understood as special situations in which:

1. the Bank's internal regulations do not take into account legal provisions,
2. the Bank fails to implement recommendations issued by the Polish Financial Supervision Authority and other supervisory authorities performing their task concerning financial institutions,
3. the Bank fails to implement recommendations arising from internal proceedings, internal and external audits and DC's inspections,
4. Bank processes and operational activities are not in compliance with legal provisions and internal regulations.

Compliance is ensured by means of compliance risk management with respect to processes operating at the bank and the control function as part of three lines of defence. The first line of defence comprises risk management and control function implementation in operating activities. The second line of defence comprises among others:

1. compliance risk management and control function implementation as part of the tasks executed by Compliance Department,
2. risk management by employees holding dedicated positions or working in dedicated organisational units in the case when part of tasks pertaining to compliance risk identification and assessment was assigned to other first and second line of defence units.

The third line of defence comprises the activity of the Internal Audit Department.

In all three lines of defence, the bank's employees duly apply control mechanisms or independently monitor the observance of control mechanisms in order to guarantee compliance of the Bank's operations with the law, internal regulations, and market standards.

Compliance of the bank's internal rules with the Polish and international law and with market standards and observing internal rules by employees guarantees fulfilment of the objectives of the internal control system and mitigates compliance risk, and eliminates or minimises the possibility of occurrence of the following risks: legal risk, reputational risk, risk of imposing sanctions and financial losses and risk resulting from discrepancies in interpretations of the law.

All the Bank employees are responsible for the implementation of compliance risk management process in line with the scope of their duties as well as granted authorisations. The Compliance Department is responsible for the coordination and supervision of the compliance risk management process.

The supervision over the implementation of common compliance standards by the mBank Group subsidiaries is exercised in a manner that does not violate applicable law, prudential regulations and independence of employees performing the compliance function in the subsidiaries, in particular under agreements concluded with the subsidiaries.

3.10. Business risk

Business risk means the risk of losses resulting from deviations between actual net operating result of the mBank Group and the planned level. The calculation of deviations between actual and planned values is done separately for revenues and costs. Business risk includes, in particular, strategic risk connected with the possibility of occurrence of negative financial consequences as a result of wrong or disadvantageous decisions or their wrong implementation. It is assumed, that the results of the strategic decisions are reflected in deviations between actual operating result and the planned level in one-year horizon.

Business risk is included in the calculation of economic capital of mBank and mBank Group.

In order to manage effectively and reduce business risk, the following actions are taken:

- verification of the planned data within planning process,
- regular analysis of the causes of observed deviations of the actual financial performance of the mBank Group organizational units from the planned level and informing the Management Board about results of the above analyses,
- periodic verification of the adopted strategy,
- regular analysis of the competitors' activities.

3.11. Model risk

Model risk is understood as the risk of negative consequences connected with the decisions made on the basis of the output data of models which have been improperly constructed or are improperly administered. Model risk may result in financial losses, improper business or strategic decisions or negatively influence the Bank's reputation.

The following specific subcategories can be distinguished, in particular, in model risk: risk inextricably linked with the restrictions connected with modelling a given phenomenon, assumption/methodology risk, data risk, models administration risk, and risk of interdependence.

Model risk is managed in the Bank on a systemic basis by proper internal regulations concerning model and their risk management process, in particular monitoring and validation of models.

An important role in the model and their risk management process is played by the Model Risk Committee. It recommends, among others, model risk tolerance level, which is finally approved by the Management Board and the Supervisory Board.

3.12. Reputational risk

The aim of management of reputational risk, defined as a risk resulting from a negative perception of the image of the bank or other member of the group among their stakeholders, is to identify, assess and reduce reputational risk in specific processes in order to protect and strengthen the good name of mBank and mBank Group.

All Bank's organizational units, foreign branches, and subsidiaries are directly responsible for any reputational risk arising from their own business activities.

Reputation risk can be secondary to other types of risk, such as credit, market, liquidity and operational risks. Reputation risk is also a primary risk when it arises directly from an ethically, environmentally or socially controversial activity. This risk is identified, measured and monitored.

To monitor and manage reputation risk, mBank uses various tools and methods:

- implementation of policies and regulations in the area of compliance, security, human and employee rights as well as services for industries and areas sensitive to the reputation risk,
- reputation risk assessment based on negative publications,
- customer satisfaction analysis,
- employee satisfaction research,
- employer brand research,
- crisis management,
- reputation risk analysis when implementing new and modifying existing products,
- analysis of customer complaints,
- building awareness in the area of compliance,
- analysis of violations of employee rights and other rules of the bank's operation.

3.13. Capital risk

In mBank there is a capital management process in order to prevent materialization of capital risk, understood as risk resulting from the lack of capital as well as lack of the possibility to achieve sufficient capital adequate to the business activity's risk undertaken by the Bank, required to absorb unexpected losses and meet regulatory requirements enabling further independent functioning of the Bank. Capital risk encompasses the risk of excessive leverage.

Capital risk management is performed, at an individual level, in mBank and, at a consolidated level, in mBank Group.

The capital management in mBank is organised as a process including planning, steering and controlling regulatory and internal capital. Within the framework of capital management process, regular monitoring of capital adequacy and effectiveness is conducted, aimed at assurance that adequate and optimum level of capital is maintained in mBank. This is supported by stress test analyses, which – among others – are based on scenarios of macro environment change, aiming to provide in depth view on current capital position, as well as its possible future developments resulting from the stress scenarios adopted for the analysis.

More information on capital adequacy of mBank is provided in Note 46.

3.14. FX loans portfolio risk

The FX loan portfolio risk is related to housing and mortgage loans in foreign currencies, granted to unsecured borrowers until 2011. This risk may result in particular from the materialization of operational (legal), as well as credit and reputational risk in relation to the above-mentioned borrowers.

The legal risk of the portfolio of loans in foreign currencies (loans indexed with a foreign exchange rate) relates to the portfolio of mortgage-secured loans granted to natural persons in the years 2004-2011.

This risk relates to the possibility of realizing losses resulting from court decisions unfavourable for the bank in cases brought by borrowers.

In managing this risk, the Bank takes action to protect its interests in court proceedings, aimed at obtaining decisions favourable to the Bank.

For effective management of legal risk of the FX loans portfolio, mBank has established the Disputed Loans Department, whose tasks include in particular:

- preparation of materials used in court proceedings,
- coordinating the activities of legal representatives,
- calculation of cost of legal risk related to housing and mortgage loans,
- preparation of recommendations for updating the strategy,
- cooperation and communication with external institutions on indexed loans.

Detailed information on the impact of legal risk related to CHF housing and mortgage loans is provided in Note 34.

Credit risk and reputational risk related to the FX loans portfolio are managed in line with the principles of managing these risks.

3.15. Tax risk

The purpose of the tax risk management (process) is effective and safe performance of all obligations provided for by the tax law. Therefore, Bank identifies tax risks and eliminates or limit them in connection with the role of:

- taxpayer,
- withholding agent,
- an entity providing tax information to the Bank's clients, the Bank's contractors or tax authorities.

Bank manages tax risk by ensuring:

- integrity of tax law with accounting law and financial reporting in the Bank's internal regulations,
- correct tax processes in accordance with the applicable tax law,
- cooperation of organizational units preparing, giving opinions and offering products to the Bank's clients,
- correct identification and monitoring of tax risks,
- rules for concluding transactions with customers,
- monitoring changes in the tax law and jurisprudence.

3.16. Fair value of assets and liabilities

Fair value is the price that would be received from the sale of asset or paid to transfer a liability in an ordinary 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:

- 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.

In line with IFRS 9, for accounting purposes, the Bank determines the valuation of its assets and liabilities through amortised cost or through fair value. In addition, for the positions that are valued through amortised cost, fair value is calculated, but only for disclosure purposes – according to IFRS 7.

The approach to the method used for the loans that are fair valued in line of IFRS 9 requirements, is described in the point 3.3.7.

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Following market practices the Bank values open positions in financial instruments using either the mark-to-market approach or is applying pricing models well established in market practice (mark-to-model method) which use as inputs market prices or market parameters, and in few cases parameters estimated internally by the Bank. All significant open positions in derivatives are valued by market models using prices observable in the market. Domestic commercial papers are marked to model (by discounting cash flows), which in addition to market interest rate curve uses credit spreads estimated internally.

For disclosure purposes, the Bank estimated that the fair value of short-term financial liabilities (less than 1 year) is equal to the balance sheet values of such items. In addition, the Bank assumed that the estimated fair value of financial assets and financial liabilities longer than 1 year is based on discounted cash flows using appropriate interest rates.

Assets and liabilities measured at amortised cost

The following table presents a summary of balance sheet values and fair values for each group of financial assets and liabilities not recognised in the statement of financial position of the Bank at their fair values.

	31.12.2021		31.12.2020	
	Carrying value	Fair value	Carrying value	Fair value
Financial assets at amortised cost				
Debt securities	**16 632 915**	**15 358 098**	**15 952 501**	**16 445 401**
Loans and advances to banks	**11 194 916**	**11 192 768**	**10 845 844**	**10 839 089**
Loans and advances to customers, including:	**86 499 146**	**86 415 449**	**82 729 021**	**83 256 569**
Loans and advances to individuals	**43 319 138**	**44 209 477**	**42 329 891**	**43 853 720**
Current accounts	7 252 733	7 488 236	6 807 188	6 948 252
Term loans	35 680 027	36 334 863	35 231 733	36 614 498
Other	386 378	386 378	290 970	290 970
Loans and advances to corporate entities	**43 099 288**	**42 129 128**	**40 255 292**	**39 258 906**
Current accounts	5 613 678	5 475 185	4 335 675	4 219 578
Term loans	36 876 632	36 044 965	35 522 354	34 642 065
Reverse repo or buy/sell back transactions	187 630	187 630	103 832	103 832
Other loans and advances	407 704	407 704	277 050	277 050
Other	13 644	13 644	16 381	16 381
Loans and advances to public sector	**80 720**	**76 844**	**143 838**	**143 943**
Financial liabilities at amortised cost				
Amounts due to banks	**3 420 001**	**3 420 001**	**2 624 286**	**2 624 286**
Amounts due to customers	**159 905 991**	**159 888 932**	**137 778 034**	**137 805 488**
Debt securities issued	**6 683 623**	**6 698 899**	**6 335 165**	**6 405 592**
Subordinated liabilities	**2 624 456**	**2 616 703**	**2 578 327**	**2 552 098**

The following sections present the key assumptions and methods used by the Bank for estimation of the fair values of financial instruments:

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

The fair value for loans and advances to banks and loans and advances to customers is calculated as the estimated value of future cash flows (adjusted by prepayments) using current interest rates, including credit spread, cost of liquidity and cost of capital margin. The level of credit spread was determined based on market quotation of median credit spreads for Moody's rating grade. Attribution of a credit spread to a given credit exposure is based on a mapping between Moody's rating grade and internal rating grades of the Bank. To reflect the fact that the Bank's exposures are in major part collateralised whereas the median of market quotation is centred around unsecured issues, the Bank applied appropriate adjustments.

<u>Financial liabilities</u>

Financial instruments representing liabilities include the following:

- Contracted borrowings;
- Deposits;
- Issues of debt securities;
- Subordinated liabilities.

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The fair value for these financial liabilities with more than 1 year to maturity is based on cash flows discounted from capital and interest rates using discounted factor. For the loans received from European Investment Bank in EUR the Bank used the EBI yield curve. With regard to the own issue as part of the EMTN programme the market price of the relevant financial services has been used.

In the case of deposits, the Bank has applied the curve constructed on the basis of quotations of interbank market rates as well as FRA and IRS contracts for appropriate currencies and maturities. In case of measurement of subordinated liabilities the Bank used curves based on cross-currency basis swap levels taking into account the original spread on subordinated liabilities and their maturities.

The Bank assumed that the fair values of these instruments with less than 1 year to maturity was equal to the carrying amounts of the instruments.

According to the fair value methodology applied by the Bank, financial assets and liabilities are classified as follows:

- Level 1: prices quoted on active markets for the same instrument (without modification);
- Level 2: prices quoted on active markets for the similar instruments or other valuation techniques for which all significant input data are based on observable market data;
- Level 3: valuation methods for which at least one significant input data is not based on observable market data.

The table below presents the fair value hierarchy of financial assets and liabilities measured at fair value in accordance with the assumptions and methods described above, exclusively for disclosure as at 31 December 2021 and as at 31 December 2020.

31.12.2021	**Including:**	**Level 1**	**Level 2**	**Level 3**
		Quoted prices in active markets	**Valuation techniques based on observable market data**	**Other valuation techniques**
VALUATION ONLY FOR PURPOSES OF DISCLOSURE				
FINANCIAL ASSETS				
Debt securities	15 358 098	12 100 420	-	3 257 678
Loans and advances to banks	11 192 768	-	-	11 192 768
Loans and advances to customers	86 415 449	-	-	86 415 449
FINANCIAL LIABILITIES				
Amounts due to banks	3 420 001	-	-	3 420 001
Amounts due to customers	159 888 932	-	2 812 699	157 076 233
Debt securities issued	6 698 899	6 673 840	-	25 059
Subordinated liabilities	2 616 703	-	2 616 703	-
Total financial assets	**112 966 315**	**12 100 420**	**-**	**100 865 895**
Total financial liabilities	**169 204 534**	**6 673 840**	**5 429 402**	**160 521 293**

31.12.2020	**Including:**	**Level 1**	**Level 2**	**Level 3**
		Quoted prices in active markets	**Valuation techniques based on observable market data**	**Other valuation techniques**
VALUATION ONLY FOR PURPOSES OF DISCLOSURE				
FINANCIAL ASSETS				
Debt securities	16 445 401	13 395 856	-	3 049 545
Loans and advances to banks	10 839 089	-	-	10 839 089
Loans and advances to customers	83 256 569	-	-	83 256 569
FINANCIAL LIABILITIES				
Amounts due to banks	2 624 286	-	-	2 624 286
Amounts due to customers	137 805 488	-	4 296 271	133 509 217
Debt securities issued	6 405 592	6 369 433	-	36 159
Subordinated liabilities	2 552 098	-	2 552 098	-
Total financial assets	**110 541 059**	**13 395 856**	**-**	**97 145 203**
Total financial liabilities	**149 387 464**	**6 369 433**	**6 848 369**	**136 169 662**

Level 1

Level 1 of financial assets includes the value of treasury securities and EIB bonds whose valuation consists in the direct use of market current prices of these instruments originating from active and liquid financial markets.

Level 1 of financial liabilities includes the fair value of bonds issued by the Bank (Note 29). For the purpose of disclosures the Bank applied market price of the issued debt securities.

Level 2

Level 2 includes the fair value of long-term loans received from banks, the fair value of long-term deposits placed by customers and the fair value of the loans received from the EIB (Note 29). In addition, at level 2, the Bank has presented subordinated liabilities.

The fair value of financial liabilities included at Level 2 with more than 1 year to maturity is based on cash flows discounted using interest rates. In case of the loans received from European Investment Bank in EUR, the Bank used EIB yield curve and the value of margin which was agreed upon the last contract. Based on that assumption, the spread of Bank to market swap curve was estimated. In case of deposits the Bank used the curve based on overnight rates, term cash rates, as well as FRA contracts for appropriate currencies and maturities. For debt securities issued the Bank used the prices directly from the market for these securities. For the purpose of measurement of subordinated liabilities the Bank used obtained primary market spreads of subordinated bonds issued by the Bank and if required corresponding cross-currency basis swap levels for the respective maturities.

Level 3

Level 3 includes:

- the fair value of loans and advances to banks and loans and advances to customers, which is disclosed, as described earlier, based on quotation of median credit spreads for Moody's ratings;
- liabilities due to banks and to customers with maturity up to one year, for which the Bank assumed that their fair value is equal to the carrying value;
- the fair value of liabilities due to banks and to customers with maturity exceeding one year, for which were used valuation methods using at least one significant input data not based on observable market data.

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Financial assets and liabilities measured at fair value and investment properties

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.

31.12.2021	Including:	Level 1	Level 2	Level 3
		Quoted prices in active markets	Valuation techniques based on observable market data	Other valuation techniques
RECURRING FAIR VALUE MEASUREMENTS				
FINANCIAL ASSETS				
Financial assets held for trading and hedging derivatives	**2 581 174**	**248 906**	**1 866 663**	**465 605**
Loans and advances to customers	40 426	-	-	40 426
Debt securities	674 085	248 906	-	425 179
Derivative financial instruments, including:	1 866 663	-	1 866 663	-
Derivative financial instruments held for trading:	2 104 819	-	2 104 819	-
Hedging derivative financial instruments:	163 715	-	163 715	-
Offsetting effect	(401 871)	-	(401 871)	-
Non-trading financial assets mandatorily at fair value through profit or loss	**1 221 063**	**870**	**-**	**1 220 193**
Loans and advances to customers	991 469	-	-	991 469
Debt securities	81 128	-	-	81 128
Equity securities	148 466	870	-	147 596
Financial assets at fair value through other comprehensive income	**54 162 657**	**25 971 560**	**8 495 243**	**19 695 854**
Loans and advances to customers	18 191 254	-	-	18 191 254
Debt securities	35 971 403	25 971 560	8 495 243	1 504 600
TOTAL FINANCIAL ASSETS	**57 964 894**	**26 221 336**	**10 361 906**	**21 381 652**
Investment properties	**127 510**	**-**	**-**	**127 510**
FINANCIAL LIABILITIES				
Derivative financial instruments, including:	1 959 827	-	1 959 827	-
Derivative financial instruments held for trading	2 272 167	-	2 272 167	-
Hedging derivative financial instruments	1 598 547	-	1 598 547	-
Offsetting effect	(1 910 887)	-	(1 910 887)	-
Liabilities from short sale of securities	84 774	84 774	-	-
TOTAL FINANCIAL LIABILITIES	**2 044 601**	**84 774**	**1 959 827**	**-**

Assets Measured at Fair Value Based on Level 3 - changes in 2021	Debt trading securities	Non-trading debt securities mandatorily at fair value through profit or loss	Non-trading equity securities mandatorily at fair value through profit or loss	Debt securities at fair value through other comprehensive income	Investment properties
As at the beginning of the period	**333 151**	**76 068**	**135 520**	**1 509 952**	**-**
Gains and losses for the period:	**11 032**	**5 060**	**11 182**	**(65 509)**	**14 118**
Recognised in profit or loss:	11 032	5 060	11 182	-	-
- Net trading income	11 032	6 196	-	-	-
- Gains or losses on non-trading financial assets mandatorily at fair value through profit or loss	-	(1 136)	11 182	-	-
Recognised in other comprehensive income:	-	-	-	(65 509)	14 118
- Financial assets at fair value through other comprehensive income	-	-	-	(65 509)	14 118
Purchases	2 368 719	-	894	1 364 162	-
Redemptions	(204 372)	-	-	(394 816)	-
Sales	(8 098 131)	-	-	(2 510 472)	-
Issues	6 014 780	-	-	1 601 283	-
Settlements	-	-	-	-	113 392
As at the end of the period	**425 179**	**81 128**	**147 596**	**1 504 600**	**127 510**

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31.12.2020	Including:	Level 1 Quoted prices in active markets	Level 2 Valuation techniques based on observable market data	Level 3 Other valuation techniques
RECURRING FAIR VALUE MEASUREMENTS				
FINANCIAL ASSETS				
Financial assets held for trading and hedging derivatives	**2 493 535**	**366 517**	**1 605 965**	**521 053**
Loans and advances to customers	187 902	-	-	187 902
Debt securities	699 668	366 517	-	333 151
Derivative financial instruments, including:	1 605 965	-	1 605 965	-
Derivative financial instruments held for trading:	1 817 678	-	1 817 678	-
Hedging derivative financial instruments:	820 483	-	820 483	-
Offsetting effect	(1 032 196)	-	(1 032 196)	-
Non-trading financial assets mandatorily at fair value through profit or loss	**1 585 029**	**960**	**-**	**1 584 069**
Loans and advances to customers	1 372 481	-	-	1 372 481
Debt securities	76 068	-	-	76 068
Equity securities	136 480	960	-	135 520
Financial assets at fair value through other comprehensive income	**47 731 612**	**33 556 650**	**149 997**	**14 024 965**
Loans and advances to customers	12 515 013	-	-	12 515 013
Debt securities	35 216 599	33 556 650	149 997	1 509 952
TOTAL FINANCIAL ASSETS	**51 810 176**	**33 924 127**	**1 755 962**	**16 130 087**
FINANCIAL LIABILITIES				
Derivative financial instruments, including:	1 414 374	-	1 414 374	-
Derivative financial instruments held for trading	1 678 160	-	1 678 160	-
Hedging derivative financial instruments	7 706	-	7 706	-
Offsetting effect	(271 492)	-	(271 492)	-
TOTAL FINANCIAL LIABILITIES	**1 414 374**	**-**	**1 414 374**	**-**

Assets Measured at Fair Value Based on Level 3 - changes in 2020	Debt trading securities	Non-trading debt securities mandatorily at fair value through profit or loss	Non-trading equity securities mandatorily at fair value through profit or loss	Debt securities at fair value through other comprehensive income
As at the beginning of the period	**460 191**	**133 774**	**86 772**	**1 488 819**
Gains and losses for the period:	**21 089**	**12 632**	**48 748**	**20 625**
Recognised in profit or loss:	21 089	12 632	48 748	-
- Net trading income	*21 089*	*1 922*	*91*	-
- Gains or losses on non-trading financial assets mandatorily at fair value through profit or loss	-	*10 710*	*48 657*	-
Recognised in other comprehensive income:	-	-	-	20 625
- Financial assets at fair value through other comprehensive income	-	-	-	*20 625*
Purchases	2 075 197	-	-	1 243 442
Redemptions	(233 837)	-	-	(433 937)
Sales	(9 729 999)	-	-	(5 090 143)
Issues	7 740 510	-	-	4 281 146
Settlements	-	(70 338)	-	-
As at the end of the period	**333 151**	**76 068**	**135 520**	**1 509 952**

In 2021 and 2020 there were no transfers of financial instruments between the levels of fair value hierarchy.

With regard to 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 the Balance Risk Management Department on the basis of internal rules. In case there is no market price used to a direct valuation for more than 5 working days, the method of valuation is changed, i.e. change from marked-to-market valuation to marked-to-model valuation under the assumption that the valuation model for the respective type of this instrument has been already approved. The return to marked-to-market valuation method takes place after a period of at least 10 working days in which the market price was available on a continuous basis. If there is no market prices for a debt treasury bonds the above terms are respectively 2 and 5 working days.

Level 1

As at 31 December 2021, at level 1 of the fair value hierarchy, Bank has presented the fair value of held for trading government bonds in the amount of PLN 248 906 thousand and the fair value of government bonds and treasury bills measured at fair value through other comprehensive income in the amount of PLN 24 468 564 thousand (31 December 2020 respectively: PLN 366 517 thousand and PLN 32 375 426 thousand. Level 1 includes the fair values of corporate bonds in the amount of PLN 1 502 996 thousand (31 December 2020: PLN 1 181 224 thousand).

In addition, as at 31 December 2021, level 1 includes the value of the registered preferred shares of Giełda Papierów Wartościowych in the amount of PLN 870 thousand (31 December 2020: PLN 960 thousand).

As at 31 December 2021, level 1 includes liabilities from short sale of securities in the amount of PLN 84 774 thousand.

These instruments are classified as level 1 because their valuation is directly derived by applying current market prices quoted on active and liquid financial markets.

Level 2

Level 2 of the fair value hierarchy mainly includes the fair values of bills issued by NBP in the amount of PLN 8 495 243 thousand (31 December 2020: PLN 149 997 thousand), whose valuation is based on a NPV model (discounted future cash flows) fed with interest rate curves generated by transformation of quotations taken directly from active and liquid financial markets.

In addition, the level 2 category includes the valuation of derivative financial instruments borne on models consistent with market standards and practices, using parameters taken directly from the markets (e.g., foreign exchange rates, implied volatilities of FX options, stock prices and indices) or parameters which transform quotations taken directly from active and liquid financial markets (e.g. interest rate curves).

Level 3

Level 3 of the hierarchy presents the fair values of commercial debt securities issued by local banks and companies in the amount of PLN 1 977 236 thousand (31 December 2020: PLN 1 882 836 thousand) and includes i.a. the fair value of a debt instrument measured at fair value through profit or loss, resulting from the reclassification of preferred stock in Visa Inc.

Level 3 includes also the fair value of local government bonds in the amount of PLN 33 671 thousand (31 December 2020: PLN 36 335 thousand).

Model valuation for these items assumes a valuation based on the market interest rate yield curve adjusted by the level of credit spread. The credit spread parameter reflects the credit risk of the security issuer and is determined in accordance with the Bank's internal model. This model uses credit risk parameters (e.g. PD, LGD) and information obtained from the market (including implied spreads from transactions). PD and LGD parameters are not observed on active markets and therefore have been determined on the basis of statistical analyses. Both models - the valuation of debt instruments and the credit spread model were built internally in the Bank by risk units, were approved by the Model Risk Committee and are subject to periodic monitoring and validation carried out by an entity independent of the units responsible for building and maintaining the model.

Level 3 as at 31 December 2021 includes the value of loans and advances to customers in the amount of PLN 19 223 149 thousand (31 December 2020: PLN 14 075 396 thousand). The principles for Fair Value calculation for loans and advances to customers is described in Note 3.3.7.

Moreover, level 3 covers mainly the fair value of equity securities amounting to PLN 147 596 thousand (31 December 2020: PLN 135 520 thousand). Equity securities presented at level 3 are valuated using the market multiples method. The market multiples method consists of valuating the equity of a company by using a relation between market values of equity or total capital invested in comparable companies and selected economic and financial figures.

As at 31 December 2021, level 3 includes also fair value measurement of investment property in the amount of PLN 127 510 thousand. The value of the property was estimated by a property appraiser entered in the Central Register of Property Appraisers kept by the Minister of Development and Technology. The property was valued using the income method. The key unobservable parameter used in the model is the capitalization rate of 9.28% used to discount cash flows.

The table below presents the sensitivity of the fair value measurement to the change of unobservable parameters used in the models for financial instruments measured at fair value at level 3.

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Portfolio	Fair value 31.12.2021	Sensitivity to change of unobservable parameter		Description
		(-)	(+)	
Commercial debt securities measured at fair value through other comprehensive income	1 504 600	(29 729)	29 729	The unobservable parameter is the credit spread. Sensitivity was calculated assuming a change in the credit spread by 100 bp. As the value of the parameter increases, the Bank expects a loss (-), as it decreases, the Bank expects a profit (+).
Commercial debt securities measured at fair value through profit or loss	425 179	(8 569)	8 569	
Loans and advances to customers held for trading	40 426	(761)	743	The valuation model uses credit risk parameters (PD and LGD). Sensitivity was calculated assuming a change in PD and LGD by +/- 10%. As the value of the parameter increases, the Bank expects a loss (-), as it decreases, the Bank expects a profit (+).
Loans and advances to customers at fair value through profit or loss	991 469	(15 630)	16 159	
Loans and advances to customers at fair value through other comprehensive income	18 191 254	(3 205)	2 978	

Portfolio	Fair value 31.12.2020	Sensitivity to change of unobservable parameter		Description
		(-)	(+)	
Commercial debt securities measured at fair value through other comprehensive income	1 509 952	(35 990)	35 990	The unobservable parameter is the credit spread. Sensitivity was calculated assuming a change in the credit spread by 100 bp. As the value of the parameter increases, the Bank expects a loss (-), as it decreases, the Bank expects a profit (+).
Commercial debt securities measured at fair value through profit or loss	333 151	(7 045)	7 045	
Loans and advances to customers held for trading	187 902	(306)	285	The valuation model uses credit risk parameters (PD and LGD). Sensitivity was calculated assuming a change in PD and LGD by +/- 10%. As the value of the parameter increases, the Bank expects a loss (-), as it decreases, the Bank expects a profit (+).
Loans and advances to customers at fair value through profit or loss	1 372 481	(25 873)	26 007	
Loans and advances to customers at fair value through other comprehensive income	12 515 013	(5 289)	4 926	

4. Major estimates and judgments made in connection with the application of accounting policy principles

The Bank applies estimates and adopts assumptions which impact the values of assets and liabilities presented in the subsequent period. Estimates and assumptions, which are continuously subject to assessment, rely on historical experience and other factors, including expectations concerning future events, which seem justified under the given circumstances.

Provisions for legal risks relating to indexation clauses in mortgage and housing loans in CHF

Detailed information on the impact of legal risk related to CHF mortgage and housing loans is provided in Note 34.

Impairment of loans and advances

The Bank reviews its loan portfolio in terms of possible impairments at least once per quarter. In order to determine whether any impairment loss should be recognised in the income statement, the Bank assesses whether any evidence exists that would indicate some measurable reduction of estimated future cash flows attached to the loan portfolio. The methodology and the assumptions (on the basis of which the estimated cash flow amounts and their anticipated timing are determined) are regularly verified. If the current value of estimated cash flows for portfolio of loans and advances as well as contingent liabilities which are impaired, change by +/-10%, the estimated loans and advances as well as contingent liabilities impairment would either decrease by PLN 31.4 million or increase by PLN 32.8 million as at 31 December 2021, respectively (as at 31 December 2020: PLN 41 million and PLN 42.6 million, respectively). This estimation was performed for portfolio of loans and advances and contingent liabilities individually assessed for impairment on the basis of future cash flows due to repayments and recovery from collateral - Stage 3. The rules of determining write-downs and provisions for impairment of credit exposures have been described under Note 3.3.6.

The impact of the COVID-19 pandemic on the Bank`s operations

Support measures implemented in the Bank as a result of the COVID-19 pandemic

In the year 2021, the Bank continued to offer its clients assistance tools aimed at supporting them in a difficult situation resulting from the ongoing COVID-19 epidemic. The purpose of these tools was to help maintain the financial liquidity of customers by reducing the financial burden in the short term. However in the year 2021, the scale of submitted support applications was significantly lower than in 2020. This was mainly due to stricter eligibility conditions for customers under non-legislative, sector solutions, as well as adjustment of the clients` business model to a new, pandemic economic environment.

The supporting measures offered by the Bank till the end of March 2021 were in line with the banks' position regarding the unification of the rules for offering supporting measures in the banking sector. This position was a non-legislative moratoria within the meaning of the European Banking Authority (EBA) guidelines on legislative and non-legislative moratoria on loan repayments applied in the light of the COVID-19 crisis notified by the Polish Financial Supervision Authority to the European Banking Authority.

The COVID-19 moratoria in Poland covered supporting instruments granted from 13 March 2020 to 30 September 2020 and afterwards – from 18 January 2021 to 31 March 2021 – supporting instruments dedicated to businesses representing sectors which suffered most due to COVID-19 pandemic.

The COVID-19 moratoria in Czech Republic covered supporting instruments granted from 1 April 2020 to 31 October 2020 and in Slovakia from 1 April 2020 to 31 March 2021.

<u>The moratoria reopened in Poland in January 2021 and in Retail Banking area</u> was offered by the Bank for SME operating in crafts especially hit by pandemic, mentioned in PFR Financial Shield 2.0. program regulations. It enabled changes in the schedule of payments by suspending the payments of principal amounts or full instalments for the limited period up to 9 months, including the moratorium periods granted in 2020, with the possibility of extending the loan period by the duration of the moratorium. Examination of applications that meet the conditions set by the moratorium took place in a simplified process, i.e. without the verification of the client's repayment ability. The application process was supported by the mechanism of automated verification of boundary conditions (i.a. industry registration, no delay in payment of more than one instalment, at least 6-month repayment history, contract date before 13 March 2020).

While deferring the repayment of the principal part of the loan instalment the sum of the principal amount remaining after the grace period is divided according to the algorithm (equal or decreasing instalments - according to the credit agreement) for the residual maturity period. The extension of the loan period translates into lower instalments after the grace period, than in case of the deferral without the extension. When suspending principal and interest payments, the mechanism for the capital was the same as for the capital repayment deferral, while the suspended interest parts of instalments are spread out proportionally over the outstanding period after the suspension period.

The Bank in Poland also offers to retail clients support under so-called Crisis Shield 4.0, effective from 23 June 2020. The customers who lost their job or another major source of income after 13 March 2020, have the right to suspend the loan repayment for up to 3 months without charging interest during the period of suspension of the agreement. This assistance tool is considered as a legislative moratorium within the meaning of the EBA guidelines. The scale of applications submitted for this form of assistance is still not significant.

<u>The moratoria offered by the Bank in Corporate Banking area</u>, was based on EBA reactivated guidelines on legislative and non-legislative moratoria on loan repayments applied due to another wave of COVID-19 pandemic. This regulation was renewed by EBA on 2 December 2020. In spite of EBA actions, Polish Bank Association (ZBP) decided to resume the non-legislative moratorium and offered supporting instruments from 18 January to 31 March 2021. The renewed moratorium was notified by the EBA through UKNF (the Polish Financial Supervision Authority), but its scale is significantly reduced than that of the first moratorium.

Reactivated moratorium granted aid was limited only to clients operating in the sectors most affected by the COVID-19 pandemics, that is industries covered by the PFR Financial Shield (according to the PKD classification) or operating in the field of renting space in commercial facilities, including retail parks with the area of more than 2000 square meters. The remaining criteria qualifying clients to assistance were similar to the rules applicable under the first moratorium, that means they only applied to loans granted before 13 March 2020 and only for client who as of 31 December 2020 was not classified as default, was not pending against bankruptcy, restructuring, liquidation or enforcement proceedings and till 31 March 2021 submitted an application on changing terms of financing.

The supporting measures offered by the Bank consisted in suspending principal amounts up to 9 months in total (taking into account the earlier period of support granted under the first moratorium) or extending revolving financing up to 9 months in total. In the case of small and medium-sized enterprises the Bank also offered the possibility of suspending full instalments for up to 6 months in total.

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The amount of suspended principal part of instalments increases the last loan instalment. Concerning the suspension of both principal and interest part of instalments, the amount of suspended principal increased the last loan instalment, while the amount of suspended interest was added to subsequent interest instalments payable after the deferral period (that correspond to the number of deferred instalments). In the case of commercial real estate financing transactions exceeding PLN 4 million, the repayment terms were negotiated individually. In addition, when granting assistance, the Bank requires maintaining collateral at least at the same level and limiting distribution to the owner.

The tables below present information on the total scope of the moratoria and new financing covered by public guarantee programs (BGK) applied in Poland as a result of the outbreak of the COVID-19 pandemic (as of 31 December 2021).

Number of obligors subject to assistance tools in Poland in the period of 13.03.2020 - 31.12.2021	31.12.2021
Moratoria	52 112
Government guarantees (BGK)	85

Value of the loans in Poland with assistance tools granted in the period of 13.03.2020-31.12.2021	31.12.2021				
	Gross carrying amount	Of which: gross carrying amount of contracts with expired support measures	Of which: gross carrying amount of contracts with active support measures	Accumulated Impairment – active support measures	Net carrying amount risk – active support measures
Moratoria	**7 395 198**	**7 394 773**	**425**	**(109)**	**316**
- Individual customers	4 920 251	4 919 826	425	(109)	316
- Corporate customers	2 474 947	2 474 947	-	-	-
Government guarantees (BGK)	**849 683**	**-**	**849 683**	**(7 184)**	**842 499**
- Individual customers	-	-	-	-	-
- Corporate customers	849 683	-	849 683	(7 184)	842 499

The tables below present information on total assistance tools in Poland broken down into active help and expired help at the date of 31 December 2021.

a) active assistance tools as of 31 December 2021

Active assistance tools in Poland as of 31.12.2021, granted in the period 13.03.2020-31.12.2021	Gross carrying amount	Performing			
		Of which: exposures with forbearance measures	Of which: grace period of capital and interest	Of which: instruments with significant increase in credit risk since initial recognition but not credit-impaired (Stage 2)	Accumulated impairment
Moratoria	-	-	-	-	-
- Individual customers	-	-	-	-	-
- Corporate customers	-	-	-	-	-
Government guarantees (BGK)	**837 767**	**2 824**	**-**	**298 545**	**(3 743)**
- Individual customers	-	-	-	-	-
- Corporate customers	837 767	2 824	-	298 545	(3 743)

Active assistance tools in Poland as of 31.12.2021, granted in the period 13.03.2020-31.12.2021	Gross carrying amount	Non-performing			Gross carrying amount – Inflows to non-performing exposures in the fourth quarter of 2021
		Of which: exposures with forbearance measures	Of which: unlikely to pay that are not past-due or past-due <= 90 days	Accumulated impairment	
Moratoria	**425**	**-**	**-**	**(109)**	**425**
- Individual customers	425	-	-	(109)	425
- Corporate customers	-	-	-	-	-
Government guarantees (BGK)	**11 916**	**11 916**	**-**	**(3 441)**	**11 916**
- Individual customers	-	-	-	-	-
- Corporate customers	11 916	11 916	-	(3 441)	11 916

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b) expired assistance tools as of 31 December 2021

Expired assistance tools in Poland as of 31.12.2021, granted in the period 13.03.2020-31.12.2021	Performing				
	Gross carrying amount	Of which: exposures with forbearance measures	Of which: instruments with significant increase in credit risk since initial recognition but not credit-impaired (Stage 2)	Accumulated impairment	Of which: instruments with significant increase in credit risk since initial recognition but not credit-impaired (Stage 2)
Moratoria	**7 145 019**	**116 716**	**608 228**	**(50 775)**	**(29 827)**
- Individual customers	4 713 924	65 056	270 309	(30 484)	(15 917)
- Corporate customers	2 431 095	51 660	337 919	(20 291)	(13 910)
Government guarantees (BGK)	**-**	**-**	**-**	**-**	**-**
- Individual customers	-	-	-	-	-
- Corporate customers	-	-	-	-	-

Expired assistance tools in Poland as of 31.12.2021, granted in the period 13.03.2020-31.12.2021	Non-performing				
	Gross carrying amount	Of which: exposures with forbearance measures	Of which: unlikely to pay that are not past-due or past-due <= 90 days	Accumulated impairment	Gross carrying amount – Inflows to non-performing exposures in the fourth quarter of 2021
Moratoria	**249 754**	**18 775**	**-**	**(122 693)**	**56 816**
- Individual customers	205 902	12 309	-	(102 876)	47 543
- Corporate customers	43 852	6 466	-	(19 817)	9 273
Government guarantees (BGK)	**-**	**-**	**-**	**-**	**-**
- Individual customers	-	-	-	-	-
- Corporate customers	-	-	-	-	-

The tables below present information on total assistance tools, in Czech Republic and Slovakia, broken down into active help and expired help at the date of 31 December 2021.

Number of obligors subject to assistance tools in Poland in the period of 1.04.2021 - 31.12.2021	
Moratoria	5 579

Value of the loans in Czech Republic and Slovakia with assistance tools granted in the period of 01.04.2020-31.12.2021	31.12.2021				
	Gross carrying amount	Of which: gross carrying amount of contracts with expired moratoria	Of which: gross carrying amount of contracts with active moratoria	Accumulated Impairment – active support measures	Net carrying amount risk – active moratoria
Moratoria	**416 902**	**416 902**	**-**	**-**	**-**
- Individual customers	416 902	416 902	-	-	-
- Corporate customers	-	-	-	-	-

a) active assistance tools as of 31 December 2021

As of 31 December 2021 there were no loans with active support measures in Czech Republic nor in Slovakia.

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b) expired assistance tools as of 31 December 2021.

Expired assistance tools as of 31.12.2021 in Czech Republic and Slovakia, granted in the period of 01.04.2020-31.12.2021	Performing				
	Gross carrying amount	Of which: exposures with forbearance measures	Of which: instruments with significant increase in credit risk since initial recognition but not credit-impaired (Stage 2)	Accumulated impairment	Of which: instruments with significant increase in credit risk since initial recognition but not credit-impaired (Stage 2)
Moratoria	**403 792**	**45 869**	**28 657**	**(2 364)**	**(1 527)**
- Individual customers	403 792	45 869	28 657	(2 364)	(1 527)
- Corporate customers	-	-	-	-	-

Expired assistance tools as of 31.12.2021 in Czech Republic and Slovakia, granted in the period of 01.04.2020-31.12.2021	Non-performing				
	Gross carrying amount	Of which: exposures with forbearance measures	Of which: unlikely to pay that are not past-due or past-due <= 90 days	Accumulated impairment	Gross carrying amount – Inflows to non-performing exposures in the fourth quarter of 2021
Moratoria	**13 110**	**1 374**	**2 390**	**(6 694)**	**-**
- Individual customers	13 110	1 374	2 390	(6 694)	-
- Corporate customers	-	-	-	-	-

In Poland, in the Czech Republic and in Slovakia, vast majority of loans subject to COVID-19 repayment moratoria, benefited only from the suspension of the principal repayments (it accounted for about 94% of the total exposure covered by the moratoria, both expired and active). Consequently the customers are still obligated to make repayments but in a lower amount. The delay in the interest payments is subject to the standard days-past-due calculation. Overdue interest payment exceeding 30 days results in the reclassification of exposure to Stage 2, and exceeding 90 days - to Stage 3.

Impact of the COVID-19 pandemic on the client's financial situation assessment process

In assessing the financial situation of corporate clients, the Bank uses only individual assessment as the most appropriate and precise (the Bank does not use a collective or sectorial approach).

The process of client and transaction risk monitoring takes into account the impact of the COVID-19 pandemic on the client's situation and the strength of the impact (i.e. temporary turbulence, long-term problem for the business model, etc.) as well as the plan to mitigate this impact implemented by the client. The Bank defined a list of industries/segments of industries with high risk of being affected by COVID-19. The list is reviewed periodically.

The client (including the client supported by the Bank due to the effect of COVID-19) is placed on the Watch List, based on standard criteria defined in the Bank 's internal regulations.

In the scope of retail customers risk assessment, the borrowers with granted assistance tools in the form of moratorium were subject to scoring approach in accordance with the standard risk assessment process.

Description of the forbearance classification approach applied in the Bank in relation to COVID-19

In year2021, Bank applied forborne classification rules to the exposures covered by COVID-19 pandemic support programs compliant with an internal regulations. As required by the EBA, the use of support tools in connection with COVID-19, did not resulted in automatic classification to forbearance.

For corporate clients, there is applied an approach based on individual assessment whether classification of such client's exposure as forborne is required, in accordance with the Bank’s internal regulations.

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Additional cost of risk due to COVID-19 pandemic:

Actions taken regarding clients subject to non-legislative moratoria

In the year 2021, Bank withdrew gradually from using additional premisses for maintaining loans subject to the moratoria in Stage 2. In the following months of the year 2021 Bank changed the stage classification for Stage 2 exposures which were repaid on time after moratoria period and for which there were no other transfer logic premises. By the end of 2021 classification to Stage 2 for all retail exposures previously subject to the moratoria were consistent with qualitative and quantitative criteria of transfer logic. The reclassification resulted in the recognition of additional income in the amount of PLN 43.2 million. The total gross carrying amount reclassified to the Stage 1 due to cancellation of additional premisses, amounted to PLN 2 793 million.

Actions taken regarding clients subject to legislative moratoria

Bank decided to automatically and temporarily reclassify exposures subject to the relief in the form of the statutory moratorium starting from 31 December 2020 to Stage 3, or, in justified cases, to Stage 2. The final allocation of the exposure to Stage 2 was possible after conducting additional analyses taking into account quantitative and qualitative factors, such as: co-borrower in the contract, credit quality of all customer exposures, the amount of cash flow after the date of the application for a moratorium. The reclassification resulted in the recognition of additional cost of credit risk in 2021 in the amount of PLN 2.4 million. The total gross carrying amount of the temporarily reclassified portfolio in 2021 was PLN 18.4 million.

In addition, in spite of an individual review of the corporate portfolio customers, which resulted in the reclassification of customers to the Stage 3 due to the deterioration of their financial situation caused by the consequences of the COVID-19 pandemic, additional cost of credit risk in the amount of PLN 7.5 million were recognised.

Summary of the impact of COVID-19 pandemic on expected cost of credit risk

In the year 2021, as a result of current pandemic developments, Bank recognised PLN 33.3 million of additional income.

Net impairment losses and fair value change on loans and advances	Period from 01.01.2021 to 31.12.2021		
	Individual customers	Corporate customers	Total
Financial asset measured at amortised cost	**40 813**	**(7 468)**	**33 345**
Stage 1	-	-	-
Stage 2	43 165	-	43 165
Stage 3	(2 352)	(7 468)	(9 820)
Financial assets measured at fair value through profit or loss	-	-	-

As of 31 December 2021, the Bank did not apply management corrections (overlays).

Impact of the macroeconomic environment forecast on the expected credit loss values

In the third quarter of 2021, the Bank updated the forecasts of future macroeconomic conditions used in the expected credit loss model. The forecasts take into account the current development of the ongoing COVID-19 pandemic and they are consistent with the forecasts used by the Bank in the planning process.

In order to assess expected credit loss (ECL) sensitivity to the future macroeconomic conditions, mBank determined the ECL value separately for each of the scenarios used for the purposes of calculating the expected credit risk losses.

The table below presents forecasts of the main macroeconomic indicators used in the expected credit loss model as of 31 December 2021 and 31 December 2020.

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Scenario as of 31.12.2021		base		optimistic		pessimistic	
Probability		60%		20%		20%	
		The first year of the forecast	The average for the next two years	The first year of the forecast	The average for the next two years	The first year of the forecast	The average for the next two years
GDP	y/y	5.1	4.5	7.1	5.6	3.5	3.5
Unemployment rate	end of the year	3.0%	2.4%	2.5%	2.0%	3.6%	3.3%
Real estate price index	y/y	107.9	106.6	109.6	108.4	104.1	104.7
CHFPLN	end of the year	3.89	3.80	3.76	3.71	4.03	3.99

Scenario as of 31.12.2020		base		optimistic		pessimistic	
Probability		60%		20%		20%	
		The first year of the forecast	The average for the next two years	The first year of the forecast	The average for the next two years	The first year of the forecast	The average for the next two years
GDP	y/y	-4.2	4.4	0.0	3.9	-6.4	0.4
Unemployment rate	end of the year	7.0%	5.5%	3.3%	2.9%	9.2%	11.9%
Real estate price index	y/y	101.0	105.5	103.0	105.9	91.9	102.8
CHFPLN	end of the year	4.21	4.03	4.11	3.93	4.43	4.43

The value of credit risk cost is the result of all presented macroeconomic scenarios and the weights assigned to them. Impact of individual scenarios on the credit risk costs is as shown in the table below (weight of a given scenario 100%).

Changes in credit risk costs	Year ended 31 December	
	2021	2020
optimistic scenario	49 078	41 360
base scenario	(6 448)	10 276
pessimistic scenario	(73 774)	(120 905)

The above results were estimated taking into account the equal allocation to the Stage 2 based on the weighted average of all 3 macroeconomic scenarios, without and assumption of additional potential migrations between stages. The ECL sensitivity analysis was performed on 80% of the assets of the portfolio of loans and advances to customers.

The reason for changes in key values in the models used for the calculation of expected credit losses was the update of the macroeconomic indicators used.

Prepayments of retail loans

CJEU ruled on 11 September 2019 that in case concerning consumer loans paid off prematurely the consumer has the right to a reduction in the total cost of the loan in the event of early repayment of the credit. The interpretation constituted an answer to a prejudicial question asked in a court case in which few banks have participated including mBank.

The above ruling impacts consumer loans granted on 18 December 2011 or later, in the amount not exceeding 255 550 PLN or its equivalent in other currency and mortgage loans granted on 22 July 2017 or later with no limit of the loan amount, which have been paid off fully or partially.

As of 31 December 2021 the provision recorded within other provisions (Note 31) related to potential reimbursements of commissions in relation to early repayments of loans before the date of the verdict amounted to PLN 4.8 million (PLN 13.8 million as of 31 December 2020).

The total negative impact of early repayments of retail loans on the Group's gross profit for 2021 amounted to PLN 91.8 million (2020: PLN 56.5 million).

The above estimates are burdened with significant uncertainty regarding the number of customers who will request the Bank to refund commissions regarding earlier repayments made by the CJEU verdict as well as the expected rate of loan prepayments in the future.

Fair value of derivatives and other financial instruments

The fair value of financial instruments not listed on active markets is determined by applying valuation techniques. All the models are approved prior to being applied 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. Methods for determining the fair value of financial instruments are described in Note 2.5.

Deferred tax assets

Deferred tax assets are recognised in respect of tax losses to the extent that it is probable that future taxable profit will be available, against which the losses can be utilised. Judgement is required to determine the amount of deferred tax assets that can be recognised, based upon the likely timing and level of future taxable profits.

Revenue and expenses from sale of insurance products bundled with loans

Revenue from sale of insurance products bundled with loans are split into interest income and fee and commission income based on the relative fair value analysis of each of these products.

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.

The Bank leads in case of insurance policies bundled with loans to upfront recognition less than 8% of bancassurance income associated with cash and car loans and 0% to approximately 20% of bancassurance income associated with mortgage loans. Recognition of the remaining part of the income is spread over the economic life of the associated loans. Expenses directly linked to the sale of insurance products are recognised using the same pattern.

Liabilities due to post-employment employee benefits

The costs of post-employment employee benefits are determined using an actuarial valuation method. The actuarial valuation involves making assumptions about discount rates, future salary increases, mortality rates and other factors. Due to the long–term nature of these programmes, such estimates are subject to significant uncertainty.

Leasing

Estimates relating to leases, where the Bank is a lessee, in areas such as determination of the duration of contracts, determining the interest rate used to discount future cash flows and determination of the depreciation rate of right-of-use assets are presented in Note 2.20.

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5. Net interest income

	Year ended 31 December	
	2021	2020
Interest income		
Interest income accounted for using the effective interest method	**3 409 087**	**3 647 495**
Interest income of financial assets at amortised cost, including:	2 800 249	2 923 474
- Loans and advances	*2 489 955*	*2 637 919*
- Debt securities	*290 070*	*273 672*
- Cash and short-term placements	*18 789*	*19 995*
- Gains (losses) on non-substantial modification (net)	*(8 693)*	*(12 744)*
- Other	*10 128*	*4 632*
Interest income on financial assets at fair value through other comprehensive income	608 838	724 021
- Debt securities	*192 614*	*364 346*
- Loans and advances	*416 068*	*360 135*
- Gains (losses) on non-substantial modification (net)	*156*	*(460)*
Income similar to interest on financial assets at fair value through profit or loss, including:	**470 156**	**461 744**
Financial assets held for trading	20 863	33 914
- Loans and advances	*2 849*	*5 259*
- Debt securities	*18 014*	*28 655*
Non-trading financial assets mandatorily at fair value through profit or loss, including:	48 660	88 027
- Loans and advances	*48 660*	*88 027*
Interest income on derivatives classified into banking book	103 776	122 832
Interest income on derivatives concluded under the fair value hedge	80 103	52 717
Interest income on derivatives concluded under the cash flow hedge	216 754	164 254
Total interest income	**3 879 243**	**4 109 239**

	Year ended 31 December	
	2021	2020
Interest expenses		
Financial liabilities held for trading	(9 371)	-
Financial liabilities measured at amortised cost, including:	(216 712)	(547 643)
- Deposits	*(65 954)*	*(348 854)*
- Loans received	*(4 276)*	*(8 567)*
- Issue of debt securities	*(84 949)*	*(46 466)*
- Subordinated liabilities	*(54 733)*	*(67 888)*
- Other financial liabilities	*(4 277)*	*(73 191)*
- Leasing agreements	*(2 523)*	*(2 677)*
Other	(30 983)	(20 434)
Total interest expense	**(257 066)**	**(568 077)**

Interest income in 2021 and 2020 was affected by recognition of cumulative effect of change in estimates regarding the amounts and timing of the cash flows related to the loans which are expected to be repaid before the contractual term. The issue was described in detail in Note 4.

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Net interest income per client groups is as follows:

	Year ended 31 December	
	2021	**2020**
Interest income		
From banking sector	324 815	337 345
From other customers, including:	3 554 428	3 771 894
- individual clients	*2 069 455*	*2 073 073*
- corporate clients	*1 140 272*	*1 169 711*
- public sector	*344 701*	*529 110*
Total interest income	**3 879 243**	**4 109 239**
Interest expenses		
From banking sector	(11 308)	(16 641)
From other customers, including:	(106 076)	(437 082)
- individual clients	*(74 762)*	*(263 644)*
- corporate clients	*(18 758)*	*(159 191)*
- public sector	*(12 556)*	*(14 247)*
Debt securities issued	(84 949)	(46 466)
Subordinated liabilities	(54 733)	(67 888)
Total interest expense	**(257 066)**	**(568 077)**

6. Net fee and commission income

	Year ended 31 December	
	2021	**2020**
Fee and commission income		
Payment cards-related fees	485 768	430 242
Credit-related fees and commissions	451 338	388 317
Commissions for foreign currencies exchange	408 107	339 629
Commissions from bank accounts	361 824	222 312
Fees from brokerage activity and debt securities issue	242 102	224 935
Commissions from money transfers	191 099	147 323
Commissions due to guarantees granted and trade finance commissions	91 119	86 043
Commissions for agency service regarding sale of insurance products of external financial entities	87 574	67 958
Commissions for agency service regarding sale of other products of external financial entities	59 629	46 834
Fees from cash services	45 195	42 586
Commissions on trust and fiduciary activities	33 214	31 454
Fees from portfolio management services and other management-related fees	27 769	23 196
Other	47 577	44 421
Total fee and commission income	**2 532 315**	**2 095 250**

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	Year ended 31 December	
	2021	**2020**
Fee and commission expenses		
Payment cards-related fees	(263 552)	(226 851)
Commissions paid to external entities for sale of the Bank's products	(136 297)	(135 918)
Commissions paid for agency service regarding sale of insurance products of external financial entities	(19 943)	(15 809)
Discharged brokerage fees	(39 046)	(39 663)
Cash services	(47 096)	(44 464)
Fees to NBP and KIR and GPW Benchmark	(18 948)	(15 910)
Other discharged fees	(187 782)	(157 676)
Total fee and commission expense	**(712 664)**	**(636 291)**

7. Dividend income

	Year ended 31 December	
	2021	**2020**
Non-trading financial assets mandatorily at fair value through profit or loss	3 982	4 926
Investments in subsidiaries, joint ventures and associates accounted for using equity method	25 049	26 345
Investments in subsidiaries, joint ventures and associates accounted for using other method than equity method	1 064	-
Total dividend income	**30 095**	**31 271**

8. Net trading income

	Year ended 31 December	
	2021	**2020**
Foreign exchange result	**188 448**	**69 224**
Net exchange differences on translation	123 207	(72 656)
Net transaction gains/(losses)	65 241	141 880
Gains or losses on financial assets and liabilities held for trading	**(78 478)**	**122 242**
Derivatives, including:	(79 962)	67 160
- Interest-bearing instruments	*(101 934)*	*54 051*
- Market risk instruments	*21 972*	*13 109*
Debt securities	4 142	59 649
Loans and advances	(2 658)	(4 567)
Gains or losses from hedge accounting	**(31 653)**	**(7 742)**
Net profit on hedged items	1 091 899	(75 933)
Net profit on fair value hedging instruments	(1 110 689)	66 573
Ineffective portion of cash flow hedge	(12 863)	1 618
Total net trading income	**78 317**	**183 724**

The foreign exchange result includes profit/(loss) on spot and forward contracts, options, futures and recalculated assets and liabilities denominated in foreign currencies. The result on derivative transactions of interest-bearing instruments includes the result of swap contracts for interest rates, options and other derivatives. The result of the market risk instruments operations include profit/(loss) on: bond futures, index futures, security options, stock exchange index options, and options on futures contracts as well as the result from securities forward transactions and commodity swaps.

The Bank applies fair value hedge accounting and cash flow hedge accounting. Detailed information on hedge accounting is included in Note 19.

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9. Gains or losses on non-trading financial assets mandatorily at fair value through profit or loss

	Year ended 31 December	
	2021	2020
Equity instruments	11 091	72 041
Debt securities	(1 136)	10 710
Loans and advances	(6 211)	(65 011)
Total gains or losses on non-trading financial assets mandatorily at fair value through profit or loss	**3 744**	**17 740**

In the item Equity instruments, the Bank recognised mainly a profit resulting from revaluation to fair value of shares of Krajowa Izba Rozliczeniowa S.A. in the amount of PLN 3 122 thousand and shares in Polski Standard Płatności sp. z o.o. in the amount of PLN 6 121 thousand. In 2020 under Equity instruments, the Bank recognised a profit, resulting from the revaluation of shares in Krajowa Izba Rozliczeniowa S.A in the amount of PLN 22 639 thousand, shares in Polski Standard Płatności Sp. z o.o. in the amount of PLN 21 203 thousand as well as result from conversion and sale of VISA Inc. shares in a total amount of PLN 23 249 thousand.

10. Gains or losses on derecognition of financial assets and liabilities not measured at fair value through profit or loss

	Year ended 31 December	
	2021	2020
Gains or losses from derecognition, including:	76 544	97 809
- Financial assets at fair value through other comprehensive income	*76 490*	*60 459*
- Financial assets at amortised cost	*(19)*	*(3 985)*
- Financial liabilities at amortised cost	*73*	*41 335*
Gains or losses related to sale or revaluation of investments in subsidiaries and associates	78	(2 695)
Total gains or losses on derecognition of financial assets and liabilities not measured at fair value through profit or loss	**76 622**	**95 114**

The result from the derecognition includes the result from the sale of debt securities, as well as the result from the sale of retail mortgage loans that were transferred from mBank to mBank Hipoteczny in pooling transactions in the amount of PLN -17 250 thousand (in 2020: PLN -31 523 thousand).

The result from derecognition of financial assets at amortised cost arises mainly from the sale of individual credit exposures.

In 2020 the result from derecognition of financial liabilities at amortised cost arises mainly from substitution of liabilities with mFinance France S.A. to mBank S.A., which is described detailly in the Note 29 and the settlement of hedge accounting in connection with the derecognition of the security deposit submitted to the Bank by mFinance France.

Gains or losses on derecognition of financial assets and liabilities not measured at fair value through profit or loss by type of instrument

	Year ended 31.12.2021		Year ended 31.12.2020	
	Gains	Losses	Gains	Losses
Debt securities	98 120	(1 923)	99 924	(3 759)
Loans and advances	12 144	(31 870)	5 203	(44 894)
Deposits	-	-	37 357	(1 610)
Liabilities due to issue of debt securities	7 655	(7 582)	5 588	-
Gains or losses on derecognition of financial assets and liabilities not measured at fair value through profit or loss	**117 919**	**(41 375)**	**148 072**	**(50 263)**

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11. Other operating income

	Year ended 31 December	
	2021	**2020**
Gains from sale or liquidation of fixed assets, intangible assets, assets held for sale and inventories	2 272	4 203
Income from services provided	2 569	1 607
Net operating income due to operating lease and subleasing right-of-use assets	-	-
Rental income from investment properties	5	-
Income due to release of provisions for future commitments	11 615	16 747
Income from recovering receivables designated previously as prescribed, remitted or uncollectible	1 404	735
Income from compensations, penalties and fines received	269	311
Other	26 180	21 740
Total other operating income	**44 314**	**45 343**

Income from services provided is earned on non-banking activities.

The table below presents net operating income due to operating lease and subleasing right-of-use assets for 2021 and 2020.

	Year ended 31 December	
	2021	**2020**
Net operating income due to operating lease and subleasing right-of-use assets		
- Income from operating lease	3 275	783
- Income from right-of-use assets in sublease	9 102	11 125
- Amortisation cost of assets in operating lease and right-of-use assets	(12 377)	(11 908)
Total net operating income due to operating lease and subleasing right-of-use assets	**-**	**-**

12. Overhead costs

	Year ended 31 December	
	2021	**2020**
Staff-related expenses	(960 382)	(863 388)
Material costs, including:	(597 415)	(591 758)
- *costs of administration and real estate services*	(210 047)	(226 203)
- *IT costs*	(179 161)	(156 586)
- *marketing costs*	(127 516)	(122 366)
- *consulting costs*	(67 876)	(77 101)
- *other material costs*	(12 815)	(9 502)
Taxes and fees	(30 104)	(24 181)
Contributions and transfers to the Bank Guarantee Fund	(218 239)	(287 159)
Contributions to the Social Benefits Fund	(11 745)	(8 358)
Total overhead costs	**(1 817 885)**	**(1 774 844)**

In 2021, the item "Material costs" consists of: costs related to leases of low-value assets in the amount of PLN 452 thousand (2020: PLN 657 thousand) and costs related to variable lease payments not included in the measurement of the lease liability (included in overhead costs) in the amount of PLN 2 030 thousand (2020: PLN 1 984 thousand). Additionally in 2020 the item "Material costs" consists of costs related to short-term lease agreements in the amount of PLN 32 thousand.

Staff-related expenses in 2021 and 2020 are presented below.

	Year ended 31 December	
	2021	**2020**
Wages and salaries	(780 992)	(696 643)
Social security expenses	(127 724)	(114 974)
Remuneration concerning share-based payments, including:	(10 487)	(10 159)
- *share-based payments settled in mBank S.A. shares*	*(10 487)*	*(10 159)*
Other staff expenses	(41 179)	(41 612)
Staff-related expenses, total	**(960 382)**	**(863 388)**

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Detailed information regarding incentive programmes to which share-based payments relate, is included under the Note 43.

13. Other operating expenses

	Year ended 31 December	
	2021	**2020**
Losses from sale or liquidation of fixed assets, intangible assets, assets held for resale and inventories	(11 323)	(1 321)
Provisions for future commitments	(100 508)	(44 647)
Costs arising from provisions created for other receivables (excluding loans and advances)	(3 313)	(1 061)
Donations made	(4 858)	(3 238)
Compensation, penalties and fines paid	(7 736)	(1 938)
Direct operating expenses (including repairs and maintenance) arising from investment properties that generated rental income during the period	(2 475)	-
Direct operating expenses (including repairs and maintenance) arising from investment properties that did not generate rental income during the period	(51)	-
Impairment provisions created for tangible fixed assets and intangible assets	(5 932)	-
Debt collection related costs	(36 578)	(39 578)
Other operating costs	(39 865)	(34 189)
Total other operating expenses	**(212 639)**	**(125 972)**

The item Provisions for future commitments in 2021 includes the costs of court cases, other than cases related to foreign currency loans.

14. Impairment or reversal of impairment on financial assets not measured at fair value through profit or loss

	Year ended 31 December	
	2021	**2020**
Financial assets at amortised cost, including:	**(646 347)**	**(950 873)**
Debt securities	(1 953)	(56)
Stage 1	*(1 953)*	*(56)*
Loans and advances	(644 394)	(950 817)
Stage 1	*(142 442)*	*(3 974)*
Stage 2	*101 764*	*(113 457)*
Stage 3	*(590 398)*	*(823 266)*
POCI	*(13 318)*	*(10 120)*
Financial assets at fair value through other comprehensive income, including:	**(2 627)**	**(9 911)**
Debt securities	(3 154)	(1 251)
Stage 1	*(4 433)*	*(459)*
Stage 2	*1 279*	*(792)*
Loans and advances	527	(8 660)
Stage 1	*202*	*(827)*
Stage 2	*6 542*	*(3 967)*
Stage 3	*(6 330)*	*(3 784)*
POCI	*113*	*(82)*
Commitments and guarantees given	**(133 887)**	**(70 492)**
Stage 1	*(19 819)*	*(25 769)*
Stage 2	*25 728*	*(14 639)*
Stage 3	*(140 122)*	*(1 984)*
POCI	*326*	*(28 100)*
Net impairment losses on financial assets not measured at fair value through profit or loss	**(782 861)**	**(1 031 276)**

The level of expected credit losses presented in the table above was mainly influenced by changes in the models described in Note 3.3.6.2.2. as well as changes resulting from the measures taken to account for the credit risk resulting from the COVID-19 pandemic, described in Note 4. The level of expected credit losses was also influenced by the debt collection sales processes of the non-performing (default) portfolio, which resulted in the release of approx. PLN 70 million in 2021 (positive impact).

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15. Income tax expense

	Year ended 31 December	
	2021	**2020**
Current tax	(640 858)	(513 452)
Deferred income tax (Note 32)	105 732	33 503
Total income tax	**(535 126)**	**(479 949)**
Profit (loss) before tax	**(680 227)**	**572 996**
Tax calculated at Polish current tax rate (19%)	129 243	(108 869)
Income not subject to tax	67 556	17 198
Costs other than tax deductible costs	(731 925)	(386 528)
Inactive tax losses	-	(1 750)
Total tax liability	**(535 126)**	**(479 949)**
Effective tax rate calculation		
Profit (loss) before income tax	(680 227)	572 996
Income tax	(535 126)	(479 949)
Effective tax rate %	**(78.67)**	**83.76**

Item "Income not subject to tax" includes i.a. dividends excluded from taxation under Article 20 item 3 of Corporate Income Tax Act from 15 February 1992 (Journal of Laws 2020, item 865).

Item "Costs other than tax deductible costs" includes i.a. impact of banking tax introduced by the Act on Tax on Certain Financial Institutions from 15 January 2016 (Journal of Laws 2016, item 68) in 2020, provisions established for legal risk related to the portfolio of mortgage and housing loans in CHF and other expenses non-deductible costs according to Article 16 item 1 of Corporate Income Tax Act from 15 February 1992 (Journal of Laws 2020, item 865).

Since 1 January 2020 mBank S.A., mBank Hipoteczny S.A., mFinanse S.A. and mLeasing Sp. z o.o. established, based on Corporate Income Tax Act, Tax Capital Group of mBank ("TCG"). According to the Corporate Income Tax Act, mBank – as a dominant entity – represents TCG with respect described by tax law. In a year preceding establishing the TCG, there was no tax losses in either of the entity that is a member of TCG. The TCG agreement has been concluded for 4 years.

The current tax breakdown by country is presented below.

	Year ended 31 December	
	2021	**2020**
Poland	(613 929)	(485 816)
Czech Republic	(25 089)	(27 636)
Slovakia	(1 840)	-
Total current tax	**(640 858)**	**(513 452)**

Information about deferred income tax is presented in Note 32. The tax on the Bank's profit before tax differs from the theoretical amount that would arise using the basic tax rate of the parent as presented above.

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16. Earnings (losses) per share

Earnings (losses) per share for 12 months

	Year ended 31 December	
	2021	2020
Basic:		
Net profit (loss)	(1 215 353)	93 047
Weighted average number of ordinary shares	42 369 790	42 355 695
Net basic profit (loss) per share (in PLN per share)	**(28.68)**	**2.20**
Diluted:		
Net profit (loss), applied for calculation of diluted earnings per share	(1 215 353)	93 047
Weighted average number of ordinary shares	42 369 790	42 355 695
Adjustments for:		
- share options and subscription warrants	80 719	24 031
Weighted average number of ordinary shares for calculation of diluted earnings per share	42 450 509	42 379 726
Diluted earnings (losses) per share (in PLN per share)	**(28.63)**	**2.20**

According to IAS 33, the Bank prepares a calculation of the diluted earnings per share taking into account contingently issuable shares as part of the incentive programmes is described in the Note 43. The calculations did not include those elements of the incentive programmes, which were antidilutive for the presented reporting periods that could potentially dilute basic earnings per share in the future. The basic earnings per share are computed as the quotient of the Bank stockholders' share of the profit and the weighted average number of ordinary shares during the year.

The diluted earnings per share are calculated by as ratio of net profits attributable to Bank's shareholder and the weighted average number of ordinary shares as if all possible ordinary shares causing the dilution were replaced with shares. The Bank has two categories of potential ordinary shares causing the dilution: share options and subscription warrants. The number of diluting shares is computed as the number of shares that would be issued if all rights to shares were executed at the market price, determined as the average annual closing price of the Bank's shares.

17. Other comprehensive income

Disclosure of tax effects relating to each component of other comprehensive income	Year ended 31 December 2021			Year ended 31 December 2020		
	Before-tax amount	Tax (expense) benefit	Net amount	Before-tax amount	Tax (expense) benefit	Net amount
Items that may be reclassified subsequently to the income statement	**(2 312 002)**	**412 782**	**(1 899 220)**	**357 054**	**(101 407)**	**255 647**
Exchange differences on translation of foreign operations	4 803	-	4 803	2 854	-	2 854
Cash flow hedges	(1 113 142)	211 497	(901 645)	350 037	(66 507)	283 530
Share of other comprehensive income of entities under the equity method	(28 110)	-	(28 110)	9 898	-	9 898
Change in valuation of debt instruments at fair value through other comprehensive income	(1 175 553)	201 285	(974 268)	(5 735)	(34 900)	(40 635)
Items that will not be reclassified to the income statement	**22 400**	**(4 255)**	**18 145**	**(7 698)**	**1 463**	**(6 235)**
Actuarial gains and losses relating to post-employment benefits	8 282	(1 573)	6 709	(7 698)	1 463	(6 235)
Reclassification to investment properties	14 118	(2 682)	11 436	-	-	-
Total comprehensive income (net)	**(2 289 602)**	**408 527**	**(1 881 075)**	**349 356**	**(99 944)**	**249 412**

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The table below presents detailed information concerning other comprehensive income for the years 2021 and 2020.

	Year ended 31 December	
	2021	2020
ITEMS THAT MAY BE RECLASSIFIED SUBSEQUENTLY TO THE INCOME STATEMENT	**(1 899 220)**	**255 647**
Exchange differences on translating foreign operations	**4 803**	**2 854**
Unrealised gains or losses on exchange differences on translation of foreign operations included in other comprehensive income	4 803	2 854
Unrealised gains (positive differences) arising during the year (net)	*4 803*	*29 566*
Unrealised losses (negative differences) arising during the year (net)	-	*(26 712)*
Cash flows hedges (effective part)	**(901 645)**	**283 530**
Unrealised gains or losses included in other comprehensive income	(726 074)	416 576
Unrealized gains arising during the year (net)	-	*416 576*
Unrealized losses arising during the year (net)	(726 074)	-
Reclassification to the income statement (net)	(175 571)	(133 046)
Valuation of debt instruments at fair value through other comprehensive income (net)	**(974 268)**	**(40 635)**
Unrealised gains or losses on valuation of debt instruments included in other comprehensive income	(917 751)	2 347
Unrealised gains on debt instruments arising during the year (net)	125 396	*217 309*
Unrealised losses on debt instruments arising during the year (net)	(1 043 147)	*(214 962)*
Reclassification adjustments of gains (losses) on debt instruments to the income statement (net)	(56 517)	(42 982)
Share of other comprehensive income of entities under the equity method	**(28 110)**	**9 898**
Share of other comprehensive income of associates arising during the year (net)	(28 110)	9 898
ITEMS THAT WILL NOT BE RECLASSIFIED TO PROFIT OR LOSS	**18 145**	**(6 235)**
Actuarial gains and losses relating to post-employment benefits	**6 709**	**(6 235)**
Actuarial gains	6 709	-
Actuarial losses	-	*(6 235)*
Reclassification to investment properties	**11 436**	-
Unrealised gains or losses included in other comprehensive income	11 436	-
Unrealised gains on reclassification to investment properties arising during the year (net)	11 436	-
Total comprehensive income (net)	**(1 881 075)**	**249 412**

18. Cash and balances with central bank

	31.12.2021	31.12.2020
Cash on hand	1 347 887	1 483 489
Cash balances at central banks	10 739 721	2 455 809
Total cash and cash balances with central banks	**12 087 608**	**3 939 298**

On the basis of the Act on the National Bank of Poland of 29 August 1997, mBank holds a mandatory reserve deposit. The arithmetic mean of daily balances of the mandatory reserve that mBank is obliged to maintain during a given period in the current account with NBP amounted to:

- PLN 2 967 925 thousand for the period from 31 December 2021 to 30 January 2022,
- PLN 631 270 thousand for the period from 31 December 2020 to 30 January 2021,

As at 31 December 2021, the mandatory reserve in Central Bank bore 1.75% interest (31 December 2020: 0.10%).

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19. Financial assets and liabilities held for trading and hedging derivatives

Financial assets held for trading and hedging derivatives

	31.12.2021	31.12.2020
Derivatives	**1 866 663**	**1 605 965**
- Derivatives held for trading classified into banking book	117 278	149 749
- Derivatives held for trading classified into trading book	1 987 541	1 667 929
- Derivatives designated as fair value hedges	135 169	192 564
- Derivatives designated as cash flow hedges	28 546	627 919
- Offsetting effect	(401 871)	(1 032 196)
Debt securities	**674 085**	**699 668**
- General governments	248 906	366 517
pledged securities	*72 888*	*19 021*
- Credit institutions	104 922	132 311
- Other financial corporations	141 329	72 785
- Non-financial corporations	178 928	128 055
Loans and advances to customers	**40 426**	**187 902**
- Corporate customers	40 426	187 902
Total financial assets held for trading and hedging derivatives	**2 581 174**	**2 493 535**

Trading securities include securities used to secure sell/buy back transactions with customers, the market value of which as at 31 December 2021 amounted to PLN 72 888 thousand (31 December 2020: PLN 19 021 thousand).

Financial liabilities held for trading and hedging derivatives

	31.12.2021	31.12.2020
Derivatives, including:	**1 959 827**	**1 414 374**
- Derivatives held for trading classified into banking book	352 518	350 426
- Derivatives held for trading classified into trading book	1 919 649	1 327 734
- Derivatives designated as fair value hedges	1 057 232	7 646
- Derivatives designated as cash flow hedges	541 315	60
- Offsetting effect	(1 910 887)	(271 492)
Liabilities from short sale of securities	**84 774**	**-**
Total financial liabilities held for trading and hedging derivatives	**2 044 601**	**1 414 374**

Derivative financial instruments

The Bank has the following types of derivative instruments:

Forward currency transactions represent commitments to purchase foreign and local currencies, including outstanding spot transactions.

Futures for currencies and interest rates are contractual commitments to receive or pay a specific net value, depending on currency rate of exchange or interest rate variations, or to buy or sell a foreign currency or a financial instrument on a specified future date for a fixed price established on the organised financial market. Because futures contracts are collateralised with fair-valued cash or securities and the changes of the face value of such contracts are accounted for daily in reference to stock exchange quotations, the credit risk is marginal.

FRA contracts are similar to futures except that each FRA is negotiated individually and each requires payment on a specific future date of the difference between the interest rate set in the agreement and the current market rate on the basis of theoretical amount of capital.

Currency and interest rate swap contracts are commitments to exchange one cash flow for another cash flow. Such a transaction results in swap of currencies or interest rates (e.g., fixed to variable interest rate) or combination of all these factors (e.g., cross-currency CIRS). With the exception of specific currency swap contracts, such transactions do not result in swaps of capital. The credit risk of the Bank consists of the potential cost of replacing swap contracts if the parties fail to discharge their liabilities. This risk is monitored daily by reference to the current fair value, proportion of the face value of the contracts and market liquidity. The Bank evaluates the parties to such contracts using the same methods as for its credit business, to control the level of its credit exposure.

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Currency and interest rate options are agreements, pursuant to which the selling party grants the buying party the right, but not an obligation, to purchase (call option) or sell (put option) a specific quantity of a foreign currency or a financial instrument at a predefined price on or by a specific date or within an agreed period. In return for accepting currency or interest rate risk, the buyer offers the seller a premium. An option can be either a public instrument traded at a stock exchange or a private instrument negotiated between the Bank and a customer (private transaction). The Bank is exposed to credit risk related to purchased options only up to the balance sheet value of such options, i.e. the fair value of the options.

Market risk transactions include futures contracts as well as commodity options, equity and index options.

Face values of certain types of financial instruments provide a basis for comparing them to instruments disclosed in the statement of financial position but they may not be indicative of the value of the future cash flows or of the present fair value of such instruments. For this reason, the face values do not indicate the level of the Bank's exposure to credit risk or price change risk. Derivative instruments can have positive value (assets) or negative value (liabilities), depending on market interest or currency exchange rate fluctuations. The aggregate fair value of derivative financial instruments may be subject to strong variations.

The Bank applies fair value hedge accounting and cash flow hedge accounting. Detailed information on hedge accounting are presented below in this Note.

The fair values of derivatives held by the Bank is presented in the table below:

31.12.2021	Contract amount		Fair value	
	Buy	Sell	Assets	Liabilities
Derivatives held for trading				
Foreign exchange derivatives				
- Currency forwards	20 993 648	21 099 960	246 761	121 050
- Currency swaps	24 134 231	24 026 137	108 846	199 181
- Cross-currency interest rate swaps	9 208 434	9 340 334	10 994	102 644
- OTC currency options bought and sold	8 750 804	10 037 217	126 824	75 953
Total OTC derivatives	**63 087 117**	**64 503 648**	**493 425**	**498 828**
- Currency futures	1 225 607	1 241 309	3 263	8
Total foreign exchange derivatives	**64 312 724**	**65 744 957**	**496 688**	**498 836**
Interest rate derivatives				
- Interest rate swap, OIS	278 635 256	278 635 256	466 331	711 012
- Forward rate agreements	13 225 000	12 908 000	4 560	4 265
- OTC interest rate options	292 705	709 607	951	3 804
Total interest rate derivatives	**292 152 961**	**292 252 863**	**471 842**	**719 081**
Market risk transactions	**3 502 701**	**3 534 806**	**1 136 289**	**1 054 250**
Total derivative assets / liabilities held for trading	**359 968 386**	**361 532 626**	**2 104 819**	**2 272 167**
Hedging derivatives				
Derivatives designated as fair value hedges	30 215 660	30 215 660	135 169	1 057 232
- Interest rate swaps, OIS	30 215 660	30 215 660	135 169	1 057 232
Derivatives designated as cash flow hedges	16 685 000	16 685 000	28 546	541 315
- Interest rate swaps	16 685 000	16 685 000	28 546	541 315
Total hedging derivatives	**46 900 660**	**46 900 660**	**163 715**	**1 598 547**
Offsetting effect			**(401 871)**	**(1 910 887)**
Total recognised derivative assets/ liabilities	**406 869 046**	**408 433 286**	**1 866 663**	**1 959 827**
Short-term (up to 1 year)	156 380 579	157 048 383	1 596 891	75 330
Long-term (over 1 year)	250 488 467	251 384 903	269 772	1 884 497

31.12.2020	Contract amount		Fair value	
	Buy	Sell	Assets	Liabilities
Derivatives held for trading				
Foreign exchange derivatives				
- Currency forwards	24 062 575	23 822 486	334 168	82 238
- Currency swaps	22 982 107	23 200 135	96 393	320 710
- Cross-currency interest rate swaps	10 749 492	10 878 299	30 373	90 251
- OTC currency options bought and sold	4 478 235	4 816 593	92 278	57 809
Total OTC derivatives	**62 272 409**	**62 717 513**	**553 212**	**551 008**
- Currency futures	700 385	696 996	-	-
Total foreign exchange derivatives	**62 972 794**	**63 414 509**	**553 212**	**551 008**
Interest rate derivatives				
- Interest rate swap, OIS	231 967 530	231 967 530	949 552	821 871
- Forward rate agreements	3 100 000	2 725 000	38	48
- OTC interest rate options	343 824	398 286	170	331
Total interest rate derivatives	**235 411 354**	**235 090 816**	**949 760**	**822 250**
Market risk transactions	**2 153 766**	**2 175 532**	**314 706**	**304 902**
Total derivative assets / liabilities held for trading	**300 537 914**	**300 680 857**	**1 817 678**	**1 678 160**
Hedging derivatives				
Derivatives designated as fair value hedges	14 236 661	14 236 661	192 564	7 646
- Interest rate swaps	14 236 661	14 236 661	192 564	7 646
Derivatives designated as cash flow hedges	14 165 000	14 165 000	627 919	60
- Interest rate swaps	14 165 000	14 165 000	627 919	60
Total hedging derivatives	**28 401 661**	**28 401 661**	**820 483**	**7 706**
Offsetting effect			**(1 032 196)**	**(271 492)**
Total recognised derivative assets/ liabilities	**328 939 575**	**329 082 518**	**1 605 965**	**1 414 374**
Short-term (up to 1 year)	105 460 483	105 402 937	55 640	728 342
Long-term (over 1 year)	223 479 092	223 679 581	1 550 325	686 032

Except of valuation of derivatives, the offsetting effect includes PLN 1 616 925 thousand of placed collaterals and PLN 107 908 thousand of collaterals received in connection with the derivative transactions subject to compensation (2020 PLN 2 232 thousand and PLN 762 936 thousand respectively).

In both reporting periods, market risk transactions comprise the fair values of: stock index options, shares and other equity securities, futures for commodities, swap contracts for commodities.

As at 31 December 2021 and 31 December 2020, the Bank did not hold any financial assets and financial liabilities designated upon initial recognition as at fair value through the income statement.

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Credit quality of financial assets held for trading and derivatives according to internal rating system

Sub-portfolio	31.12.2021		31.12.2020	
	Derivatives	Loans and advances to customers	Derivatives	Loans and advances to customers
1	609 481	-	1 089 902	-
2	1 166 008	-	402 190	-
3	186 448	3 813	765 232	-
4	85 300	-	186 943	187 902
5	14 995	36 613	55 767	-
6	30	-	577	-
7	3 039	-	10 005	-
8	203 177	-	127 447	-
default	56	-	98	-
offsetting effect	(401 871)		(1 032 196)	
Total	**1 866 663**	**40 426**	**1 605 965**	**187 902**

Rating	31.12.2021	31.12.2020
	Debt securities	Debt securities
1.0 - 1.2	248 906	366 517
1.4 - 1.6	77 463	23 202
1.8 - 2.0	27 626	73 342
2.2 - 2.8	154 751	134 975
3.0 - 3.8	165 339	101 632
Total	**674 085**	**699 668**

Hedge accounting

The Group applies fair value hedge accounting and cash flow hedge accounting. Detailed information on hedge accounting is presented in these Note below.

In accordance with the IFRS9 provisions, only on the day of initial application the Bank had the opportunity to choose as its accounting policy element to continue to apply the IAS 39 hedge accounting requirements instead of the IFRS 9 requirements.

IFRS 9 requires the Bank to ensure that its hedging relationships are compliant with the risk management strategy applied by the Bank and its objectives. IFRS 9 introduces new requirements with regard to the assessment of hedge effectiveness, rebalancing of the hedge relationship as well as it prohibits voluntary discontinuation of hedge accounting (i.e. in the absence of the conditions to stop the application of hedge accounting, as defined in the standard).

The Bank decided to continue from 1 January 2018, to apply the hedge accounting requirements in accordance with IAS 39.

The Bank determines the hedge ratio based on the nominal value of the hedged item and hedging instrument and it is 1:1 (except for the fair value hedge of loan portfolios granted by mBank's Czech Branch, where the nominal value of hedging instruments is determined at an amount lower than the nominal value of the hedged item in order to take into account the risk of prepayment).

The sources of hedge ineffectiveness for hedging relationships for which the ineffectiveness arises include mismatch of cash flow dates and repricing periods, base mismatch (e.g. another WIBOR), CVA/DVA mismatch which is in hedging instrument and is not in hedged instrument and mismatch due to initial valuation of hedging instruments if a previously acquired derivative was included in hedging relationship.

Fair value hedge accounting

The Bank has been applying fair value hedge accounting. The interest rate risk is the only type of risk hedged for which hedge accounting is applied.

At the end of each month, the Bank evaluates effectiveness of the applied hedging by carrying out analysis of changes in fair value of the hedged and hedging instruments in respect of the hedged risk in order to confirm that hedging relationships are effective in accordance with the accounting policy described in Note 2.11.

Description of the hedging relation

The Bank hedges against the risk of change in fair value:

- fixed interest rate eurobonds issued by mFinance France S.A. (mFF), subsidiary of mBank, acquired by the Bank in the substitution process. The hedged risk results from changes in interest rates,
- fixed interest rate loans received by mBank from European Investment Bank. The hedged risk results from changes in interest rates,
- fixed rate bonds issued by mBank S.A. The hedged risk results from changes in interest rates,
- senior non-preferred bonds issued by mBank – fixed interest rate during five years since the issue date. The hedged risk results from changes in interest rates,
- part of the fixed interest rate mortgage portfolio granted by mBank's foreign branch in Czech Republic. The hedged risk results from changes in interest rates,
- part of portfolio of modelled deposits by mBank in PLN with economic characteristics of fixed-rate deposits. The hedged risk results from changes in interest rates.

Hedged items

The hedged items are:

- one tranche of fixed interest rate eurobonds issued by mFF, acquired by the Bank in the substitution process, with a total nominal value of CHF 200 000 thousand,
- fixed interest rate loans received by mBank from European Investment Bank with a nominal value of CHF 113 110 thousand, CHF 175 560 thousand and CHF 138 388 thousand,
- fixed rate bonds issued by mBank S.A. with a nominal value of CHF 305 000 thousand,
- fixed rate bonds issued by mBank S.A. with a nominal value of EUR 460 030 thousand,
- senior non-preferred bonds issued by mBank S.A., fixed rate during five years since the issue date, with nominal value of EUR 500 000 thousand,
- part of the fixed interest rate mortgage portfolio, denominated in CZK, granted by mBank's foreign branch in the Czech Republic,
- part of portfolio of modelled deposits by mBank in PLN with economic characteristics of fixed-rate deposits.

Hedging instruments

Interest Rate Swap and Overnight Index Swap 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 assets and 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 interest cost of interest part of valuation of hedging instruments, presented in item "Interest income/cost on derivatives concluded under the fair value hedge accounting".

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Hedged items – fair value hedges

31.12.2021	Carrying amount of the hedged items in the statement of financial position	Accumulated amount of fair value hedge adjustment of hedged item included in carrying amount of hedged item recognised in the statement of financial position	The line item in the statement of financial position that includes hedged item	The change in value of the hedged item used as the basis for recognising hedge ineffectiveness for the period
Fixed interest rate mortgage loans in CZK	1 203 178	(110 033)	Financial assets at amortised cost – Loans and advances to customers	(98 871)
Bonds issued by mBank S.A. with a fixed interest rate (including those subject to substitution)	(6 658 576)	18 305	Financial liabilities measured at amortised cost – Debt securities issued	52 872
Fixed interest rate loans received by mBank from European Investment Bank	(1 906 621)	(5 131)	Financial liabilities measured at amortised cost – Amounts due to customers – Loans and advances received	33 782
Deposits modelled by mBank in PLN with economic characteristics of fixed-rate deposits	(12 315 000)	1 055 478	Financial liabilities measured at amortised cost – Amounts due to customers - deposits	1 104 116
TOTAL				**1 091 899**

31.12.2020	Carrying amount of the hedged items in the statement of financial position	Accumulated amount of fair value hedge adjustment of hedged item included in carrying amount of hedged item recognised in the statement of financial position	The line item in the statement of financial position that includes hedged item	The change in value of the hedged item used as the basis for recognising hedge ineffectiveness for the period
Fixed interest rate mortgage loans in CZK	820 225	(10 986)	Financial assets at amortised cost – Loans and advances to customers	(10 850)
Bonds issued by mBank S.A. with a fixed interest rate (including those subject to substitution	(6 300 149)	(34 567)	Financial liabilities measured at amortised cost – Debt securities issued	(3 227)
Fixed interest rate loans received by mBank from European Investment Bank	(2 331 637)	(46 568)	Financial liabilities measured at amortised cost – Amounts due to customers – Loans and advances received	(20 815)
Deposits modelled by mBank in PLN with economic characteristics of fixed-rate deposits	(4 980 000)	(48 638)	Financial liabilities measured at amortised cost – Amounts due to customers - deposits	(48 638)
Fixed interest rate security deposits given by mFF	-	-	-	7 597
TOTAL				**(75 933)**

The change in value of the hedging item used as the basis for recognising hedge ineffectiveness for the period – fair value hedging

	31.12.2021	31.12.2020
Instruments hedging fixed interest rate mortgage portfolio denominated in CZK	79 233	8 215
Instruments hedging bonds issued by mBank S.A. with a fixed interest rate (including those subject to substitution)	(73 415)	(3 786)
Instruments hedging fixed interest rate loans received by mBank from European Investment Bank	(33 362)	20 667
Instruments hedging deposits modelled by mBank in PLN with economic characteristics of fixed-rate deposits	(1 083 145)	41 477
Total	**(1 110 689)**	**66 573**

Nominal values of hedging derivatives - fair value hedges

	up to 1 month	1-3 months	3-12 months	1-5 years	over 5 years	Total
31.12.2021	1 561 922	5 618 307	4 028 766	18 391 062	615 603	**30 215 660**
31.12.2020	-	-	1 973 219	11 673 344	590 098	**14 236 661**

The increase in the nominal value of hedging instruments with maturities of up to 3 months results from the conversion by the LCH clearing house of IRS transactions based on LIBOR indices into a combination of short-term IRS and OIS transactions and a long-term OIS transaction based on the alternative rate for LIBOR.

The total results of fair value hedge accounting recognised in the income statement

for period	Year ended 31 December 2021	Year ended 31 December 2020
Interest income on derivatives concluded under the fair value hedge accounting (Note 5)	80 103	52 717
Net profit on hedged items (Note 8)	1 091 899	(75 933)
Net profit on fair value hedging instruments (Note 8)	(1 110 689)	66 573
The total result of fair value hedge accounting recognised in the income statement	**61 313**	**43 357**

Cash flow hedge accounting

Cash flow hedge accounting of the part of loans at a variable interest rate indexed to the market rate portfolio, granted by the Bank

The Bank applies cash flow hedge accounting of the part of loans at a variable interest rate indexed to the market rate portfolio, granted by the Bank. An Interest Rate Swap is the hedging instrument changing the variable interest rate to a fixed interest rate. The interest rate risk is the hedged risk within applied by the Bank cash flow hedge accounting. The ineffective portion of the gains or losses on the hedging instrument is presented in Note 8 in the position "Other net trading income and result on hedge accounting". Portion of the gains or losses on the hedging instrument that is an effective hedge, is presented in the statement of comprehensive income as "Cash flow hedges (net)".

Hedged items – cash flow hedges

	Nominal value of hedged items		The change in value of the hedged item used as the basis for recognising hedge ineffectiveness for the period		The balances in the cash flow hedge reserve for continuing hedges	
	31.12.2021	31.12.2020	31.12.2021	31.12.2020	31.12.2021	31.12.2020
Loans and advances to customers - loans in variable interest rate indexed to the market rate	16 685 000	14 165 000	613 321	(511 146)	(495 965)	405 680

The change in value of the hedging item used as the basis for recognising hedge ineffectiveness for the period – cash flow hedges

	31.12.2021	31.12.2020
Instruments hedging loans and advances to customers - loans in variable interest rate indexed to the market rate	(624 867)	501 189

Nominal values of hedging derivatives - cash flow hedges

31.12.2021	up to 1 month	1-3 months	3-12 months	1-5 years	over 5 years	Total
INTEREST RATE RISK						
Interest rate swaps hedging cash flows arising from granted loans with a variable interest rate denominated in PLN						
Nominal value (PLN thousand)	530 000	350 000	3 595 000	12 010 000	200 000	**16 685 000**
The average rate of fixed leg	2.074%	1.952%	2.121%	1.595%	1.928%	

31.12.2020	up to 1 month	1-3 months	3-12 months	1-5 years	over 5 years	Total
INTEREST RATE RISK						
Interest rate swaps hedging cash flows arising from granted loans with a variable interest rate denominated in PLN						
Nominal value (PLN thousand)	300 000	70 000	650 000	12 945 000	200 000	**14 165 000**
The average rate of fixed leg	1.838%	2.283%	2.163%	1.825%	1.928%	

The period from January 2022 to August 2029 is the period in which the cash flows are expected, and when they are expected to have an impact on the results.

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Below is given the timetable prepared as at 31 December 2021 and 31 December 2020, presenting the periods in which the cash flows from loans secured under the cash flow hedge accounting are expected and their impact on the income statement.

	up to 3 months	period from 3 months to 1 year	period from 1 to 5 years	over 5 years
31.12.2021	99 851	423 499	619 887	15 754
31.12.2020	6 865	13 122	92 059	9 974

The following note presents other comprehensive income due to cash flow hedges in the period between 1 January and 31 December 2021 and 1 January and 31 December 2020.

for period	Year ended 31 December	
	2021	2020
Other gross comprehensive income from cash flow hedge at the beginning of the period	**500 839**	**150 802**
Unrealised gains/losses included in other gross comprehensive income during the reporting period	(896 388)	514 291
The amount transferred in the period from comprehensive income to income statement	(216 754)	(164 254)
- net interest income	*(216 754)*	*(164 254)*
Accumulated other gross comprehensive income at the end of the reporting period	**(612 303)**	**500 839**
Deferred income tax on accumulated other comprehensive income at the end of the reporting period	116 338	(95 159)
Accumulated other net comprehensive income at the end of the reporting period	**(495 965)**	**405 680**
Impact on other comprehensive income in the reporting period (gross)	(1 113 142)	350 037
Deferred tax on cash flow hedges	211 497	(66 507)
Impact on other comprehensive income in the reporting period (net)	**(901 645)**	**283 530**

for period	Year ended 31 December	
	2021	2020
Gains/losses recognised in comprehensive income (gross) during the reporting period, including:		
Unrealised gains/losses included in other comprehensive income (gross)	(1 113 142)	350 037
Results of cash flow hedge accounting recognised in the income statement	203 891	165 872
- amount included as interest income in income statement during the reporting period (Note 5)	*216 754*	*164 254*
- ineffective portion of hedge recognised included in other net trading income in income statement (Note 8)	*(12 863)*	*1 618*
Impact on other comprehensive income in the reporting period (gross)	**(909 251)**	**515 909**

Impact of the IBOR reform

Following the amendments to IFRS 9, IAS 39 and IFRS 7, Interest Rate Benchmark Reform - Phase 2, as described in Note 2.28, and as a result of the reform of the interest rate benchmarks and its replacement with a risk-free alternative interest rates, the Bank has established a project to manage the change for any of its contracts that may be affected. The specific impact of IBOR reform on the Bank's hedge accounting activity is being managed as part of the overall project to implement IBOR reform at the Bank.

In preparing the 2019 financial statements, the Bank opted for early application of the amendments under Phase 1 of the interest rate benchmark reform: the amendments to IFRS 9/IAS 39 and IFRS 7. The amendments in question modified certain requirements for hedge accounting, allowing it to continue to be applied to hedging relationships covered by the amendments during the period of uncertainty before the hedged items or hedging instruments change as a result of the interest rate benchmark reform.

In 2021, the Bank has applied for the first time the amendments to IFRS 9 Financial Instruments, IAS 39 Financial Instruments: Recognition and Measurement, IFRS 7 Financial Instruments: Disclosures, IFRS 4 Insurance Contracts and IFRS 16 Leases under Interest Rate Benchmark Reform - Phase 2, published in August 2020.

Application of the abovementioned Phase 1 measures allowed to maintain the hedge relationships despite uncertainty related to the value and timing of the hedged cashflows resulting from interest rate benchmark reform and lack of ability to separate reference rate interest rate component in case of IBOR related fair value hedges.

The Bank was also not required to cease hedge accounting if retrospective assessment of hedge effectiveness of relation impacted by interest rate benchmark reform was outside of 80-125% effectiveness range. In the current reporting period no hedge relations were outside of the above-mentioned range.

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The Bank retained cumulative gains or losses in the cash flow hedge reserve for designated cash flow hedges related to IBORs subject to the interest rate benchmark reform despite the uncertainty caused by the interest rate benchmark reform related to the timing and amount of cash flows from the hedged items. In cases where the hedged future cash flows are no longer expected for reasons other than the interest rate benchmark reform, the cumulative gain or loss would be immediately reclassified to profit or loss.

Bank will be taking advantage of the measures resulting from changes to IAS 39/IFRS 9 introduced within Phase 1 until uncertainty related to timing and amount of cashflows resulting from the interest benchmark reform ceases to impact the Bank. The above-mentioned uncertainty will be impacting the Bank until IBOR related contracts are amended to include clauses regulating replacement of reference benchmark and establishing alternative reference rate including fixed spread as basis for contractual cashflows

As a result of the Phase 2 amendments, in cases where the contractual terms of non-derivative financial instruments have been changed as a direct result of the interest rate benchmark reform and the new basis for determining contractual cash flows is economically equivalent to the previous basis (i.e. the basis immediately before the change), the Bank has changed the basis for determining contractual cash flows prospectively by changing the effective interest rate. Where additional changes were made that are not directly related to the reform, the relevant requirements under IFRS 9 were applied to such changes.

In cases were the interest rate benchmark reform resulted in conversion of the hedging instrument, the Bank updated the hedging documentation without terminating the hedge relationship.

Additionally for cashflow hedge relationships, if the hedged item was modified as a result of the interest rate benchmark reform, the cumulated profits or losses recognised in the cashflow hedge reserve related to IBOR hedge relations are treated as if they were calculated based on alternative reference rate.

In December 2021, the LCH clearing house converted the LIBOR CHF based derivative instruments used in hedge relations to equivalent instruments based on SARON (risk free rate). After this conversion the Bank has only such LIBOR CHF based hedging instruments, for which the last repricing period began before the end of 2021, that is, before cessation of LIBOR CHF publishing. All other derivative instruments designated in hedge relations are based on SARON, WIBOR, PRIBOR or EURIBOR rates.

20. Non-trading financial assets mandatorily at fair value through profit or loss

	31.12.2021	31.12.2020
Equity instruments	**148 466**	**136 480**
- Other financial corporations	148 166	136 480
- Non-financial corporations	300	-
Debt securities	**81 128**	**76 068**
- Other financial corporations	81 128	76 068
Loans and advances to customers	**991 469**	**1 372 481**
- Individual customers	948 636	1 216 809
- Corporate customers	42 693	154 939
- Public sector customers	140	733
Total non-trading financial assets mandatorily at fair value through profit or loss	**1 221 063**	**1 585 029**
Short-term (up to 1 year) gross	886 275	1 054 912
Long-term (over 1 year) gross	334 788	530 117

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Credit quality of non-trading financial assets mandatorily at fair value through profit or loss according to internal rating system

Rating	Debt securities	
	31.12.2021	31.12.2020
1.4 - 1.6	81 128	-
1.8 - 2.0	-	76 068
Total	**81 128**	**76 068**

Sub-portfolio	Loans and advances to customers	
	31.12.2021	31.12.2020
1	2 113	15 450
2	99 363	240 577
3	155 765	202 580
4	307 060	440 053
5	290 856	248 674
6	28 681	22 282
7	69 635	59 856
default	37 996	143 009
Total	**991 469**	**1 372 481**

21. Financial assets at fair value through other comprehensive income

31.12.2021	Carrying amount	Gross carrying amount				Accumulated impairment			
		Stage 1	Stage 2	Stage 3	POCI	Stage 1	Stage 2	Stage 3	POCI
Debt securities	**35 971 403**	**35 936 194**	**43 948**	**-**	**-**	**(8 151)**	**(588)**	**-**	**-**
- Central banks	8 495 243	8 496 392	-	-	-	(1 149)	-	-	-
- General governments, including:	24 502 235	24 505 730	-	-	-	(3 495)	-	-	-
pledged assets	*644 292*	*644 292*	-	-	-	-	-	-	-
- Credit institutions	754 251	754 468	-	-	-	(217)	-	-	-
- Other financial corporations, including:	1 639 729	1 597 246	43 948	-	-	(877)	(588)	-	-
pledged assets	*107 957*	*107 957*	-	-	-	-	-	-	-
- Non-financial corporations	579 945	582 358	-	-	-	(2 413)	-	-	-
Loans and advances to customers	**18 191 254**	**18 059 705**	**114 831**	**31 557**	**402**	**(3 520)**	**(2 758)**	**(9 003)**	**40**
- Individual customers	18 191 254	18 059 705	114 831	31 557	402	(3 520)	(2 758)	(9 003)	40
Total financial assets at fair value through other comprehensive income	**54 162 657**	**53 995 899**	**158 779**	**31 557**	**402**	**(11 671)**	**(3 346)**	**(9 003)**	**40**

Short-term (up to 1 year) gross	16 757 963
Long-term (over 1 year) gross	37 428 674

31.12.2020	Carrying amount	Gross carrying amount				Accumulated impairment			
		Stage 1	Stage 2	Stage 3	POCI	Stage 1	Stage 2	Stage 3	POCI
Debt securities	**35 216 599**	**35 110 658**	**111 568**	**-**	**-**	**(3 716)**	**(1 911)**	**-**	**-**
- Central banks	149 997	149 997	-	-	-	-	-	-	-
- General governments, including:	32 411 761	32 411 848	-	-	-	(87)	-	-	-
pledged assets	*1 243 749*	*1 243 749*	-	-	-	-	-	-	-
- Credit institutions	747 934	748 124	-	-	-	(190)	-	-	-
- Other financial corporations	1 373 371	1 374 996	-	-	-	(1 625)	-	-	-
- Non-financial corporations	533 536	425 693	111 568	-	-	(1 814)	(1 911)	-	-
Loans and advances to customers	**12 515 013**	**10 897 552**	**1 616 606**	**16 461**	**548**	**(3 394)**	**(8 266)**	**(4 426)**	**(68)**
- Individual customers	12 515 013	10 897 552	1 616 606	16 461	548	(3 394)	(8 266)	(4 426)	(68)
Total financial assets at fair value through other comprehensive income	**47 731 612**	**46 008 210**	**1 728 174**	**16 461**	**548**	**(7 110)**	**(10 177)**	**(4 426)**	**(68)**

Short-term (up to 1 year) gross	13 111 119
Long-term (over 1 year) gross	34 642 274

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As at 31 December 2021, the carrying amounts of debt securities with fixed interest rates amounted to PLN 24 309 495 thousand and debt securities with variable interest rates PLN 11 670 647 thousand (31 December 2020: PLN 20 372 229 thousand and PLN 14 849 997 thousand).

The above note includes government bonds pledged under the Bank Guarantee Fund (BFG), government bonds pledged as sell/buy back transactions, government bonds pledged as collateral for the loans received from the European Investment Bank.

In accordance with the Act of 10 June 2016 on the Bank Guarantee Fund (BFG), Deposit Guarantee Scheme and Resolution, as at 31 December 2021 the Bank held government bonds and bills included in the statement of financial position in the amount of PLN 603 504 thousand with a nominal value of PLN 645 000 thousand, which were pledged as collateral for the BFG and were deposited in a separate account at the National Depository of Securities (31 December 2020: PLN 638 044 thousand and PLN 610 660 thousand, respectively).

In addition, as at 31 December 2021, the Bank held government bonds, which were securing the payment commitment to the BFG guarantee fund and forced restructuring fund in the amount of PLN 57 029 thousand.

Movements in expected credit losses allowance on financial assets at fair value through other comprehensive income

Changes between 1 January and 31 December 2021	As at the beginning of the period	Transfer to Stage 1	Transfer to Stage 2	Transfer to Stage 3	New financial assets originated or purchased	Financial assets derecognised during the period	Changes in credit risk	Changes due to new default definition	As at the end of the period
Debt securities	**(5 627)**	**-**	**-**	**-**	**(11 980)**	**9 206**	**(338)**	**-**	**(8 739)**
Stage 1	(3 716)	(125)	327	-	(11 980)	6 894	449	-	(8 151)
Stage 2	(1 911)	125	(327)	-	-	2 312	(787)	-	(588)
Loans and advances to customers	**(16 154)**	**-**	**-**	**-**	**(613)**	**1 875**	**(4 588)**	**4 239**	**(15 241)**
Stage 1	(3 394)	(11 896)	913	192	(613)	289	9 816	1 173	(3 520)
Stage 2	(8 266)	11 099	(1 118)	1 288	-	376	(7 298)	1 161	(2 758)
Stage 3	(4 426)	797	205	(1 480)	-	1 210	(7 190)	1 881	(9 003)
POCI	(68)	-	-	-	-	-	84	24	40
Expected credit loss allowance, total	**(21 781)**	**-**	**-**	**-**	**(12 593)**	**11 081**	**(4 926)**	**4 239**	**(23 980)**

Changes between 1 January and 31 December 2020	As at the beginning of the period	Transfer to Stage 1	Transfer to Stage 2	Transfer to Stage 3	New financial assets originated or purchased	Financial assets derecognised during the period	Changes in credit risk	As at the end of the period
Debt securities	**(4 362)**	**-**	**-**	**-**	**(1 978)**	**2 210**	**(1 497)**	**(5 627)**
Stage 1	(3 242)	-	182	-	(1 978)	2 192	(870)	(3 716)
Stage 2	(1 120)	-	(182)	-	-	18	(627)	(1 911)
Loans and advances to customers	**(8 138)**	**-**	**-**	**-**	**(814)**	**1 327**	**(8 529)**	**(16 154)**
Stage 1	(2 874)	(14 248)	1 988	5	(912)	348	12 299	(3 394)
Stage 2	(4 560)	13 742	(2 162)	1 202	-	360	(16 848)	(8 266)
Stage 3	(693)	506	174	(1 207)	-	619	(3 825)	(4 426)
POCI	(11)	-	-	-	98	-	(155)	(68)
Expected credit loss allowance, total	**(12 500)**	**-**	**-**	**-**	**(2 792)**	**3 537**	**(10 026)**	**(21 781)**

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Explanation of changes in the financial instruments gross carrying amount impacting the changes on expected credit losses allowance

Changes between 1 January and 31 December 2021	As at the beginning of the period	Transfer to Stage 1	Transfer to Stage 2	Transfer to Stage 3	New financial assets originated or purchased	Financial assets derecognised during the period	Changes in credit risk	As at the end of the period
Debt securities	**35 222 226**	**-**	**-**	**-**	**16 190 155**	**(15 664 156)**	**231 917**	**35 980 142**
Stage 1	35 110 658	-	(43 749)	-	16 190 155	(15 552 588)	231 718	35 936 194
Stage 2	111 568	-	43 749	-	-	(111 568)	199	43 948
Loans and advances to customers	**12 531 167**	**-**	**-**	**-**	**7 465 867**	**(2 057 978)**	**267 439**	**18 206 495**
Stage 1	10 897 552	1 305 452	(44 633)	(9 918)	7 455 114	(1 811 567)	267 705	18 059 705
Stage 2	1 616 606	(1 300 163)	46 292	(11 756)	8 288	(244 385)	(51)	114 831
Stage 3	16 461	(5 289)	(1 659)	21 674	2 465	(2 026)	(69)	31 557
POCI	548	-	-	-	-	-	(146)	402
Financial assets at fair value through other comprehensive income, gross	**47 753 393**	**-**	**-**	**-**	**23 656 022**	**(17 722 134)**	**499 356**	**54 186 637**

Changes between 1 January and 31 December 2020	As at the beginning of the period	Transfer to Stage 1	Transfer to Stage 2	Transfer to Stage 3	New financial assets originated or purchased	Financial assets derecognised during the period	Changes in credit risk	As at the end of the period
Debt securities	**21 881 319**	**-**	**-**	**-**	**21 303 582**	**(7 764 380)**	**(198 295)**	**35 222 226**
Stage 1	21 840 198	-	(96 872)	-	21 298 904	(7 764 380)	(167 192)	35 110 658
Stage 2	41 121	-	96 872	-	4 678	-	(31 103)	111 568
Loans and advances to customers	**8 429 828**	**-**	**-**	**-**	**5 184 208**	**(1 594 527)**	**511 658**	**12 531 167**
Stage 1	7 907 525	273 340	(816 435)	(8 130)	4 617 110	(1 515 519)	439 661	10 897 552
Stage 2	519 400	(273 340)	816 983	(6 515)	566 236	(78 245)	72 087	1 616 606
Stage 3	2 796	-	(548)	14 093	862	(763)	21	16 461
POCI	107	-	-	552	-	-	(111)	548
Financial assets at fair value through other comprehensive income, gross	**30 311 147**	**-**	**-**	**-**	**26 487 790**	**(9 358 907)**	**313 363**	**47 753 393**

Credit quality of financial assets at fair value through other comprehensive income according to internal rating system

As at 31 December 2021	Stage 1	Stage 2	Stage 3	POCI	TOTAL
Debt securities at fair value through other comprehensive income					
1.0 - 1.2	34 452 644	-	-	-	34 452 644
1.4 - 1.6	523 627	-	-	-	523 627
1.8 - 2.0	66 102	-	-	-	66 102
2.2 - 2.8	528 600	-	-	-	528 600
3.0 - 3.8	332 443	-	-	-	332 443
4.0 - 5.0	32 778	43 948	-	-	76 726
Gross carrying amount	**35 936 194**	**43 948**	**-**	**-**	**35 980 142**
Accumulated impairment	(8 151)	(588)	-	-	(8 739)
Total carrying amount	**35 928 043**	**43 360**	**-**	**-**	**35 971 403**

As at 31 December 2021	Stage 1	Stage 2	Stage 3	POCI	TOTAL
Loans and advances to customers at fair value through other comprehensive income					
1	10 605 457	12 135	-	-	10 617 592
2	6 552 069	28 926	-	-	6 580 995
3	597 085	13 488	-	-	610 573
4	226 746	9 648	-	-	236 394
5	53 839	10 758	-	-	64 597
6	6 177	4 766	-	-	10 943
7	18 332	35 110	-	-	53 442
default	-	-	31 557	402	31 959
Gross carrying amount	**18 059 705**	**114 831**	**31 557**	**402**	**18 206 495**
Accumulated impairment	(3 520)	(2 758)	(9 003)	40	(15 241)
Total carrying amount	**18 056 185**	**112 073**	**22 554**	**442**	**18 191 254**

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As at 31 December 2020	Stage 1	Stage 2	Stage 3	POCI	TOTAL
Debt securities at fair value through other comprehensive income					
1.0 - 1.2	33 506 322	-	-	-	33 506 322
1.4 - 1.6	525 610	-	-	-	525 610
1.8 - 2.0	460 856	-	-	-	460 856
2.2 - 2.8	217 712	-	-	-	217 712
3.0 - 3.8	400 158	68 206	-	-	468 364
unrated	-	43 362	-	-	43 362
Gross carrying amount	**35 110 658**	**111 568**	**-**	**-**	**35 222 226**
Accumulated impairment	(3 716)	(1 911)	-	-	(5 627)
Total carrying amount	**35 106 942**	**109 657**	**-**	**-**	**35 216 599**

As at 31 December 2020	Stage 1	Stage 2	Stage 3	POCI	TOTAL
Loans and advances to customers at fair value through other comprehensive income					
1	5 594 653	398 232	-	-	5 992 885
2	4 780 715	905 488	-	-	5 686 203
3	384 972	125 098	-	-	510 070
4	118 551	110 786	-	-	229 337
5	17 779	45 943	-	-	63 722
6	882	6 441	-	-	7 323
7	-	24 618	-	-	24 618
default	-	-	16 461	548	17 009
Gross carrying amount	**10 897 552**	**1 616 606**	**16 461**	**548**	**12 531 167**
Accumulated impairment	(3 394)	(8 266)	(4 426)	(68)	(16 154)
Total carrying amount	**10 894 158**	**1 608 340**	**12 035**	**480**	**12 515 013**

Financial effect of collaterals

As at 31 December 2021	Gross amount	Accumulated impairment	Accumulated impairment without cash flow from collaterals	Financial effect of collaterals
Balance sheet data				
Loans and advances to customers	18 206 495	(15 241)	(22 014)	6 773
Individual customers	18 206 495	(15 241)	(22 014)	6 773
Total balance sheet data	**18 206 495**	**(15 241)**	**(22 014)**	**6 773**

As at 31 December 2020	Gross amount	Accumulated impairment	Accumulated impairment without cash flow from collaterals	Financial effect of collaterals
Balance sheet data				
Loans and advances to customers	12 531 167	(16 154)	(23 619)	7 465
Individual customers	12 531 167	(16 154)	(23 619)	7 465
Total balance sheet data	**12 531 167**	**(16 154)**	**(23 619)**	**7 465**

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22. Financial assets at amortised cost

31.12.2021	Carrying amount	Gross carrying amount				Accumulated impairment			
		Stage 1	Stage 2	Stage 3	POCI	Stage 1	Stage 2	Stage 3	POCI
Debt securities	**16 632 915**	**16 635 003**	**-**	**-**	**-**	**(2 088)**	**-**	**-**	**-**
General governments, including:	11 517 053	11 518 593	-	-	-	(1 540)	-	-	-
pledged assets	*1 361 945*	*1 361 945*	-	-	-	-	-	-	-
Credit institutions	2 640 979	2 641 308	-	-	-	(329)	-	-	-
Other financial corporations, including:	2 474 883	2 475 102	-	-	-	(219)	-	-	-
pledged assets	*462 075*	*462 075*	-	-	-	-	-	-	-
Loans and advances to banks	**11 194 916**	**11 196 202**	**-**	**-**	**-**	**(1 286)**	**-**	**-**	**-**
Loans and advances to customers	**86 499 146**	**82 108 050**	**3 822 250**	**2 939 041**	**230 771**	**(428 785)**	**(258 476)**	**(1 935 789)**	**22 084**
Individual customers	43 319 138	41 050 149	1 844 583	2 158 936	139 266	(244 702)	(198 576)	(1 439 126)	8 608
Corporate customers	43 099 288	40 977 041	1 977 667	780 104	91 505	(183 943)	(59 900)	(496 662)	13 476
Public sector customers	80 720	80 860	-	1	-	(140)	-	(1)	-
Total financial assets at amortised cost	**114 326 977**	**109 939 255**	**3 822 250**	**2 939 041**	**230 771**	**(432 159)**	**(258 476)**	**(1 935 789)**	**22 084**

Short-term (up to 1 year) gross	42 043 502
Long-term (over 1 year) gross	74 887 815

31.12.2020	Carrying amount	Gross carrying amount				Accumulated impairment			
		Stage 1	Stage 2	Stage 3	POCI	Stage 1	Stage 2	Stage 3	POCI
Debt securities	**15 952 501**	**15 952 636**	**-**	**-**	**-**	**(135)**	**-**	**-**	**-**
General governments, including:	11 303 908	11 303 908	-	-	-	-	-	-	-
pledged assets	*2 705 060*	*2 705 060*	-	-	-	-	-	-	-
Credit institutions	1 984 770	1 984 770	-	-	-	-	-	-	-
Other financial corporations	2 663 823	2 663 958	-	-	-	(135)	-	-	-
Loans and advances to banks	**10 845 844**	**10 846 771**	**-**	**-**	**-**	**(927)**	**-**	**-**	**-**
Loans and advances to customers	**82 729 021**	**73 397 394**	**8 552 628**	**3 521 765**	**288 681**	**(274 423)**	**(332 339)**	**(2 371 638)**	**(53 047)**
Individual customers	42 329 891	36 161 542	5 739 367	2 087 515	108 829	(159 499)	(278 243)	(1 322 037)	(7 583)
Corporate customers	40 255 292	37 093 935	2 811 096	1 434 249	179 852	(114 681)	(54 095)	(1 049 600)	(45 464)
Public sector customers	143 838	141 917	2 165	1	-	(243)	(1)	(1)	-
Total financial assets at amortised cost	**109 527 366**	**100 196 801**	**8 552 628**	**3 521 765**	**288 681**	**(275 485)**	**(332 339)**	**(2 371 638)**	**(53 047)**

Short-term (up to 1 year) gross	41 574 463
Long-term (over 1 year) gross	70 985 412

The above note includes government bonds pledged under the Bank Guarantee Fund and government bonds pledged as collateral for the loans received from the European Investment Bank.

In addition the Bank held government bonds, which were securing the payment commitment to the BFG guarantee fund and forced restructuring fund in the amount of PLN 305 374 thousand (31 December 2020: PLN 244 046 thousand).

In the item loans and advances granted to individual customers were also included loans granted to microenterprises serviced by mBank S.A. Retail Banking.

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Loans and advances to banks

	31.12.2021	31.12.2020
Current accounts	305 347	259 699
Placements with other banks (up to 3 months)	30 001	6 135
Included in cash equivalents (Note 42)	**335 348**	**265 834**
Loans and advances	2 182 349	2 667 757
Reverse repo or buy/sell back	5 790 914	6 301 724
Other receivables	2 887 591	1 611 456
Total (gross) loans and advances to banks	**11 196 202**	**10 846 771**
Provisions created for loans and advances to banks (negative amount)	**(1 286)**	**(927)**
Total (net) loans and advances to banks	**11 194 916**	**10 845 844**
Short-term (up to 1 year) gross	8 218 331	8 148 407
Long-term (over 1 year) gross	2 977 871	2 698 364

The item "Other receivables" includes cash collaterals in the amount of PLN 691 729 thousand, placed with other banks under the derivative transactions concluded by the Bank (Note 36) (31 December 2020: PLN 593 824 thousand).

As at 31 December 2021, the variable rate loans to banks amounted to PLN 2 112 572 thousand and the fixed rate loans to banks amounted to PLN 69 777 thousand (31 December 2020: PLN 2 592 125 thousand and PLN 75 632 thousand, respectively).

As at 31 December 2021 and as at 31 December 2020 the term placements with other banks were fixed rated. An average interest rate for placements in other banks and loans granted to other banks amounted to 0.62% (31 December 2020: 0.75%).

The following table presents receivables from Polish and foreign banks:

	31.12.2021		31.12.2020	
	Loans and advances to Polish banks	Loans and advances to foreign banks	Loans and advances to Polish banks	Loans and advances to foreign banks
Gross carrying amount	4 187 735	7 008 467	3 687 624	7 159 147
Accumulated impairment	(736)	(550)	(457)	(470)
Loans and advances to banks, net	**4 186 999**	**7 007 917**	**3 687 167**	**7 158 677**

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Loans and advances to customers

Loans and advances to customers 31.12.2021	Gross carrying amount	including: Individual customers	including: Corporate customers	including: Public sector customers
Current accounts	13 709 533	7 922 189	5 785 907	1 437
Term loans, including:	74 393 760	36 884 367	37 429 969	79 424
- housing and mortgage loans to natural persons	*22 165 303*	*22 165 303*		
Reverse repo or buy/sell back	187 630	-	187 630	-
Other loans and advances	409 167	-	409 167	-
Other receivables	400 022	386 378	13 644	-
Total gross carrying amount	**89 100 112**	**45 192 934**	**43 826 317**	**80 861**

Loans and advances to customers 31.12.2021	Accumulated impairment	including: Individual customers	including: Corporate customers	including: Public sector customers
Current accounts	(841 689)	(669 456)	(172 229)	(4)
Term loans, including:	(1 757 814)	(1 204 340)	(553 337)	(137)
- housing and mortgage loans to natural persons	*(427 278)*	*(427 278)*		
Other loans and advances	(1 463)	-	(1 463)	-
Total accumulated impairment	**(2 600 966)**	**(1 873 796)**	**(727 029)**	**(141)**

Total gross carrying amount	**89 100 112**	**45 192 934**	**43 826 317**	**80 861**
Total accumulated impairment	(2 600 966)	(1 873 796)	(727 029)	(141)
Total carrying amount	**86 499 146**	**43 319 138**	**43 099 288**	**80 720**

Short-term (up to 1 year) gross	33 268 051
Long-term (over 1 year) gross	55 832 061

Loans and advances to customers 31.12.2020	Gross carrying amount	including: Individual customers	including: Corporate customers	including: Public sector customers
Current accounts	11 992 641	7 389 930	4 601 392	1 319
Term loans, including:	73 077 836	36 416 353	36 518 719	142 764
- housing and mortgage loans to natural persons	*23 607 799*	*23 607 799*		
Reverse repo or buy/sell back	103 832	-	103 832	-
Other loans and advances	278 808	-	278 808	-
Other receivables	307 351	290 970	16 381	-
Total gross carrying amount	**85 760 468**	**44 097 253**	**41 519 132**	**144 083**

Loans and advances to customers 31.12.2020	Accumulated impairment	including: Individual customers	including: Corporate customers	including: Public sector customers
Current accounts	(848 459)	(582 742)	(265 717)	-
Term loans, including:	(2 181 230)	(1 184 620)	(996 365)	(245)
- housing and mortgage loans to natural persons	*(427 300)*	*(427 300)*		
Other loans and advances	(1 758)	-	(1 758)	-
Total accumulated impairment	**(3 031 447)**	**(1 767 362)**	**(1 263 840)**	**(245)**

Total gross carrying amount	**85 760 468**	**44 097 253**	**41 519 132**	**144 083**
Total accumulated impairment	(3 031 447)	(1 767 362)	(1 263 840)	(245)
Total carrying amount	**82 729 021**	**42 329 891**	**40 255 292**	**143 838**

Short-term (up to 1 year) gross	30 494 872
Long-term (over 1 year) gross	55 265 596

As at 31 December 2021, gross amount of variable interest rate loans amounted to PLN 86 531 400 thousand and fixed interest rate loans amounted to PLN 2 568 712 thousand (31 December 2020: PLN 83 638 310 thousand and PLN 2 122 158 thousand, respectively). In 2021, an average interest rate for loans granted to customers (excluding reverse repos) amounted to 2.68% (in 2020: 3.01%).

In the item loans and advances granted to individual customers were also included loans granted to microenterprises serviced by mBank S.A. Retail Banking.

As at 31 December 2021, the above note includes receivables in the amount of PLN 222 684 thousand from the National Depository of Securities CCP in connection with the Brokerage Office activity (31 December 2020: PLN 182 801 thousand).

In addition, the item "other loans and advances" includes cash collaterals in the amount of PLN 283 160 thousand placed by the Bank under derivatives transactions (Note 36) (31 December 2020: PLN 191 307 thousand).

The currency structure of housing and mortgage loans to natural persons

	31.12.2021	31.12.2020
Housing and mortgage loans to natural persons (in PLN thousand), including:	**21 738 025**	**23 180 499**
- PLN	2 776 146	2 735 321
- CHF	9 063 602	12 295 153
- EUR	4 297 995	3 832 060
- CZK	5 407 924	4 113 213
- USD	173 638	180 718
- other	18 720	24 034
Housing and mortgage loans to natural persons in original currencies (main currencies in thousand)		
- PLN	2 776 146	2 735 321
- CHF	2 037 497	2 883 411
- EUR	934 469	830 385
- CZK	29 232 022	23 463 851
- USD	42 768	48 084

The table above presents currency breakdown of net carrying value of housing and mortgage loans measured at amortised cost granted to natural persons. The table above does not present housing and mortgage loans measured at fair value through other comprehensive income in the amount of PLN 18 191 254 thousand (31 December 2020: PLN 12 515 013 thousand), granted entirely in PLN (Note 21).

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Credit quality of financial assets at amortised cost according to internal rating system

31.12.2021	Stage 1	Stage 2	Stage 3	POCI	TOTAL
DEBT SECURITIES AT AMORTISED COST					
1.0 - 1.2	12 939 555	-	-	-	12 939 555
1.4 - 1.6	500 806	-	-	-	500 806
1.8 - 2.0	2 140 502	-	-	-	2 140 502
2.2 - 2.8	1 054 140	-	-	-	1 054 140
Total gross carrying amount	**16 635 003**	**-**	**-**	**-**	**16 635 003**
Total accumulated impairment	(2 088)	-	-	-	(2 088)
Total carrying amount	**16 632 915**	**-**	**-**	**-**	**16 632 915**
LOANS AND ADVANCES TO BANKS AT AMORTISED COST					
1	10 851 199	-	-	-	10 851 199
2	179 357	-	-	-	179 357
3	101 137	-	-	-	101 137
4	62 083	-	-	-	62 083
5	980	-	-	-	980
7	391	-	-	-	391
8	1 055	-	-	-	1 055
Total gross carrying amount	**11 196 202**	**-**	**-**	**-**	**11 196 202**
Total accumulated impairment	(1 286)	-	-	-	(1 286)
Total carrying amount	**11 194 916**	**-**	**-**	**-**	**11 194 916**
LOANS AND ADVANCES TO CUSTOMERS AT AMORTISED COST					
1	12 310 193	26 034	-	11 320	12 347 547
2	21 794 048	191 324	-	15 625	22 000 997
3	22 645 903	311 442	-	6 539	22 963 884
4	15 125 927	700 343	-	11 788	15 838 058
5	8 868 633	1 376 100	-	7 440	10 252 173
6	294 695	182 082	-	1 033	477 810
7	331 631	1 034 925	-	13 075	1 379 631
8	737 020	-	-	-	737 020
default	-	-	2 939 041	163 951	3 102 992
Total gross carrying amount	**82 108 050**	**3 822 250**	**2 939 041**	**230 771**	**89 100 112**
Total accumulated impairment	**(428 785)**	**(258 476)**	**(1 935 789)**	**22 084**	**(2 600 966)**
Total carrying amount	**81 679 265**	**3 563 774**	**1 003 252**	**252 855**	**86 499 146**

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31.12.2020	Stage 1	Stage 2	Stage 3	POCI	TOTAL
DEBT SECURITIES AT AMORTISED COST					
1.0 - 1.2	12 914 524	-	-	-	12 914 524
1.8 – 2.0	3 038 112	-	-	-	3 038 112
Total gross carrying amount	**15 952 636**	**-**	**-**	**-**	**15 952 636**
Total accumulated impairment	(135)	-	-	-	(135)
Total carrying amount	**15 952 501**	**-**	**-**	**-**	**15 952 501**
LOANS AND ADVANCES TO BANKS AT AMORTISED COST					
1	10 530 062	-	-	-	10 530 062
2	272 589	-	-	-	272 589
3	283	-	-	-	283
4	38 242	-	-	-	38 242
8	5 595	-	-	-	5 595
Total gross carrying amount	**10 846 771**	**-**	**-**	**-**	**10 846 771**
Total accumulated impairment	(927)	-	-	-	(927)
Total carrying amount	**10 845 844**	**-**	**-**	**-**	**10 845 844**
LOANS AND ADVANCES TO CUSTOMERS AT AMORTISED COST					
1	8 421 195	186 991	-	-	8 608 186
2	31 214 163	1 751 116	-	3 969	32 969 248
3	7 866 672	722 673	-	3 510	8 592 855
4	21 160 384	2 460 289	-	4 455	23 625 128
5	3 859 155	2 197 525	-	7 748	6 064 428
6	108 334	243 562	-	49	351 945
7	131 781	990 472	-	8 406	1 130 659
8	635 710	-	-	-	635 710
default	-	-	3 521 765	260 544	3 782 309
Total gross carrying amount	**73 397 394**	**8 552 628**	**3 521 765**	**288 681**	**85 760 468**
Total accumulated impairment	**(274 423)**	**(332 339)**	**(2 371 638)**	**(53 047)**	**(3 031 447)**
Total carrying amount	**73 122 971**	**8 220 289**	**1 150 127**	**235 634**	**82 729 021**

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Movements in expected credit losses allowance

Change from 1 January to 31 December 2021	As at the beginning of the period	Transfer to Stage 1	Transfer to Stage 2	Transfer to Stage 3	New financial assets originated or purchased	Financial assets derecognised during the period	Changes in credit risk	Changes due to new default definition	Write-offs	Other movements	As at the end of the period
Debt securities	**(135)**	**-**	**-**	**-**	**(384)**	**93**	**(1 662)**	**-**	**-**	**-**	**(2 088)**
Stage 1	(135)	-	-	-	(384)	93	(1 662)	-	-	-	(2 088)
Loans and advances to banks	**(927)**	**-**	**-**	**-**	**(2 638)**	**2 172**	**109**	**(2)**	**-**	**-**	**(1 286)**
Stage 1	(927)	-	-	-	(2 638)	2 172	109	(2)	-	-	(1 286)
Loans and advances to customers	**(3 031 447)**	**-**	**-**	**-**	**(235 615)**	**258 791**	**(697 727)**	**(7 007)**	**1 037 039**	**75 000**	**(2 600 966)**
Stage 1	(274 423)	(503 890)	133 631	6 816	(127 049)	85 461	261 666	(10 997)	-	-	(428 785)
Stage 2	(332 339)	485 793	(163 193)	190 501	(15 569)	47 067	(450 278)	(20 458)	-	-	(258 476)
Stage 3	(2 371 638)	18 097	29 562	(197 317)	(90 450)	125 057	(562 426)	10 860	1 027 466	75 000	(1 935 789)
POCI	(53 047)	-	-	-	(2 547)	1 206	53 311	13 588	9 573	-	22 084
Expected credit losses allowance, total	**(3 032 509)**	**-**	**-**	**-**	**(238 637)**	**261 056**	**(699 280)**	**(7 009)**	**1 037 039**	**75 000**	**(2 604 340)**

Change from 1 January to 31 December 2020	As at the beginning of the period	Transfer to Stage 1	Transfer to Stage 2	Transfer to Stage 3	New financial assets originated or purchased	Financial assets derecognised during the period	Changes in credit risk	Write-offs	Other movements	As at the end of the period
Debt securities	**(79)**	**-**	**-**	**-**	**(18)**	**-**	**(38)**	**-**	**-**	**(135)**
Stage 1	(79)	-	-	-	(18)	-	(38)	-	-	(135)
Loans and advances to banks	**(1 132)**	**-**	**-**	**-**	**(1 376)**	**1 527**	**54**	**-**	**-**	**(927)**
Stage 1	(1 132)	-	-	-	(1 376)	1 527	54	-	-	(927)
Loans and advances to customers	**(2 743 409)**	**-**	**-**	**-**	**(222 076)**	**227 236**	**(1 043 372)**	**711 397**	**38 777**	**(3 031 447)**
Stage 1	(269 215)	(398 156)	161 660	5 141	(107 400)	64 215	269 332	-	-	(274 423)
Stage 2	(217 482)	380 317	(192 594)	153 230	(20 480)	33 156	(468 486)	-	-	(332 339)
Stage 3	(2 240 936)	17 839	30 934	(158 371)	(75 254)	129 865	(822 581)	708 089	38 777	(2 371 638)
POCI	(15 776)	-	-	-	(18 942)	-	(21 637)	3 308	-	(53 047)
Expected credit losses allowance, total	**(2 744 620)**	**-**	**-**	**-**	**(223 470)**	**228 763**	**(1 043 356)**	**711 397**	**38 777**	**(3 032 509)**

Movements in expected credit losses resulting from changes in models are described in Note 3.3.6.2.2.

Explanation of changes in the gross carrying amount impacting the changes on expected credit losses allowance

Change from 1 January to 31 December 2021	As at the beginning of the period	Transfer to Stage 1	Transfer to Stage 2	Transfer to Stage 3	New financial assets originated or purchased	Financial assets derecognised during the period	Write-offs	Other changes	As at the end of the period
Debt securities	**15 952 636**	**-**	**-**	**-**	**2 840 649**	**(2 931 185)**	**-**	**772 903**	**16 635 003**
Stage 1	15 952 636	-	-	-	2 840 649	(2 931 185)	-	772 903	16 635 003
Loans and advances to banks	**10 846 771**	**-**	**-**	**-**	**8 744 195**	**(8 626 098)**	**-**	**231 334**	**11 196 202**
Stage 1	10 846 771	-	-	-	8 744 195	(8 626 098)	-	231 334	11 196 202
Loans and advances to customers	**85 760 468**	**-**	**-**	**-**	**29 182 619**	**(15 854 319)**	**(1 037 039)**	**(8 951 617)**	**89 100 112**
Stage 1	73 397 394	4 560 619	(1 360 134)	(365 615)	28 289 159	(13 995 897)	-	(8 417 476)	82 108 050
Stage 2	8 552 628	(4 460 991)	1 468 021	(539 143)	613 246	(1 505 964)	-	(305 547)	3 822 250
Stage 3	3 521 765	(99 628)	(107 887)	877 827	202 279	(266 031)	(1 027 466)	(161 818)	2 939 041
POCI	288 681	-	-	26 931	77 935	(86 427)	(9 573)	(66 776)	230 771
Financial assets at amortised cost, gross	**112 559 875**	**-**	**-**	**-**	**40 767 463**	**(27 411 602)**	**(1 037 039)**	**(7 947 380)**	**116 931 317**

Change from 1 January to 31 December 2020	As at the beginning of the period	Transfer to Stage 1	Transfer to Stage 2	Transfer to Stage 3	New financial assets originated or purchased	Financial assets derecognised during the period	Write-offs	Other changes	As at the end of the period
Debt securities	**11 234 952**	**-**	**-**	**-**	**5 880 802**	**(1 764 212)**	**-**	**601 094**	**15 952 636**
Stage 1	11 234 952	-	-	-	5 880 802	(1 764 212)	-	601 094	15 952 636
Loans and advances to banks	**7 338 835**	**-**	**-**	**-**	**7 842 246**	**(4 535 106)**	**-**	**200 796**	**10 846 771**
Stage 1	7 338 835	-	-	-	7 842 246	(4 535 106)	-	200 796	10 846 771
Loans and advances to customers	**85 113 571**	**-**	**-**	**-**	**23 798 003**	**(17 288 829)**	**(711 397)**	**(5 150 880)**	**85 760 468**
Stage 1	76 301 055	1 414 091	(5 458 720)	(666 293)	22 275 662	(15 637 170)	-	(4 831 231)	73 397 394
Stage 2	5 309 623	(1 387 399)	5 504 087	(407 987)	1 068 965	(1 280 006)	-	(254 655)	8 552 628
Stage 3	3 292 442	(26 692)	(45 367)	970 984	440 442	(360 356)	(708 089)	(41 599)	3 521 765
POCI	210 451	-	-	103 296	12 934	(11 297)	(3 308)	(23 395)	288 681
Financial assets at amortised cost, gross	**103 687 358**	**-**	**-**	**-**	**37 521 051**	**(23 588 147)**	**(711 397)**	**(4 348 990)**	**112 559 875**

The most significant changes affecting transfers between Stages in 2021 are presented below:

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- withdrawal from using additional premisses for maintaining loans subject to the moratoria in Stage 2. The total gross carrying amount reclassified during the year 2021 to the Stage 1 due to cancellation of additional premisses, amounted to PLN 2 793 million. The reclassification resulted in the recognition of additional income in the amount of PLN 43.2 million.
- In the 2021, in the model management process, Bank has implemented improvements of the sensitivity of the quantitative staging model (determining the allocation level separately for segments or product portfolios). This resulted in reclassification of PLN 1 959 million from the Stage 2 to the Stage 1, and PLN 653 million PLN from the Stage 1 to the Stage 2. Changes also included adjustments related to the implementation of Recommendation R (detailed description is provided in section 3.3.6.2.4). The impact of the changes on the expected credit loss is included in Note 3.3.6.2.2.

Financial effect of collaterals

31.12.2021	Gross amount	Accumulated impairment	Accumulated impairment without cash flow from collaterals	Financial effect of collaterals
Balance sheet data				
Loans and advances to banks	11 196 202	(1 286)	(3 863)	2 577
Loans and advances to customers, including:	89 100 112	(2 600 966)	(3 049 756)	448 790
Individual customers	45 192 934	(1 873 796)	(2 006 379)	132 583
- housing and mortgage loans to natural persons	*22 165 303*	*(427 278)*	*(537 806)*	*110 528*
Corporate customers	43 826 317	(727 029)	(1 043 214)	316 185
Public sector customers	80 861	(141)	(163)	22
Total balance sheet data	**100 296 314**	**(2 602 252)**	**(3 053 619)**	**451 367**
Off-balance sheet data				
Loan commitments and other commitments	31 067 266	(90 636)	(109 744)	19 108
Guarantees, banker's acceptances, documentary and commercial letters of credit	7 556 406	(261 198)	(268 567)	7 369
Total off-balance sheet data	**38 623 672**	**(351 834)**	**(378 311)**	**26 477**

31.12.2020	Gross amount	Accumulated impairment	Accumulated impairment without cash flow from collaterals	Financial effect of collaterals
Balance sheet data				
Loans and advances to banks	10 846 771	(927)	(1 139)	212
Loans and advances to customers, including:	85 760 468	(3 031 447)	(3 556 609)	525 162
Individual customers	44 097 253	(1 767 362)	(1 934 229)	166 867
- housing and mortgage loans to natural persons	*23 607 799*	*(427 300)*	*(568 660)*	*141 360*
Corporate customers	41 519 132	(1 263 840)	(1 622 114)	358 274
Public sector customers	144 083	(245)	(266)	21
Total balance sheet data	**96 607 239**	**(3 032 374)**	**(3 557 748)**	**525 374**
Off-balance sheet data				
Loan commitments and other commitments	31 063 320	(89 432)	(108 622)	19 190
Guarantees, banker's acceptances, documentary and commercial letters of credit	8 072 975	(132 759)	(143 911)	11 152
Total off-balance sheet data	**39 136 295**	**(222 191)**	**(252 533)**	**30 342**

The carrying amount of loans and advances to customers as at 31 December 2021, for which the Bank has not recognised a loss allowance because of the collateral amounted to PLN 2 369 688 thousand (31 December 2020 PLN 1 748 176 thousand).

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23. Investments in subsidiaries

31 December 2021

No.	Name of the company	Country of registration	Assets	Liabilities	Revenues	Net profit / (loss)	% interest held	Carrying value
1.	**BRE Property Partner Sp. z o.o.**	Poland	866	12	6	(433)	100.00	906
2.	**Future Tech Fundusz Inwestycyjny Zamknięty**	Poland	189 731	1 731	(5 731)	(6 057)	98.04	186 280
3.	**G-Invest Sp. z o.o.**	Poland	6 690	59	219	38	100.00	6 628
4.	**Herut Sp. z o.o.**	Poland	30	4	-	(9)	100.00	39
5.	**mBank Hipoteczny S.A.**	Poland	12 991 653	11 717 523	134 903	8 979	100.00	1 259 529
6.	**mBox Sp. z o.o.**	Poland	818	22	156	9	100.00	796
7.	**mElements S.A.**	Poland	26 073	4 590	8 531	(53)	100.00	21 483
8.	**mFaktoring S.A.**	Poland	3 193 780	3 045 427	55 261	19 989	100.00	152 074
9.	**mFinanse S.A.**	Poland	388 155	188 902	112 984	44 654	100.00	72 313
10.	**mInvestment Banking S.A.**	Poland	7 543	3 259	10 209	1 606	100.00	2 048
11.	**mLeasing Sp. z o.o.**	Poland	13 979 630	13 380 230	366 222	117 626	100.00	624 513
12.	**mServices Sp. z o.o.**	Poland	6 425	2 881	4 803	401	100.00	4 186
13.	**mTFI S.A.**	Poland	9 826	474	-	(648)	100.00	10 000
14.	**Octopus Sp. z o.o.**	Poland	440	1	16	(1)	99.90	50
15.	**Unitop Sp. z o.o.**	Poland	142 999	54 416	32 971	5 810	100.00	16 223
								2 357 068

** Data for Unitop Sp. z o.o. presented for the financial year running from 1 July 2020 to 30 June.*

On 22 December 2020 the Management Board of mBank S.A. decided to establish its own investment fund company by way of founding a company under the name of mTowarzystwo Funduszy Inwestycyjnych Spółka Akcyjna (mTFI S.A.). The company was formally established on 8 April 2021. The Bank acquired 100% of mTFI S.A. shares.

On 15 July 2021, mBank S.A. signed a conditional agreement for the sale of shares in the subsidiary Tele Tech Investment Sp. z o.o. and bonds issued by this company. After fulfilling the conditions precedent, on 19 July 2021, the Bank sold 100% of shares in the subsidiary and all bonds held by the Bank issued by that subsidiary.

31 December 2020

No.	Name of the company	Country of registration	Assets	Liabilities	Revenues	Net profit / (loss)	% interest held	Carrying value
1.	**BRE Property Partner Sp. z o.o.**	Poland	1 318	15	-	(506)	100.00	1 362
2.	**Future Tech Fundusz Inwestycyjny Zamknięty**	Poland	196 188	1 736	-	(7 871)	98.04	193 193
3.	**G-Invest Sp. z o.o. (previously Garbary Sp. z o.o.)**	Poland	6 655	52	72	(90)	100.00	6 602
4.	**mBank Hipoteczny S.A.**	Poland	12 889 572	11 579 669	179 816	20 262	100.00	1 276 945
5.	**mBox Sp. z o.o.**	Poland	800	29	31	2	100.00	776
6.	**mElements S.A.**	Poland	18 221	3 685	7 932	(98)	100.00	14 536
7.	**mFaktoring S.A.**	Poland	2 181 807	2 053 601	44 611	7 144	100.00	129 247
8.	**mFinance France S.A.**	Poland	-	-	2 708	895	99.998	2 349
9.	**mFinanse S.A.**	Poland	410 796	231 101	89 759	24 387	100.00	64 238
10.	**mInvestment Banking S.A.**	Poland	6 321	245	855	731	100.00	2 121
11.	**mLeasing Sp. z o.o.**	Poland	13 100 655	12 619 524	300 214	4 861	100.00	490 935
12.	**mServices Sp. z o.o.**	Poland	6 355	3 378	1 307	1 127	100.00	5 769
13.	**Octopus Sp. z o.o.**	Poland	442	1	19	4	99.90	50
14.	**Tele -Tech Investment Sp. z o.o.**	Poland	177 937	177 361	157	27	100.00	576
15.	**Unitop Sp. z o.o.**	Poland	142 605	127 213	14 765	5 933	100.00	16 223
								2 204 922

In November 2020, the liquidation process of mFinance France S.A. began. On 22 April 2021, the Ordinary Shareholders' Meeting of the company decided to finish the liquidation of the company on 22 April 2021, and thus to submit an application for company's removal from the French register of enterprises. The company was legally removed from the French register of entrepreneurs on 4 June 2021.

On 4 December 2020, the liquidation process of CSK Sp. z o.o. was completed. The company was legally removed from the National Court Register on 16 March 2021.

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Changes in investments in subsidiaries

	31.12.2021	31.12.2020
As at the beginning of the period	**2 204 922**	**2 164 112**
Foreign exchange differences	-	25
Increase	17 039	16 223
Decrease	(5 147)	(11 056)
Changes resulting from the application of the equity method, including:	140 176	37 261
- recognised in the income statement	168 286	*27 363*
- recognised in the other components of equity	(28 110)	*9 898*
Change of valuation of investment in subsidiaries not measured at equity method	78	(1 643)
As at the end of the period	**2 357 068**	**2 204 922**

24. Non-current assets and disposal groups classified as held for sale and liabilities held for sale

In December 2021 the Bank's Management Board approved the sale of real estate in Katowice at ul. Powstańców 43, owned by mBank. The property consists of an office, service building with equipment and the right of perpetual usufruct of land.

On 5 January 2022, the Bank concluded a preliminary agreement for the sale of this property and therefore, in accordance with the accounting principles described in Note 2.18, the Bank reclassified the value of the building with its equipment and the right of use perpetual usufruct of land to Non-current assets and disposal groups classified as held for sale, and the value of the lease liability related to the right of perpetual usufruct of land to the Liabilities classified as held for sale. The parties to the contract undertook to conclude the promised contract by 31 December 2022.

The financial data for assets and liabilities held for sale are presented below.

Non-current assets held for sale	31.12.2021	31.12.2020
Fixed asset	31 247	-
Total non-current assets held for sale	**31 247**	**-**

Liabilities classified as held for sale	31.12.2021	31.12.2020
Financial liabilities measured at amortised cost, including:	7 425	-
Amounts due to customers	*7 425*	-
Total liabilities classified as held for sale	**7 425**	**-**

25. Intangible assets

	31.12.2021	31.12.2020
Goodwill	-	3 532
Patents, licences and similar assets, including:	858 734	798 819
- computer software	*713 590*	*645 046*
Intangible assets under development	252 745	211 395
Total intangible assets	**1 111 479**	**1 013 746**

In 2021 and 2020, the Bank performed impairment tests of intangible assets under development. As a result of the tests, as at 31 December 2021, the Bank wrote down goodwill in the amount of PLN 3 532 thousand.

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Movements in intangible assets

Movements in intangible assets from 1 January to 31 December 2021	Patents, licences and other similar assets		Other intangible assets	Intangible assets under development	Goodwill	Total intangible assets
		Computer software				
Gross value of intangible assets as at the beginning of the period	**1 546 898**	**1 210 442**	**-**	**211 395**	**3 532**	**1 761 825**
Increase (due to):	**213 015**	**158 483**	**-**	**282 710**	**-**	**495 725**
- purchase	36 944	-	-	210 311	-	247 255
- transfer from intangible assets under development	175 786	158 371	-	-	-	175 786
- development costs	-	-	-	34 012	-	34 012
- other increases	285	112	-	38 387	-	38 672
Decrease (due to):	**(210 935)**	**(128 292)**	**-**	**(241 360)**	**(3 532)**	**(455 827)**
- liquidation	(210 929)	(128 288)	-	-	-	(210 929)
- transfer to intangible assets given to use	-	-	-	(175 786)	-	(175 786)
- other decreases	(6)	(4)	-	(65 574)	(3 532)	(69 112)
Gross value of intangible assets as at the end of the period	**1 548 978**	**1 240 633**	**-**	**252 745**	**-**	**1 801 723**
Accumulated amortisation as at the beginning of the period	**(748 079)**	**(565 396)**	**-**	**-**	**-**	**(748 079)**
Amortisation for the period (due to):	**57 835**	**38 353**	**-**	**-**	**-**	**57 835**
- amortisation	(144 014)	(80 922)	-	-	-	(144 014)
- other increases	(179)	(112)	-	-	-	(179)
- liquidation	202 028	119 387	-	-	-	202 028
Accumulated amortisation as at the end of the period	**(690 244)**	**(527 043)**	**-**	**-**	**-**	**(690 244)**
Impairment losses as at the beginning of the period	**-**	**-**	**-**	**-**	**-**	**-**
- increase	-	-	-	-	(3 532)	**(3 532)**
- decrease	-	-	-	-	3 532	**3 532**
Impairment losses at the end of the period	**-**	**-**	**-**	**-**	**-**	**-**
Net value of intangible assets as at the end of the period	**858 734**	**713 590**	**-**	**252 745**	**-**	**1 111 479**

Movements in intangible assets from 1 January to 31 December 2020	Patents, licences and other similar assets		Other intangible assets	Intangible assets under development	Goodwill	Total intangible assets
		Computer software				
Gross value of intangible assets as at the beginning of the period	**1 450 505**	**1 135 011**	**9 961**	**187 041**	**3 532**	**1 651 039**
Increase (due to):	**310 666**	**201 164**	**-**	**283 201**	**-**	**593 867**
- purchase	97 047	125	-	216 577	-	313 624
- transfer from intangible assets under development	213 072	200 895	-	-	-	213 072
- development costs	-	-	-	30 946	-	30 946
- other increases	547	144	-	35 678	-	36 225
Decrease (due to):	**(214 273)**	**(125 733)**	**(9 961)**	**(258 847)**	**-**	**(483 081)**
- liquidation	(214 273)	(125 733)	(9 961)	-	-	(224 234)
- transfer to intangible assets given to use	-	-	-	(213 072)	-	(213 072)
- other decreases	-	-	-	(45 775)	-	(45 775)
Gross value of intangible assets as at the end of the period	**1 546 898**	**1 210 442**	**-**	**211 395**	**3 532**	**1 761 825**
Accumulated amortization as at the beginning of the period	**(817 969)**	**(606 511)**	**(9 961)**	**-**	**-**	**(827 930)**
Amortization for the period (due to):	**69 890**	**41 115**	**9 961**	**-**	**-**	**79 851**
- amortization	(144 167)	(84 479)	-	-	-	(144 167)
- other increases	(216)	(139)	-	-	-	(216)
- liquidation	214 273	125 733	9 961	-	-	224 234
Accumulated amortization as at the end of the period	**(748 079)**	**(565 396)**	**-**	**-**	**-**	**(748 079)**
Net value of intangible assets as at the end of the period	**798 819**	**645 046**	**-**	**211 395**	**3 532**	**1 013 746**

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26. Tangible assets

	31.12.2021	31.12.2020
Tangible assets, including:	**417 228**	**372 004**
- land	653	653
- buildings and structures	35 860	142 961
- equipment	166 430	146 564
- vehicles	7	19
- other fixed assets	214 278	81 807
Fixed assets under construction	**62 818**	**175 560**
Right-of-use, including:	**724 634**	**698 932**
- real estate	708 604	630 829
- perpetual usufruct of land	2 177	47 670
- vehicles	13 612	19 948
- other	241	485
Total tangible assets	**1 204 680**	**1 246 496**

Movements in tangible assets

Movements in tangible assets from 1 January to 31 December 2021	Land	Buildings and structures	Equipment	Vehicles	Other tangible assets	Tangible assets under construction	Total
Gross value of tangible assets as at the beginning of the period	**653**	**313 853**	**563 920**	**47**	**332 350**	**175 560**	**1 386 383**
Increase (due to)	**-**	**-**	**98 236**	**-**	**168 022**	**193 426**	**459 684**
- purchase	-	-	31 446	-	1 596	128 157	161 199
- transfer from tangible assets under construction	-	-	66 236	-	165 266	-	231 502
- other increases	-	-	554	-	1 160	65 269	66 983
Decrease (due to)	**-**	**(223 409)**	**(77 308)**	**-**	**(46 733)**	**(306 168)**	**(653 618)**
- sale	-	-	(5 390)	-	(16 071)	-	(21 461)
- liquidation	-	-	(34 573)	-	(30 082)	-	(64 655)
- transfer to tangible assets	-	-	-	-	-	(231 502)	(231 502)
- non-current assets held for sale	-	(89 962)	(3 615)	-	(215)	-	(93 792)
- reclassification to investment properties	-	(133 447)	(32 185)	-	(365)	-	(165 997)
- other decreases	-	-	(1 545)	-	-	(74 666)	(76 211)
Gross value of tangible assets as at the end of the period	**653**	**90 444**	**584 848**	**47**	**453 639**	**62 818**	**1 192 449**
Accumulated depreciation as at the beginning of the period	**-**	**(121 622)**	**(417 356)**	**(28)**	**(250 543)**	**-**	**(789 549)**
Depreciation for the period (due to)	**-**	**87 818**	**(1 062)**	**(12)**	**11 182**	**-**	**97 926**
- depreciation charge	-	(5 147)	(77 433)	(12)	(34 138)	-	(116 730)
- other increases	-	-	(359)	-	(905)	-	(1 264)
- sale	-	-	5 358	-	15 891	-	21 249
- liquidation	-	-	34 197	-	29 754	-	63 951
- non-current assets held for sale	-	35 159	3 615	-	215	-	38 989
- reclassification to investment properties	-	57 806	32 181	-	365	-	90 352
- other decreases	-	-	1 379	-	-	-	1 379
Accumulated depreciation as at the end of the period	**-**	**(33 804)**	**(418 418)**	**(40)**	**(239 361)**	**-**	**(691 623)**
Impairment losses as at the beginning of the period	**-**	**(49 270)**	**-**	**-**	**-**	**-**	**(49 270)**
- increase	-	(2 400)	-	-	-	-	(2 400)
- decrease	-	30 890	-	-	-	-	30 890
Impairment losses as at the end of the period	**-**	**(20 780)**	**-**	**-**	**-**	**-**	**(20 780)**
Net value of tangible assets as at the end of the period	**653**	**35 860**	**166 430**	**7**	**214 278**	**62 818**	**480 046**

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Movements in tangible assets from 1 January to 31 December 2020	Land	Buildings and structures	Equipment	Vehicles	Other tangible assets	Tangible assets under construction	Total
Gross value of tangible assets as at the beginning of the period	**1 033**	**318 571**	**570 151**	**47**	**362 882**	**69 815**	**1 322 499**
Increase (due to)	**-**	**-**	**54 471**	**-**	**27 094**	**178 046**	**259 611**
- purchase	-	-	22 043	-	1 541	166 496	190 080
- transfer from tangible assets under construction	-	-	31 879	-	23 934	-	55 813
- other increases	-	-	549	-	1 619	11 550	13 718
Decrease (due to)	**(380)**	**(4 718)**	**(60 702)**	**-**	**(57 626)**	**(72 301)**	**(195 727)**
- sale	(380)	(4 718)	(7 878)	-	(14 528)	-	(27 504)
- liquidation	-	-	(52 824)	-	(43 088)	-	(95 912)
- transfer to tangible assets	-	-	-	-	-	(55 813)	(55 813)
- other decreases	-	-	-	-	(10)	(16 488)	(16 498)
Gross value of tangible assets as at the end of the period	**653**	**313 853**	**563 920**	**47**	**332 350**	**175 560**	**1 386 383**
Accumulated depreciation as at the beginning of the period	**-**	**(115 849)**	**(403 015)**	**(17)**	**(270 766)**	**-**	**(789 647)**
Depreciation for the period (due to)	**-**	**(5 773)**	**(14 341)**	**(11)**	**20 223**	**-**	**98**
- depreciation charge	-	(7 304)	(74 263)	(11)	(30 894)	-	(112 472)
- other increases	-	-	(400)	-	(1 222)	-	(1 622)
- sale	-	1 531	7 856	-	10 747	-	20 134
- liquidation	-	-	52 466	-	41 592	-	94 058
Accumulated depreciation as at the end of the period	**-**	**(121 622)**	**(417 356)**	**(28)**	**(250 543)**	**-**	**(789 549)**
Impairment losses as at the beginning of the period	**-**	**(49 270)**	**-**	**-**	**-**	**-**	**(49 270)**
Impairment losses as at the end of the period	**-**	**(49 270)**	**-**	**-**	**-**	**-**	**(49 270)**
Net value of tangible assets as at the end of the period	**653**	**142 961**	**146 564**	**19**	**81 807**	**175 560**	**547 564**

The recoverable value of impaired tangible assets is the net sale price determined on the basis of market prices for similar assets.

Movements in right-of-use assets

Movements in right-of-use from 1 January to 31 December 2021	Real estate	Perpetual usufruct of land	Vehicles	Other	Total
Gross value of right-of-use as at the beginning of the period	**821 104**	**49 046**	**32 187**	**2 015**	**904 352**
Increase (due to)	**326 136**	**-**	**3 037**	**455**	**329 628**
- new contracts	258 370	-	1 994	205	260 569
- modification of contracts	59 008	-	309	233	59 550
- other increases	8 758	-	734	17	9 509
Decrease (due to)	**(135 863)**	**(46 775)**	**(4 428)**	**(1 463)**	**(188 529)**
- termination of contracts	(9 956)	-	(1 803)	(1 313)	(13 072)
- modification of contracts	(123 186)	-	(13)	-	(123 199)
- other decreases	(2 721)	(46 775)	(2 612)	(150)	(52 258)
Gross value of right-of-use as at the end of the period	**1 011 377**	**2 271**	**30 796**	**1 007**	**1 045 451**
Accumulated depreciation as at the beginning of the period	**(190 275)**	**(1 376)**	**(12 239)**	**(1 530)**	**(205 420)**
Depreciation for the period (due to)	**(112 498)**	**1 282**	**(4 945)**	**764**	**(115 397)**
- depreciation charge	(119 501)	(412)	(8 146)	(354)	(128 413)
- other increases	(1 107)	-	(56)	(7)	(1 170)
- modification of contracts	777	-	7	-	784
- termination of contracts	7 333	-	1 303	975	9 611
- other decreases	-	1 694	1 947	150	3 791
Accumulated depreciation as at the end of the period	**(302 773)**	**(94)**	**(17 184)**	**(766)**	**(320 817)**
Net value of right-of-use as at the end of the period	**708 604**	**2 177**	**13 612**	**241**	**724 634**

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Movements in right-of-use from 1 January to 31 December 2020	Real estate	Perpetual usufruct of land	Vehicles	Other	Total
Gross value of right-of-use as at the beginning of the period	**504 797**	**49 046**	**32 528**	**1 930**	**588 301**
Increase (due to)	**370 198**	**-**	**9 333**	**85**	**379 616**
- new contracts	342 910	-	9 272	35	352 217
- modification of contracts	23 943	-	61	50	24 054
- other increases	3 345	-	-	-	3 345
Decrease (due to)	**(53 891)**	**-**	**(9 674)**	**-**	**(63 565)**
- termination of contracts	(47 346)	-	(9 674)	-	(57 020)
- modification of contracts	(6 545)	-	-	-	(6 545)
Gross value of right-of-use as at the end of the period	**821 104**	**49 046**	**32 187**	**2 015**	**904 352**
Accumulated depreciation as at the beginning of the period	**(113 734)**	**(688)**	**(11 058)**	**(797)**	**(126 277)**
Depreciation for the period (due to)	**(76 541)**	**(688)**	**(1 181)**	**(733)**	**(79 143)**
- depreciation charge	(122 427)	(688)	(7 790)	(727)	(131 632)
- other increases	(50)	-	-	(6)	(56)
- modification of contracts	1 234	-	-	-	1 234
- termination of contracts	44 702	-	6 609	-	51 311
Accumulated depreciation as at the end of the period	**(190 275)**	**(1 376)**	**(12 239)**	**(1 530)**	**(205 420)**
Net value of right-of-use as at the end of the period	**630 829**	**47 670**	**19 948**	**485**	**698 932**

27. Investment properties

Due to the change of the Bank's head office, in 2021 the Bank reclassified its building at ul. Królewska 14 in Warsaw, previously recognised as a fixed asset with a total carrying amount of PLN 75 645 thousand and the right of perpetual usufruct of land recognised as the right of use in the amount of PLN 37 747 thousand to the item "Investment properties". The difference in the revaluation of these components to fair value amounting to PLN 14 118 thousand was recognised in other comprehensive income (Note 17). The building is intended for rent.

	31.12.2021	31.12.2020
Gross value as at the beginning of the period	**-**	**-**
Increase (due to):	**127 510**	**-**
- reclassification to investment properties	113 392	-
- revaluation to fair value	14 118	-
Fair value at the end of the period	**127 510**	**-**

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28. Other assets

	31.12.2021	31.12.2020
Other assets:		
- debtors, including:	584 319	483 871
- payment cards settlements	*47 398*	*139 391*
- KDPW receivables under compensation scheme	*16 024*	*13 880*
- interbank balances	22 867	15 033
- settlements of securities transactions	26 093	35 014
- other accruals	143 817	142 457
- accrued income	77 275	91 485
- inventories	3 106	3 961
- other	-	1 432
Total other assets	**857 477**	**773 253**
Short-term (up to 1 year)	733 510	761 492
Long-term (over 1 year)	123 967	11 761

In 2021 and in 2020, the item "settlements of the securities transaction" relates entirely to the settlements of securities transactions in connection with the Brokerage Office activity.

As at 31 December 2021, the above note includes financial assets in amount of PLN 633 279 thousand (31 December 2020: PLN 533 918 thousand).

Other financial assets included in the other assets

	31.12.2021	31.12.2020
Gross other financial assets, including:	**650 200**	**550 411**
- not past due	628 963	528 947
- past due from 1 to 90 days	11 894	7 887
- past due over 90 days	9 343	13 577
Provisions for impaired assets (negative amount)	(16 921)	(16 493)
Net other financial assets	**633 279**	**533 918**

Movements of impairment allowance for other assets

	31.12.2021	31.12.2020
As at the beginning of the period	**(16 493)**	**(16 080)**
Change in the period (due to):	**(428)**	**(413)**
- increase of provisions	(3 138)	(1 097)
- release of provisions	477	466
- write-offs	2 233	271
- foreign exchange differences	-	(53)
As at the end of the period	**(16 921)**	**(16 493)**

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29. Financial liabilities measured at amortised cost

Amounts due to other banks and customers

31.12.2021	Amounts due to banks	Amounts due to customers	including:		
			Individual customers	Corporate customers	Public sector customers
Deposits	**2 264 479**	**156 135 235**	**112 225 674**	**43 302 151**	**607 410**
Current accounts	805 729	147 253 206	103 992 478	42 667 497	593 231
Term deposits	770 328	8 794 207	8 233 196	546 832	14 179
Repo or sell/buy back transactions	688 422	87 822	-	87 822	-
Loans and advances received	**-**	**1 906 621**	-	**1 906 621**	-
Other financial liabilities	**1 155 522**	**1 864 135**	**220 397**	**1 610 857**	**32 881**
Liabilities in respect of cash collaterals	988 663	704 995	75 252	629 743	-
Lease liabilities	-	953 996	-	921 117	32 879
Other	166 859	205 144	145 145	59 997	2
Total financial liabilities measured at amortised cost	**3 420 001**	**159 905 991**	**112 446 071**	**46 819 629**	**640 291**

Short-term (up to 1 year)	3 420 001	157 117 474
Long-term (over 1 year)	-	2 788 517

31.12.2020	Amounts due to banks	Amounts due to customers	including:		
			Individual customers	Corporate customers	Public sector customers
Deposits	**1 988 417**	**133 073 430**	**97 862 007**	**34 765 842**	**445 581**
Current accounts	1 349 144	121 882 297	87 703 713	33 747 457	431 127
Term deposits	-	11 097 909	10 158 294	925 161	14 454
Repo or sell/buy back transactions	639 273	93 224	-	93 224	-
Loans and advances received	**-**	**3 254 591**	**-**	**3 254 591**	**-**
Other financial liabilities	**635 869**	**1 450 013**	**114 241**	**1 295 144**	**40 628**
Liabilities in respect of cash collaterals	394 290	509 222	37 881	471 341	-
Lease liabilities	-	748 497	-	707 911	40 586
Other	241 579	192 294	76 360	115 892	42
Total financial liabilities measured at amortised cost	**2 624 286**	**137 778 034**	**97 976 248**	**39 315 577**	**486 209**

Short-term (up to 1 year)	1 984 671	133 593 182
Long-term (over 1 year)	639 615	4 184 852

In the item amounts due to individual customers liabilities to microenterprises were also included.

The average interest rate for loans obtained from banks in 2021 amounted to 0.10% (31 December 2020: 0.23%).

The Bank did not note any violations of contractual terms related to liabilities in respect of loans received.

As at 31 December 2021 and 31 December 2020, the majority of the deposits from retail and corporate customers bore fixed interest rates. The average interest rate for amounts due to customers (excluding repos) amounted to 0.04% (31 December 2020: 0.29%).

As at 31 December 2021, loans and advances received include loans received from European Investment Bank amounting to PLN 1 906 621 thousand (31 December 2020: PLN 3 254 591 thousand). The loans with fixed interest rate are collateralized with treasury bonds, which have been disclosed as pledged assets under Note 22 and Note 36.

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Lease liabilities

Lease liabilities breakdown by maturity dates is presented below.

	31.12.2021	31.12.2020
Lease liabilities breakdown by maturity dates (undiscounted)		
Up to 3 months	25 097	25 337
From 3 months to 1 year	88 839	68 370
From 1 year to 5 years	477 047	325 970
Over 5 years	396 929	352 465
Total	**987 912**	**772 142**

Debt securities issued

31 December 2021 Debt securities by type	Nominal value (currency of issue)	Carrying amount of the liability by maturity date				Total carrying amount
		up to 3 months	from 3 to 12 months	from 1 to 5 years	more than 5 years	
Bonds, including:		**-**	**2 913 146**	**1 445 730**	**2 299 700**	**6 658 576**
- EUR	960 030	-	2 103 666	-	2 299 700	4 403 366
- CHF	505 000	-	809 480	1 445 730	-	2 255 210
Deposit certificates		**-**	**15 047**	**10 000**	**-**	**25 047**
- PLN	25 000	-	15 047	10 000	-	25 047
Total		**-**	**2 928 193**	**1 455 730**	**2 299 700**	**6 683 623**

31 December 2020 Debt securities by type	Nominal value (currency of issue)	Carrying amount of the liability by maturity date				Total carrying amount
		up to 3 months	from 3 to 12 months	from 1 to 5 years	more than 5 years	
Bonds, including:		**35 267**	**1 988 566**	**4 276 316**	**-**	**6 300 149**
- EUR	887 613	28 727	1 977 495	2 122 946	-	4 129 168
- CHF	505 000	6 540	11 071	2 153 370	-	2 170 981
Deposit certificates		**16**	**20 000**	**15 000**	**-**	**35 016**
- PLN	35 000	16	20 000	15 000	-	35 016
Total		**35 283**	**2 008 566**	**4 291 316**	**-**	**6 335 165**

Bank has not registered any contractual conditions infringement related to liabilities due to debt security issuance.

Movements in debt securities issued

Movements from 1 January to 31 December	2021	2020
As at the beginning of the period	**6 335 165**	**3 361 997**
Additions (issue)	2 309 950	35 000
Disposals (redemptions)	(2 020 661)	(178 042)
Substitution with mFinance France	-	2 773 866
Exchange differences	114 185	313 437
Other changes	(55 016)	28 907
Debt securities issued as at the end of the period	**6 683 623**	**6 335 165**

Issues in 2021

- On 20 September 2021, the Bank issued senior non-preferred notes under the EMTN Programme in the total nominal value of EUR 500 000 thousand, which is the equivalent of PLN 2 299 950 thousand at the average NBP exchange rate as of 20 September 2021, maturing on 21 September 2027 (with an option of early redemption at the issuer's request on 21 September 2026). The bonds bear interest at a fixed rate of 0.966% per annum for five years from the issue date and a variable rate of EURIBOR 3M plus a margin of 1.25% throughout the sixth year.
  The bonds were admitted to trading on the regulated market of the Luxembourg Stock Exchange.
- In 2021 mBank issued certificates of deposit with a nominal value of PLN 10 000 thousand.

Redemptions in 2021

- On 26 November 2021, the Bank redeemed bonds, issued on 26 November 2014, with a total nominal value of EUR 427 583 thousand, obtained by the Bank in the substitution process.
- In 2021, mBank S.A. redeemed certificates of deposit in the amount of PLN 20 000 thousand.

Issues in 2020

- mBank issued certificates of deposits with a nominal value of PLN 35 000 thousand.
- Substitution from mFinance France S.A.

On 1 October 2020, the substitution came into force. As the result, the financial liabilities of the mFinance France towards the bondholders expired, and the corresponding liabilities towards the bondholders arose on the Bank's side. The substitution covers two series of bonds issued by the mFF as part of the established program for the issue of debt securities with a total nominal value of up to EUR 3 000 000 thousand.

a. bonds with a total nominal value of EUR 500 000 thousand, issued on 26 November 2014, with a fixed interest rate, maturing on 26 November 2021 and listed on the regulated market operated by the Luxembourg Stock Exchange. The current face value of these outstanding bonds is EUR 427 583 thousand (the equivalent of PLN 1 930 666 thousand according to the average NBP exchange rate as of 1 October 2020) and
b. bonds with a total nominal value of CHF 200 000 thousand, issued on 28 March 2017, with a fixed interest rate, maturing on 28 March 2023 and listed on the regulated market operated by the Swiss Stock Exchange (the equivalent of PLN 837 680 thousand according to the average NBP exchange rate of 1 October 2020).

Redemptions in 2020

- On 29 May 2020, the Bank addressed to holders of outstanding bonds issued by mFF:

a. with a total nominal value of EUR 500 000 thousand, with maturity date on 26 September 2020,
b. with a total nominal value of EUR 500 000 thousand, with maturity date on 26 November 2021, and
c. issued by the Bank with a total nominal value of EUR 500 000 thousand with a maturity date on 5 September 2022, invitations to submit these bonds for redemption by the Bank.

As a result of the announced redemption offer, Bank accepted for purchase all correctly issued bonds with nominal value, respectively: (a) EUR 35 178 thousand, (b) EUR 72 417 thousand, (c) EUR 39 970 thousand. The redemption offer was settled on 10 June 2020.

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Subordinated liabilities

31.12.2021	Nominal value	Currency	Terms of interest rate (%)	Effective interest rate (%)	Redemption date	As at the end of the period
Commerzbank AG	250 000	CHF	3M LIBOR + 2.75%	1.97	21.03.2028	1 112 709
Investors not associated with mBank S.A	550 000	PLN	6M WIBOR + 1.8%	2.14	10.10.2028 [1)]	552 643
Investors not associated with mBank S.A	200 000	PLN	6M WIBOR + 1.95%	2.29	10.10.2030 [1)]	201 028
Investors not associated with mBank S.A	750 000	PLN	6M WIBOR + 2.1%	2.35	17.01.2025	758 076
						2 624 456

31.12.2020	Nominal value	Currency	Terms of interest rate (%)	Effective interest rate (%)	Redemption date	As at the end of the period
Commerzbank AG	250 000	CHF	3M LIBOR + 2.75%	2.02	21.03.2028	1 066 605
Investors not associated with mBank S.A	550 000	PLN	6M WIBOR + 1.8%	2.06	10.10.2028 [1)]	552 545
Investors not associated with mBank S.A	200 000	PLN	6M WIBOR + 1.95%	2.21	10.10.2030 [1)]	200 992
Investors not associated with mBank S.A	750 000	PLN	6M WIBOR + 2.1%	2.38	17.01.2025	758 185
						2 578 327

[1)] The issue conditions assume the possibility of early redemption of bonds with a nominal value of PLN 550 000 thousand on 10 October 2023, and bonds with a nominal value of PLN 200 000 thousand on 10 October 2025.

The effective interest rate specified in the tables above means the interest rate at the inception day of the last interest period.

Movements in subordinated liabilities

Movements from 1 January to 31 December	2021	2020
As at the beginning of the period	**2 578 327**	**2 500 217**
Exchange differences	46 075	85 700
Other changes	54	(7 590)
Subordinated liabilities as at the end of the period	**2 624 456**	**2 578 327**
Short-term (up to 1 year)	12 356	12 302
Long-term (over 1 year)	2 612 100	2 566 025

On 29 March 2018, the Polish Financial Supervision Authority gave consent for qualifying funds from subordinated loan in the amount of CHF 250 000 thousand, taken on 21 March 2018, as instrument in the Bank's Tier II capital. The amount of CHF 250 000 thousand according to the average exchange rate of the National Bank of Poland of 29 March 2018 is the equivalent of PLN 893 200 thousand.

On 9 October 2018, mBank S.A. issued two series of subordinated bonds with a total nominal value of PLN 750 000 thousand. 1 100 pieces of 10-year subordinated bonds with a nominal value of PLN 500 thousand each were issued, with maturity on 10 October 2028, and 400 pieces of 12-year subordinated bonds with a nominal value of PLN 500 thousand each, with maturity on 10 October 2030.

The Bank applied to the Polish Financial Supervision Authority for permission to include in the supplementary capital of the Bank, in accordance with art. 127 para. 3 point 2 letter b) of the Banking Law Act, a monetary liability in the amount of PLN 750 000 thousand obtained by the Bank for the above-mentioned subordinated bond issue. The Bank obtained such consent on 28 November 2018.

According to the decision dated 8 January 2015 mBank obtained permission of the PFSA to include in Tier II capital the amount of PLN 750 000 thousand constituting subordinated liability from the bonds issue dated 17 December 2014 on total nominal value of PLN 750 000 thousand with redemption date on 17 January 2025 on terms that meet the requirements arising from the CRR Regulation.

In 2021 and 2020, the Bank did not note any delays in repayments of interest instalments and was not in default of any other contractual provisions related to its subordinated liabilities.

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30. Other liabilities

	31.12.2021	31.12.2020
Other liabilities, including		
Tax liabilities	286 202	209 674
Interbank settlements	1 042 600	935 581
Creditors, including:	748 452	1 019 740
- settlements due to payment cards	*47 543*	*219 201*
- liabilities payable to Bank Guarantee Fund	*251 044*	*249 181*
Accrued expenses	259 277	182 689
Deferred income	273 081	248 896
Provisions for post-employment employee benefits	24 131	31 797
Provisions for holiday equivalents	22 003	17 367
Provisions for other liabilities to employees	139 668	95 489
Other	6 198	5 943
Total other liabilities	**2 801 612**	**2 747 176**

As at 31 December 2021, the note presented above includes financial liabilities in the amount of PLN 2 050 329 thousand (31 December 2020: PLN 2 138 010 thousand), the maturity of which has been presented under Note 3.8.1. The other components of presented liabilities, except for part of provisions for post-employment benefits that were calculated on actuarial basis as a rule, are short-term liabilities.

Movements in provisions for post-employment employee benefits

Period from 1 January to 31 December 2021	Pension and disability provisions	Provisions for death severance	Provisions for the Social Benefit Fund	Total
Provisions for post-employment employee benefits				
As at the beginning of the period	**14 080**	**5 563**	**12 154**	**31 797**
Change in the period (due to)	(1 023)	(2 686)	(3 957)	(7 666)
Provisions created	835	152	626	1 613
Interest expense	177	75	164	416
Actuarial gains and losses recognised in other comprehensive income (Note 17), due to:	(1 283)	(2 913)	(4 086)	(8 282)
- change in financing assumptions	*(2 750)*	*(571)*	*(5 359)*	(8 680)
- change in demographic assumptions	*387*	*(2 369)*	*516*	(1 466)
- other changes	*1 080*	*27*	*757*	1 864
Benefits paid	(752)	-	(661)	(1 413)
As at the end of the period (by type)	**13 057**	**2 877**	**8 197**	**24 131**
Short-term (up to 1 year)	1 740	202	111	**2 053**
Long-term (over 1 year)	11 317	2 675	8 086	**22 078**

Period from 1 January to 31 December 2020	Pension and disability provisions	Provisions for death severance	Provisions for the Social Benefit Fund	Total
Provisions for post-employment employee benefits				
As at the beginning of the period	**11 463**	**4 671**	**7 567**	**23 701**
Change in the period (due to)	**2 617**	**892**	**4 587**	**8 096**
Provisions created	626	113	335	**1 074**
Interest expense	215	93	151	**459**
Actuarial gains and losses recognised in other comprehensive income (Note 17), due to:	2 237	847	4 614	**7 698**
- change in financing assumptions	*662*	*266*	*1 803*	***2 731***
- change in demographic assumptions	*181*	*(31)*	*166*	***316***
- other changes	*1 394*	*612*	*2 645*	***4 651***
Benefits paid	(461)	(161)	(513)	**(1 135)**
As at the end of the period (by type)	**14 080**	**5 563**	**12 154**	**31 797**
Short-term (up to 1 year)	1 948	313	102	**2 363**
Long-term (over 1 year)	12 132	5 250	12 052	**29 434**

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The discount rate is one of the key assumptions used in the actuarial valuation of provisions for post-employment benefits. If the discount rate used in the calculation of these provisions as at 31 December 2021 was decreased by 0.5 p.p., the value of the provisions would increase by PLN 1 682 thousand, and in the case of an increase of the discount rate by 0.5 p.p. the value of the provisions would fall by PLN 1 498 thousand (31 December 2020, respectively: PLN 1 031 thousand and PLN 950 thousand).

31. Provisions

	31.12.2021	31.12.2020
Provisions for legal proceedings, including:	395 446	200 426
- provisions for individual cases concerning indexation clauses in mortgage and housing loans in CHF	*261 851*	*161 886*
- provisions for other legal proceedings relating to loans in foreign currencies	*96 956*	*26 581*
- provisions for remaining legal proceedings	*36 639*	*11 959*
Off-balance commitments and guarantees given	351 834	222 191
Other provisions	92 418	92 594
Provisions, total	**839 698**	**515 211**

Estimated dates of granted contingent liabilities realisation are presented in Note 35.

Estimated cash flows due to created provisions for legal proceedings and other provisions are expected to occur over 1 year period.

The description regarding individual cases concerning indexation clauses in mortgage and housing loans in CHF is presented in Note 34.

The item "Other provisions" includes provisions recognised in connection with the judgment of the CJEU dated 11 September 2019 regarding commission reimbursement in the case of early repayment of consumer loans and mortgage loans. Detailed information on the impact of this judgment is described in Note 4.

Movements in provisions

Change from 1 January to 31 December	2021			
	Provisions for individual cases concerning indexation clauses in mortgage and housing loans in CHF	Provisions for other legal proceedings relating to loans in foreign currencies	Other provisions for remaining legal proceedings	Other provisions
Provisions as at the beginning of the period	**161 886**	**26 581**	**11 959**	**92 594**
Change in the period, due to:	**99 965**	**70 375**	**24 680**	**(176)**
- increase of provisions	196 012	73 370	53 412	43 841
- release of provisions	-	(334)	(2 148)	(3 489)
- utilization	(87 560)	(2 661)	(26 608)	(39 931)
- reclassification to other positions	(8 487)	-	-	-
- foreign exchange differences	-	-	24	(597)
Provisions as at the end of the period	**261 851**	**96 956**	**36 639**	**92 418**

Change from 1 January to 31 December	2020			
	Provisions for individual cases concerning indexation clauses in mortgage and housing loans in CHF	Provisions for other legal proceedings relating to loans in foreign currencies	Other provisions for remaining legal proceedings	Other provisions
Provisions as at the beginning of the period	**50 098**	**61 103**	**5 916**	**100 631**
Change in the period, due to:	**111 788**	**(34 522)**	**6 043**	**(8 037)**
- increase of provisions	136 515	8 782	7 742	36 905
- release of provisions	-	(20 705)	(453)	(8 000)
- utilization	(24 727)	(22 599)	(1 246)	(34 568)
- reclassification to other positions	-	-	-	(3 040)
- foreign exchange differences	-	-	-	666
Provisions as at the end of the period	**161 886**	**26 581**	**11 959**	**92 594**

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Movements in provisions for loan commitments, guarantees and other financial facilities

Change in the period from 1 January to 31 December 2021	As at the beginning of the period	Transfer to Stage 1	Transfer to Stage 2	Transfer to Stage 3	Increases due to granting and takeover	Reductions caused by derecognition	Changes in credit risk	Changes due to new default definition	As at the end of the period
Loan commitments	**89 432**	**-**	**-**	**-**	**42 524**	**(33 267)**	**(13 578)**	**5 525**	**90 636**
Stage 1	44 598	50 411	(7 237)	(107)	31 399	(16 586)	(48 909)	(3 230)	50 339
Stage 2	36 829	(48 420)	7 708	(2 628)	7 216	(11 027)	21 543	3 355	14 576
Stage 3	5 510	(1 991)	(471)	2 735	3 184	(6 416)	16 600	5 404	24 555
POCI	2 495	-	-	-	725	762	(2 812)	(4)	1 166
Guarantees and other financial facilities	**132 759**	**-**	**-**	**-**	**104 949**	**(133 290)**	**156 756**	**24**	**261 198**
Stage 1	20 630	1 444	(271)	-	35 466	(39 903)	18 291	35	35 692
Stage 2	6 134	(1 444)	271	(1 145)	1 016	(4 124)	456	(11)	1 153
Stage 3	80 055	-	-	1 145	68 333	(58 419)	134 746	-	225 860
POCI	25 940	-	-	-	134	(30 844)	3 263	-	(1 507)
Total provisions on off-balance sheet items	**222 191**	**-**	**-**	**-**	**147 473**	**(166 557)**	**143 178**	**5 549**	**351 834**

Change in the period from 1 January to 31 December 2020	As at the beginning of the period	Transfer to Stage 1	Transfer to Stage 2	Transfer to Stage 3	Increases due to granting and takeover	Reductions caused by derecognition	Changes in credit risk	As at the end of the period
Loan commitments	**62 296**	**-**	**-**	**-**	**48 176**	**(55 430)**	**34 390**	**89 432**
Stage 1	34 290	38 907	(5 912)	(5)	23 299	(17 059)	(28 922)	44 598
Stage 2	23 489	(38 907)	5 953	(317)	12 956	(13 877)	47 532	36 829
Stage 3	2 136	-	(41)	322	10 835	(23 358)	15 616	5 510
POCI	2 381	-	-	-	1 086	(1 136)	164	2 495
Guarantees and other financial facilities	**89 568**	**-**	**-**	**-**	**100 323**	**(77 788)**	**20 656**	**132 759**
Stage 1	4 781	1 425	(764)	-	33 308	(17 124)	(996)	20 630
Stage 2	4 713	(1 425)	764	(278)	2 526	(3 719)	3 553	6 134
Stage 3	79 684	-	-	278	38 317	(56 229)	18 005	80 055
POCI	390	-	-	-	26 172	(716)	94	25 940
Provisions on off-balance sheet items	**151 864**	**-**	**-**	**-**	**148 499**	**(133 218)**	**55 046**	**222 191**

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32. Deferred income tax assets and liabilities

Assets and liabilities for deferred income tax are calculated for all temporary differences in accordance with the balance sheet method, using an effective income tax rate of 19% in 2021 and 2020.

Assets and liabilities for deferred income tax are not recognised as short term assets and liabilities.

Changes in assets and liabilities for deferred income tax are presented below:

Deferred income tax assets	As at 01.01.2021	Recognised in the income statement	Recognised in other comprehensive income	Other changes	As at 31.12.2021
Interest accrued	11 846	(1 251)	-	-	10 595
Valuation of derivative financial instruments	-	(18 852)	116 338	-	97 486
Valuation of securities	110 750	20 652	162 938	-	294 340
Provisions for impairment of loans and advances	503 705	(27 600)	-	-	476 105
Provisions for employee benefits	23 519	10 968	(1 573)	-	32 914
Other provisions	11 408	26 510	-	-	37 918
Prepayments/accruals	31 550	1 839	-	-	33 389
Difference between tax and book value of tangible and intangible assets	154 667	48 619	-	-	203 286
Other negative temporary differences	44 274	(7 597)	-	141	36 818
Total deferred income tax assets	**891 719**	**53 288**	**277 703**	**141**	**1 222 851**

Deferred income tax liabilities	As at 01.01.2021	Recognised in the income statement	Recognised in other comprehensive income	Other changes	As at 31.12.2021
Interest accrued	(46 778)	(4 960)	-	-	(51 738)
Valuation of derivative financial instruments	(174 835)	79 676	95 159	-	-
Valuation of securities	(196 987)	30 712	38 347	-	(127 928)
Interest and fees received in advance	(26 017)	(22 237)	-	-	(48 254)
Difference between tax and book value of tangible and intangible assets	(186 328)	(47 098)	-	-	(233 426)
Prepayments regarding amortization of applied investment relief	(18 657)	9 494	-	-	(9 163)
Other positive temporary differences	(35 282)	6 857	(2 682)	-	(31 107)
Total deferred income tax liabilities	**(684 884)**	**52 444**	**130 824**	**-**	**(501 616)**

Deferred income tax assets	As at 01.01.2020	Recognised in the income statement	Recognised in other comprehensive income	Other changes	As at 31.12.2020
Interest accrued	31 232	(19 386)	-	-	11 846
Valuation of securities	50 214	61 708	(1 172)	-	110 750
Provisions for impairment of loans and advances	415 642	88 063	-	-	503 705
Provisions for employee benefits	39 245	(17 189)	1 463	-	23 519
Other provisions	21 822	(10 414)	-	-	11 408
Prepayments/accruals	32 150	(600)	-	-	31 550
Difference between tax and book value of tangible and intangible assets	91 601	63 066	-	-	154 667
Other negative temporary differences	41 902	2 271	-	101	44 274
Total deferred income tax assets	**723 808**	**167 519**	**291**	**101**	**891 719**

Deferred income tax liabilities	As at 01.01.2020	Recognised in the income statement	Recognised in other comprehensive income	Other changes	As at 31.12.2020
Interest accrued	(56 332)	9 554	-	-	(46 778)
Valuation of derivative financial instruments	(65 091)	(43 237)	(66 507)	-	(174 835)
Valuation of securities	(134 925)	(28 334)	(33 728)	-	(196 987)
Interest and fees received in advance	(16 413)	(9 604)	-	-	(26 017)
Difference between tax and book value of tangible and intangible assets	(121 293)	(65 035)	-	-	(186 328)
Prepayments regarding amortization of applied investment relief	(18 657)	-	-	-	(18 657)
Other positive temporary differences	(37 922)	2 640	-	-	(35 282)
Total deferred income tax liabilities	**(450 633)**	**(134 016)**	**(100 235)**	**-**	**(684 884)**

The item "Difference between tax and book value of tangible and intangible assets" includes the impact of IFRS16 on the deferred tax.

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	As of 31 December	
	2021	2020
Interest accrued	(6 211)	(9 832)
Valuation of derivative financial instruments	60 824	(43 237)
Valuation of securities	51 364	33 374
Provisions for impairment of loans and advances	(27 600)	88 063
Provisions for employee benefits	10 968	(17 189)
Other provisions	26 510	(10 414)
Prepayments/accruals	1 839	(600)
Interest and fees received in advance	(22 237)	(9 604)
Prepayments regarding amortisation of applied investment relief	9 494	-
Difference between tax and book value of tangible and intangible assets	1 521	(1 969)
Other temporary differences	(740)	4 911
Total deferred income tax included in the income statement (Note 15)	**105 732**	**33 503**

The item "Other positive temporary differences" includes the impact of the creation of deferred tax provision in the amount of PLN 11 265 thousand resulting from the implementation of IFRS 9 in respect of recognised in previous years tax-deductible costs from the provision for incurred undocumented credit risk (in 2020: PLN 15 019 thousand). According to art. 12 para. 4 of the Act of 27 October 2017 on amendments to the Personal Income Tax Act, the Corporate Income Tax Act and the Act on Flat Rate Income Tax on Certain Revenue Earned by Natural Persons, in the event that the bank included IBNR to the tax-deductible costs before 1 January 2018, after the entry into force of the amendment the bank is obliged to recognise income up to the amount previously recognised as tax cost. The Bank recognises revenues on this account pro rata for a period of 7 consecutive tax years.

Bank evaluated the recoverability of deferred tax assets. Following the rules of IAS 12 paragraph 28 and 29 the Bank recognised deferred tax assets to the extent that it is probable that the Bank will have sufficient taxable profits in the future periods or tax planning opportunities are available that will create taxable profit in future periods.

A level of deferred tax asset for the year 2021 and 2020 does not include tax losses of the foreign branch in Slovakia in the amount of: EUR 933 thousand (equivalent of PLN 4 290 thousand at the average exchange rate of the National Bank of Poland as of 31 December 2021) and EUR 1 997 thousand (equivalent of PLN 9 216 thousand at the average exchange rate of the National Bank of Poland as of 31 December 2020). Potential inclusion of the tax losses into deferred tax asset in years to come will depend upon an assessment of the corporate income tax base level in a future (including the periods scheduled for settlement of tax losses). Right to tax losses' settlement expires between 2022 and 2023 year.

Bank recognises deferred tax liabilities or assets related to temporary differences arising from investments in subsidiaries and affiliated except that the implementation of the temporary differences is controlled by Bank and it is probable that in the foreseeable future, these differences will not be reversed. At the end of 2021 Bank did not include settlements on temporary differences in the total amount of PLN 1 607 289 thousand incurred due to investments in subsidiaries and affiliated companies in deferred tax calculation (at the end of 2020: PLN 1 490 835 thousand).

33. Proceedings before court, arbitration body or public administration authority

The Bank monitors the status of all court cases brought against entities of the Bank, including the status of court rulings regarding loans in foreign currencies in terms of shaping of and possible changes in the line of verdicts of the courts, as well as the level of required provisions for legal proceedings.

The Bank creates provisions for litigations, which as a result of the risk assessment involve a probable outflow of funds from fulfilling the liability and when a reliable estimate of the amount of the liability can be made. The amount of provisions is determined taking into account the amounts of outflow of funds calculated on the basis of scenarios of potential settlements of disputable issues and their probability estimated by the Bank based on the previous decisions of courts in similar cases and the experience of the Bank.

The value of provisions for litigations as at 31 December 2021 amounted to PLN 395 446 thousand (PLN 200 426 thousand as at 31 December 2020). A potential outflow of funds due to the fulfilment of the obligation takes place at the moment of the final resolution of the cases by the courts, which is beyond the control of the Bank.

Information on the most important court proceedings relating to the issuer's contingent liabilities

1. Claims of Interbrok's clients

   Since 2008, Nine compensation lawsuits were filed against the Bank in relation to activities of Interbrok Investment E. Dróżdż i Spółka Sp. jawna (hereinafter "Interbrok"). Eight of the nine lawsuits were filed by former clients of Interbrok for the total amount of PLN 800 thousand with the provision that the claims may be extended up to the total amount of PLN 5 950 thousand. The plaintiffs alleged that the Bank had aided in Interbrok's illegal activities, which caused damage to them. With regard to seven of the afore-mentioned cases, legal proceedings against the Bank were dismissed and the cases were finally concluded. In the eighth case, a plaintiff withdrew their suit waiving the claim and the Regional Court dismissed the action. As far as the ninth suit is concerned, the amount in dispute is PLN 276 499 thousand, including statutory interest and costs of proceedings. According to the claims brought in the suit, this amount comprises the receivables, acquired by the plaintiff by way of assignment, due to the parties aggrieved by Interbrok on account of a reduction (as a result of Interbrok's bankruptcy) of the receivables by a return of the deposits paid by the aggrieved for making investments on the forex market. The plaintiff claims i.a. the Bank's liability on the grounds of the Bank's aid in committing the illicit act of Interbrok, consisting in unlicensed brokerage operations. On 7 November 2017, the Regional Court in Warsaw dismissed the action in its entirety. The plaintiff appealed. On 25 January 2021, the Court of Appeal in Warsaw dismissed the Plantiff's appellation in its entirety. The ruling of the Regional Court in Warsaw, as well as the ruling of the Court of Appeal are binding. Plaintiff filed a cassation complaint with the Supreme Court.

2. A lawsuit filed by LPP S.A.

   On 17 May 2018, mBank S.A. received a lawsuit filed by LPP S.A. with its registered office in Gdańsk seeking damages amounting to PLN 96 307 thousand on account of interchange fee. In the lawsuit, LPP S.A. petitioned the court for awarding the damages jointly from mBank S.A. and from other domestic bank.

   The plaintiff accuses the two sued banks as well as other banks operating in Poland of taking part in a collusion breaching the Competition and Consumer Protection Act and the Treaty on the Functioning of the European Union. In the plaintiff's opinion, the collusion took the form of an agreement in restriction of competition in the market of acquiring services connected with settling clients' liabilities towards the plaintiff on account of payments for goods purchased by them with payment cards in the territory of Poland.

   On 16 August 2018 mBank S.A. has submitted its statement of defence and requested that the action be dismissed. The court accepted the Defendants' requests to summon sixteen banks to join the proceedings and ordered that the banks be served with the summons. Two banks have notified of their intention to intervene in the case as an indirect intervener.

3. A lawsuit filed by Polski Koncern Naftowy ORLEN S.A.

   On 7 February 2020, mBank S.A. received a lawsuit filed by Polski Koncern Naftowy ORLEN S.A. (Orlen) with its registered office in Płock seeking damages amounting to PLN 635 681 thousand on account of interchange fee. In the lawsuit, Orlen petitioned the court for awarding the damages jointly from mBank S.A. and other domestic bank and also from Master Card Europe and VISA Europe Management Services.

   The plaintiff accuses the two sued banks as well as other banks operating in Poland of taking part in a collusion breaching the Competition and Consumer Protection Act and the Treaty on the Functioning of the European Union, i.e. a collusion restricting competition in the market of acquiring services connected with settling clients' liabilities towards the plaintiff on account of card payments for goods and services purchased by clients on the territory of Poland. On 28 May 2020, mBank S.A. filed a response to the lawsuit. On 28 May 2020 mBank S.A. has submitted its statement of defence and requested that the action be dismissed. The court accepted the Defendants' requests to summon sixteen banks to join the proceedings and ordered that the banks be served with the summons. Two banks have notified of their intention to intervene in the case as an indirect intervener.

4. Class action against mBank S.A. concerning the clause on changing interest rate

   Detailed information on the class action against the Bank is provided in Note 34.

5. Individual court proceedings concerning indexation clauses in CHF

   Detailed information on individual court cases against the Bank regarding CHF indexed loans is provided in Note 34.

Tax inspections

On 11 May 2021, the Head of the Customs and Tax Office in Opole (Urząd Celno-Skarbowy w Opolu) has initiated tax audits regarding the correctness and reliability of withholding tax (WHT) settlements on payments listed in Art. 21 sec. 1 of the Act of 15 February 1992 on corporate income tax for years 2018 and 2019. The tax audit is under way.

The tax authorities may inspect at any time the books and records within 5 years subsequent to the reported tax year and may impose additional tax assessments and penalties. In the opinion of the Management Board there are no circumstances, which would indicate that crystallising of material tax liabilities in this respect is probable.

Inspection by the Office of the Polish Financial Supervision Authority (PFSA Office)

In the period from October till December 2018 the PFSA Office employees carried out an inspection in the Bank in order to investigate whether the activities of mBank S.A. in the area of fulfilling its duties as the depositary were in conformity with the law and agreements on the performance of functions of the depositary, in particular in conformity with the Act of 27 May 2004 on Investment Funds and Management of Alternative Investment Funds (Journal of Laws of 2018, item 1355, as later amended).

The detailed findings of the inspection were presented in the protocol delivered to the Bank on 11 February 2019. On 25 February 2019 the Bank delivered to the PFSA office its objections to the protocol as well as additional explanations related to the issues being the subject of the inspection.

On 1 April 2019 the Bank received PFSA response to the objections to the inspection protocol as well as PFSA recommendations in regard to the adjustment of Bank’s activity as a depositary bank for investment funds to the applicable law. All objections of the Bank have been rejected by the regulator.

On 25 April 2019, Bank submitted to PFSA Office a declaration of actions taken as realization of post inspection recommendations. PFSA by letter dated 4 September 2019 objected to the implementation of selected recommendations. On 11 October 2019 Bank submitted to PFSA the response addressing given objections, in which the description of taken actions was further specified as well as some new solutions for implementation were presented. On 5 December 2019, the PFSA Office sent to the Bank a reply to the letter containing the acceptance of some of the Bank's activities aimed at implementing post-audit recommendations and clarifications of other expectations that are being implemented. On 14 May 2020, Bank formally confirmed the realisation of all PFSA recommendations.

On 27 February 2020, the Bank received the decision of PFSA Office dated 25 February 2020 to initiate administrative proceedings regarding the imposition of an administrative penalty on the Bank, pursuant to the provisions of the Act dated 27 May 2004 on investment funds and management of alternative investment funds.

On 23 April 2021 the Bank received a decision of the PFSA dated 16 April 2021 regarding this proceeding, imposing a fine on the Bank in the total amount of PLN 4 300 thousand. The Bank created provision for the abovementioned fine in the amount of PLN 4 300 thousand.

On 7 May 2021, the Bank applied to the Financial Supervision Authority for reconsideration of the case. On 17 December 2021, UKNF upheld its decision of 16 April 2021. On 21 January 2022, the Bank filed a complaint with the Voivodship Administrative Court against the decision of PFSA. As at the date of approval of these financial statements, the case is pending before the administrative court.

Proceedings initiated by the Office of Competition and Consumer Protection (UOKiK)

- Proceedings for considering provisions of a template agreement as abusive instituted ex officio on 12 April 2019. The proceedings concern amendment clauses stipulating under which circumstances the bank is authorised to amend the terms and conditions of the agreement, including the amount of fees and commissions. In the opinion of the President of the Office of Competition and Consumer Protection (UOKiK), the amendment clauses used by the bank give it an unlimited right to unilaterally and freely change the manner of performing the agreement. As a consequence, the UOKiK President represents the view that the clauses used by the bank define the rights and obligations of consumers contrary to good morals and grossly violate their interest and, thus, are abusive. mBank does not agree with this stance. mBank responded to the decision on instituting the proceedings in letters dated 28 May 2019 and 10 January 2020. As at the date of approval these financial statements, the UOKiK President did not take any further actions in the case in question, did not take a stance, and did not respond to mBank’s letters. The proceedings were extended until 31 March 2022.
- By a judgment of 2 February 2021, the Court of Appeal in Warsaw dismissed the Bank's appeal in a case concerning UOKiK proceedings initiated in 2015 regarding the application by mBank S.A. practices violating collective consumer interests, due to the fact that mBank did not apply a negative interest rate due to the negative base rate of LIBOR, and changed the judgment of SOKiK in the part.

- revoking the decision to impose a fine. The Bank complied with the judgment and paid a fine of PLN 6 585 thousand. On 14 June 2021, the Bank filed a cassation complaint with the Supreme Court.
- On 21 July 2017 the UOKiK instigated proceedings against mBank with regard to violation of consumers' collective interests. The UOKiK charged the bank with failing to adequately inform clients about FX risk and about shifting FX risk onto consumers, and with incorrectly determining (inflating) credit instalments. In the letter dated 18 August 2017 the bank responded to the charges. In the letter dated 18 February 2019 the UOKiK President requested detailed information on the handling of mortgages indexed to foreign currencies, to which the bank replied. In the letter dated 14 October 2021 the UOKiK President informed the bank that the evidentiary proceedings had ended and appointed a time limit for the bank to peruse the case file and to comment on the evidence collected in the case. The Bank commented on the evidence collected within the prescribed deadline. The President of UOKiK extended the termination of the proceedings until 30 April 2022.

34. Legal risk related to mortgage and housing loans granted to individual customers in CHF

Introduction

In recent years, a significant number of individual customers who took out mortgage and housing loans in CHF, challenged in court some of the provisions or all agreements on the basis of which the Bank granted these loans. So far, there is no uniform line of judgments issued by courts in such cases.

The carrying amount of mortgage and housing loans granted to individual customers in CHF as of 31 December 2021 amounted to PLN 9.1 billion (i.e. CHF 2.0 billion) compared to PLN 12.3 billion (i.e. CHF 2.9 billion) as at the end of 2020. Additionally the volume of the portfolio of loans granted in CHF that were already fully repaid as of 31 December 2021 amounted to PLN 7.3 billion (31 December 2020: PLN 6.8 billion).

Due to the significance of the legal issues related to the CHF loan portfolio for the financial position of mBank as at 31 December 2021, detailed information is presented below regarding these lawsuits, significant judgments, which, in the Bank's opinion, may affect the future ruling on loans indexed to CHF, proposed potential settlements with customers, accounting principles for the recognition of legal risk related to these court cases and the voluntary settlement program, as well as information on the impact of legal risk related to these court cases on the balance sheet and income statement of mBank and the methodology used to determine this impact.

Individual court cases against the Bank concerning loans indexed to CHF

As of 31 December 2021, 13 373 individual court proceedings (31 December 2020: 7 508 proceedings) were initiated against the Bank by its customers in connection with CHF loan agreements with the total value of claims amounting to PLN 3 506.5 million (31 December 2020: PLN 1 454.2 million).

Out of the individual proceedings 13 036 proceedings (31 December 2020: 6 870 proceedings) with the total value of claims amounting to PLN 3 499.9 million (31 December 2020: PLN 1 442.2 million) related to indexation clauses in CHF loan agreements and include claims for declaring ineffectiveness or invalidity in part (i.e. to the extent that the agreement contains contractual provisions related to indexation) or invalidity in whole of the loan agreements.

As of 31 December 2021 mBank received 473 final rulings in individual lawsuits (31 December 2020: 173 final rulings), out of which 82 rulings were favourable to the Bank and 391 rulings were unfavourable (31 December 2020: 70 rulings favourable and 103 unfavourable).

At the same time 227 proceedings (as of 31 December 2021) at the second instance courts have remained suspended due to the legal issues referred to the Supreme Court and the Court of Justice of the European Union (CJEU). The Bank submits cassation appeals to the Supreme Court against legally binding judgments unfavourable for the Bank. Unfavourable judgments were based on the same patterns of facts which in the past had resulted in different verdicts. Approximately 70% of unfavourable verdicts led to the invalidation of the loan agreement, others led to the conversion of the agreement into PLN + LIBOR / WIBOR.

In the fourth quarter of 2021, in some cases where final judgments were issued stating the invalidity of the loan agreement, as well as in some pending cases where the client filed for invalidity of loan agreement, the Bank filed 2471 counterclaims against borrowers. The counterclaims includes a claim of the Bank against the consumer for payment of the principal and the remuneration of using it, and as the measure of the value of the bank's benefit, the interest rate on PLN housing loans secured with a mortgage published by the National Bank of Poland was used. Counterclaims concern cases in which borrowers filed lawsuits with the court till the end of 2018.

Class action against mBank S.A. concerning adjustment clauses

The Bank was also sued by the Municipal Consumer Ombudsman representing a group of 390 individuals - retail banking customers who entered into mortgage loan agreements indexed to CHF. This class action concerning indexation clauses was filed in the District Court in Łódź on 4 April 2016.

The lawsuit contains alternative claims for declaring the loan agreements partially invalid, i.e. with respect to the indexation provisions or for declaring the agreements invalid in their entirety or for declaring the indexation provisions of the agreements invalid due to the fact that they allow the loan to be valorised above 20% and below 20% of the CHF exchange rate from mBank S.A. table of exchange rates in effect on the date each of the loan agreements was concluded.

By Order dated 13 March 2018 the Court set the Class at 1 731 persons. On 19 October 2018 the Court issued judgment dismissing all of Plaintiff's claims. In its oral reasoning, the Court argued that the Claimant failed to prove that it has a legal interest in bringing the claim in question and also addressed the issue of the validity of the CHF valorised loan agreements, emphasizing that both the agreements themselves and the valorisation clause are in compliance with both applicable laws and the principles of social interaction. On 11 January 2019 the Plaintiff's appeal was delivered to the Bank, to which the Bank filed a response. On 27 February 2020 a hearing was held in the Court of Appeal in Łódź. On 9 March 2020 a judgment was rendered in the case, in which the Court of Appeal returned the case to the District Court for reconsideration. On 9 June 2020 the Court of Appeal, on the motion of the Plaintiff, issued a decision by which it granted security to the Plaintiff's claims by suspending the obligation to pay principal and interest instalments and prohibiting the Bank from making statements calling for payment and terminating the loan agreement.

On 12 January 2022 a hearing was held in the District Court in Łódź. The publication of the decision will take place on 9 February 2022. As of 31 December 2021 the value of claims in this class action was equal to PLN 377 million. On 12 January 2022, a hearing was held before the Regional Court in Łódź, and on 9 February 2022 the court issued a verdict dismissing the claim in its entirety. The plaintiff may appeal against this verdict. As of the date of approval of these financial statements the Bank did not change its risk assessment related to this proceeding as described below in the section concerning methodology of calculation the impact of the legal risk related to the class action case. As of 31 December 2021 the value of claims in this class action was equal to PLN 377 million.

Information on the most important court proceedings regarding loans indexed to CHF

Rulings of the Court of Justice of the European Union regarding a CHF mortgages

On 3 October 2019 the CJEU issued the ruling in the prejudicial mode regarding a mortgage linked to the Swiss franc granted by a Polish bank. The submitted prejudicial questions were to determine, among other things, if a generally applicable custom can be used where there is no provision in domestic law that could replace an abusive exchange rate clause. In accordance with CJEU's ruling, the question of abusiveness will be decided by Polish courts. CJEU did not refer to this issue. In addition, CJEU did not make a clear-cut decision regarding the consequences of an exchange rate clause being considered abusive by a domestic court. However, the possibility of a credit agreement being performed further in PLN and with interest calculated according to LIBOR was found doubtful by the Court. If an exchange rate clause is found abusive, a domestic court must decide whether the agreement in question can be performed further or should be declared invalid, taking into account the client's will and the consequences of invalidity for the client. CJEU approved the application of a disposable norm (in the bank's opinion article 358 of the Polish Civil Code referring to the NBP fixing rate can be considered to be a disposable norm), if the invalidity of the agreement would be unfavourable for the client. CJEU rejected the application of general provisions referring to a custom or equity principles.

In October 2020, prejudicial questions were referred to CJEU in two individual cases against mBank. The question referred in first case aims at determining the starting point for the limitation period in the case of consumer claims for undue performance. The question referred in the second case aims at determining whether, in the event of declaring the exchange rate clause abusive, it is possible to apply in its place the provision of the Civil Code referring to the average NBP exchange rate. The Bank expects decisions on both these matters in 2022.

On 29 April 2021, the CJEU issued a judgment in case C-19/20. According to this judgment, if the unfair (abusive) nature of the contractual provision leads to annulment of the contract, the Court should not annul the contract until the Court informs the consumer in an objective and comprehensive manner about the legal consequences the annulment of such a contract may cause (whether or not the consumer is represented by a legal advisor) and until the Court allows the consumer to express a free and informed consent to the questioned provision and the continuation of the contract.

By the decision of 12 August 2021, another question was addressed to the CJEU, the subject of which is to determine whether in the event of cancellation of the loan agreement, the parties, in addition to the reimbursement of money paid in the performance of this agreement and statutory interest for delay from the moment of the call for payment, may also claim any other benefits in particular remuneration, unjust enrichment, compensation, reimbursement or valorisation of the benefit. The case has not yet been dealt with in the CJEU.

On 18 November 2021, the Court of Justice of the EU delivered its judgment in Case C-212/20, in which it assessed that in accordance with the provisions of Directive 93/13, the content of a so-called spreads clause must (on the basis of clear and comprehensible criteria) enable a reasonably well-informed, reasonably observant and rational consumer to understand how the exchange rate is to be determined, in such a way that the consumer is able to determine the rate applied by the trader himself at any time. Moreover CJEU made an assessment that the provisions of Directive 93/13 preclude the interpretation of an illicit contract term in order to mitigate its unfairness.

Supreme Court resolutions on loans in CHF

On 29 January 2021 the motion for adopting a resolution has been submitted to the Supreme Court by the First President of the Supreme Court. The full bench of the Civil Chamber of the Supreme Court was to answer to the questions if abusive provisions can be replaced with provisions of civil law or common practice, whether it is possible to maintain indexed/denominate loan as a PLN loan with an interest rate based on LIBOR, whether the theory of balance or the theory of two conditionalities will apply on the event of the CHF loan invalidity, the starting point of the limitation period in the case of the bank's claim for reimbursement of the amounts paid under the loan and whether banks and consumers can receive a remuneration for the use of their funds by the other party. The lack of a jurisprudence line, both domestic and of the CJEU, concerning remuneration for the use of capital is also significant for the shape of the provision. The position presented by banks has been strengthened by the opinions of the Polish Financial Supervision Authority (UKNF) and the Polish Bank Association (ZBP) submitted to case no. III CZP 11/21, which support granting banks the right to such remuneration. Thus, the banks' claims in this respect should be regarded as at least plausible.

There was one non-public sitting in this case, during which the Supreme Court decided to request the Ombudsman, Financial Ombudsman, Children's Ombudsman, NBP and the Polish Financial Supervision Authority to take a position. The positions of these bodies have been submitted.

At a closed session on 2 September 2021, the Supreme Court, pursuant to Article 267 of the Treaty on the Functioning of the European Union, decided to refer to the Court of Justice of the European Union with three questions for a preliminary ruling on the issue of appointing judges in the Republic of Poland. The verdict on the questions asked by the First President of the Supreme Court was not issued.

The resolution of the Supreme Court of 16 February 2021 in case III CZP 11/20 endorsed the theory of two conditionalities if a credit agreement is declared to be invalid. The Supreme Court in written justification found that the risk of insolvency of either of the unduly enriched parties is largely mitigated by the right of retention of received benefits until the other party offers to repay received benefits or secures the claims for repayment.

On 7 May 2021 (III CZP 6/21), a resolution of 7 of the Supreme Court's judges which have the force of a legal principle was issued, in which it was decided that:

- the prohibited contractual provision (Civil Code Art.3851 §1) is from the very beginning, by virtue of law ineffective for the benefit of the consumer, who may grant subsequently informed and free consent to this provision and thus restore its effectiveness retroactively,
- if the loan agreement cannot be binding after removal an ineffective provision, the consumer and the bank are entitled to separate claims for the reimbursement of cash benefits provided in the performance of this agreement (Article 410 § 1 in conjunction with Article 405 of the Civil Code). The bank may request the return of the benefit from the moment the loan agreement becomes permanently ineffective.

In the written justification, the Supreme Court confirmed its earlier positions as to the application of the theory of two conditionalities and the issue of calculating the limitation period for the bank's claims in the event that the contract cannot be upheld after the abusive provisions have been eliminated. The Supreme Court explained that due to the possibility granted to the consumer to make a binding decision regarding the sanctioning of the prohibited clause and to accept the consequences of the total invalidity of the contract, it should be recognised that, as a rule, the limitation period for these claims may start running only after the consumer has made a binding decision in this regard. Only then, in the opinion of the Supreme Court, can it be concluded that the lack of a legal basis for the benefit has become definitive (as in the case of condictio causa finita), and the parties could effectively demand the return of the undue benefit. This means, in particular, that the consumer cannot assume that the bank's claim has expired within the time limit calculated as if the call to return the loan was possible already on the day it was made available. In justifying the resolution, the Supreme Court also confirmed that in order to avoid risks related to the borrower's insolvency, the bank may use the right of retention provided in Art. 497 in connection with Art. 496 of the Civil Code, thus protecting its claim for the return of used principal, since the obligation to return it is - in relation to the obligation to put the funds at the disposal of the borrower - something more than a consideration obligation.

On 6 July 2021, the Civil Chamber of the Supreme Court refused to pass a resolution on Swiss franc indexed loans. The Supreme Court indicated that the question of whether the balance theory or the two conditionalities theory should be applied has already been resolved in the jurisprudence of the Supreme Court, including the resolution of 7 judges of 7 May 2021 (III CZP 6/21), and earlier in the resolution of 16 February 2021 (III CZP 11/20).

On 29 July 2021 the Supreme Court composed of 3 judges presented the legal issue to be resolved by a panel of 7 judges of the Supreme Court, which came down to the answer to the question whether, in the event of a loan agreement being declared invalid, a loan granted in Polish currency, indexed to a foreign currency, repaid by borrowers, the amount of possible enrichment of the lender should be calculated taking into account only the nominal amount of loan instalments, or the interest rate on instalments according to the reference rate appropriate for loans indexed to a foreign currency or appropriate for loans in PLN should be taken into account. The deadline for examining the issue was initially set for 8 November 2021, was removed from the case list, and the judge-rapporteur was also changed.

PFSA’s Chairman proposal

The general assumptions of the PFSA’s Chairman proposal to convert FX loans to PLN have been announced in December 2020. The PFSA’s Chairman proposal assumes that indexed to/denominated in foreign currency loan (CHF/EUR/USD) would be converted as it was from beginning a PLN loan with an interest rate of WIBOR 3M increased by a margin used historically for such loans.

The Bank analysed the costs it would have to incur in the indicated scenario, as the sum of the differences between the current balances of loans indexed to/denominated in a foreign currency (CHF/EUR/USD) and the corresponding hypothetical loan balances in PLN based on the 3M WIBOR rate increased by the loan margin in PLN granted at the same time and for the same period as the loan indexed to/denominated in foreign currencies (CHF/EUR/USD).

Hypothetical PLN loan balances include in their schedule differences from the actual repayments of loans indexed to / denominated in foreign currencies (CHF/EUR/USD) by adjusting the value of the outstanding principal according to the scheme provided by the PFSA.

The estimated potential impact of implementation of the conversion plan on mBank, calculated as of 31 December 2021, would amount to PLN 5.6 billion if only active portfolio was converted (data unaudited). Detailed assumptions for the estimation of this impact were adopted on the basis of the Polish Financial Supervision Authority's survey dated 27 January 2021. The PFSA’s Chairman proposal assumes that only active portfolio would be converted.

As at the date of approval this report mBank has not made any decisions on offering settlements according to the PFSA’s Chairman proposal nor has taken any steps to acquire any corporate consents in that matter.

Pilot of a settlements program

On 6 December 2021, the Bank began a pilot of a settlement program for borrowers who have an active CHF indexed loan. The pilot is expected to be completed by the end of the first quarter of 2022. The settlement offer presented in the program consists in conversion of the CHF indexed loan into a PLN loan with simultaneous write-off of a portion of the loan balance. Similar to the PFSA’s Chairman proposal this portion constitutes the difference between the current balance of the indexed loan expressed in PLN at the average exchange rate of the National Bank of Poland and the hypothetical balance that would exist if the loan had been originally contracted in PLN. In the Bank's pilot this difference is divided equally between the parties to the contract, and the Bank offers to cancel the loan balance in the amount equal to the part of this difference attributable to the Bank. This method of loan conversion guarantees equal distribution of materialized foreign exchange risk costs, which scale could not be foreseen by any of the parties to the loan agreement at the time of its conclusion. This will represent half of the benefits arising for the clients from the PFSA Chairman’s proposal.

The offer was addressed to 1 278 active contracts, which in Bank’s opinion is a representative sample of the whole portfolio of active loans indexed to CHF.

The purpose of the pilot is to verify the attractiveness of the offer and the process proposed by the Bank as well as to gather feedback in this respect from the clients included in the pilot.

The maximum, hypothetical cost of the program would amount to PLN 2.97 billion, assuming that the settlements would be offered to all clients with active loans and all those clients would accept the conditions described above.

Accounting policies for recognizing the effect of legal risk related to court cases concerning CHF mortgage and housing loans to individual customers and the voluntary settlement program

The Bank recognises the impact of the legal risk related to court cases concerning indexation clauses in mortgage and housing loans in CHF and voluntary settlements offered to CHF borrowers is reflected under:

- IFRS 9 "Financial Instruments" paragraph B5.4.6 in relation to active loans, including active loans covered by the class action case and voluntary settlements, and
- IAS 37 "Provisions, Contingent Liabilities and Contingent Assets" in relation to repaid loans.

Mortgage and housing loans to customers that are subject to court proceedings are within the scope of IFRS 9. Under IFRS 9, these loans are measured at amortised cost using the effective interest rate.

Legal claims filed by borrowers, including invalidity claims, impact the Bank's estimate of the expected life of the loan and the expected cash flows. In particular, the Bank takes into account the risk that the remaining life of the loan may be shorter than the contractual term, or the Bank may not receive some of the contractual cash flows, and in case of invalidity verdict, the Bank may have to reimburse the borrowers for undue benefits received. In addition, any voluntary settlements offered by the Bank to borrowers (including those who have not previously made legal claims), may also affect the amount and timing of expected cash flows from these loans.

Therefore the Bank believes that the appropriate way to recognise the impact of legal risk with respect to active loans and the expected impact of the voluntary settlement program offered to borrowers is to revise the cash flow estimates associated with the loans and reduce the gross carrying amount of the loans in accordance with IFRS 9 paragraph B5.4.6.

In relation to repaid loans and loans for which the estimated adjustment in cash flows is higher than the carrying amount, the Bank recognises provisions for legal proceedings in accordance with IAS 37 "Provisions, Contingent Liabilities and Contingent Assets".

According to IAS 37 the amount recognised as a provision is the best estimate of the expenditure required to settle the present obligation at the end of reporting period. The best estimate of the expenditure required to settle the present obligation is the amount that the Bank would rationally pay to settle the obligation at the end of the reporting period or to transfer it to a third party at that time. This amount is discounted at the balance sheet date.

For repaid loans, there is no asset that could be adjusted, therefore any potential liability arising from the legal risks has to be accounted for under IAS 37. As the provisions being measured in case of repaid loans involves a large population of items, the Bank applies "expected value" method in which the obligation is estimated by weighting all possible outcomes by their associated probabilities.

The above estimates are determined by the judgement of the Bank, supplemented by experience of similar events and opinions of independent experts. The evidence considered includes any additional evidence provided by events after the end of the reporting period. The details of the methodology and calculation are described further in this note.

The impact of the legal risk related to court cases concerning indexation clauses in mortgage and housing loans in CHF and the voluntary settlement program

The method used to calculate the impact of the legal risk related to court cases concerning indexation clauses in mortgage and housing loans in CHF and the voluntary settlement program is based on parameters that are highly judgmental and with a high range of possible values. It is possible that the impact of the legal risk will have to be adjusted significantly in the future, particularly that important parameters used in calculations are interdependent.

The cumulative impact of legal risk associated with litigation (individual lawsuits and class actions) related to indexation clauses in CHF mortgages and home loans and the voluntary settlement program included in the Bank's statement of financial position is shown in the table below.

PLN thousand	31.12.2021	31.12.2020
Impact of legal risk concerning individual lawsuits related to active loans recognised as a reduction of gross carrying amount of loans	2 484 852	1 264 677
Impact of legal risk concerning class action case related to active loans recognised as a reduction of gross carrying amount of loans	290 445	-
Impact of legal risk concerning individual lawsuits related to repaid loans and low value active loans recorded as provisions for legal proceedings	348 476	175 911
Potential costs of voluntary settlement program recognised as a reduction of gross carrying amount of loans	1 009 800	-
The cumulative impact of legal risk associated with litigation related to indexation clauses mortgages and home loans in CHF	**4 133 573**	**1 440 588**

Total costs of legal risk related to foreign currency loans recognised in the income statement for 2021 amounted to PLN 2 758.1 million (in 2020: PLN 1 021.7 million). The most important element of these costs in 2021 was the increase of the impact of the legal risk related to individual court cases in the amount of PLN 1 298.7 million, which mainly resulted from (i) higher than expected inflow of cases in 2021, (ii) changes in level of loss on loan exposure in case of losing the case by the Bank including an increase in the probability of the occurrence of a negative scenario for the bank of cancellation of loan agreements without the possibility of an effective claim for payment of the cost of using the capital made available to the borrower.

In addition, significant components of the amount recognised in the income statement in 2021 are costs of the potential settlement program in the amount of PLN 1 009.8 million, costs of the class action case concerning indexation clauses contained in CHF mortgage and housing loan agreements in the amount of PLN 363.0 million as well as cost of counterclaims related to securing the Bank's claims in indexation cases in the amount of PLN 86.1 million.

Methodology of calculation the impact of the legal risk related to individual court cases

The methodology of calculation the impact of the legal risk related to individual court cases concerning both active and repaid loans applied by the Bank depends on numerous assumptions that take into account historical data adjusted with the Bank’s expectations regarding the future and associated with significant degree of expert judgement. The most important assumptions are: an expected population of borrowers who will file a lawsuit against the Bank, the probability of losing the case having final and binding judgement, the distribution of expected verdicts judged by the courts and the loss to be incurred by the Bank in case of a losing the case in court.

Expected population of borrowers

The population of borrowers who will file a lawsuit against the Bank has been projected over the remaining life of the portfolio based on the Bank’s history of legal cases in the past and assumes a further inflow of new cases. The Bank assumes that inflow of plaintiffs will be significant until the end of 2025. The Bank assumes that vast majority of the projected cases will be filed until the end of 2023, and then their number will decrease following the expected clarification of the legal environment.

For the purpose of calculating the impact of legal risk mBank assumes that approximately 27% of FX borrowers (i.e. 23 thousand borrowers with both, active: 41% and repaid loans: 9.4%) filed or will file a lawsuit against the Bank (as of 31 December 2020: 18%, i.e. 15.4 thousand). The Bank observes that clients with higher loan amounts were the first ones to file the claims (27% of customers represent 35% of the total CHF loan portfolio, both active and repaid), and therefore that average ticket of the suing population will be decreasing over time. The assumption, due to significant legal uncertainties surrounding CHF cases as well as other external factors that may shape clients’ preferences to file the lawsuits, is highly judgmental and may be a subject to an adjustment in future. In 2021 the Bank increased the assumed number of court cases by 47%, in comparison to the assumptions for the end of 2020. This was due to an increase in the forecast of lawsuits that the Bank estimates will be filed with the Bank in the future, and greater than expected number of lawsuits that were filed with the Bank. If an additional 1% of the borrowers (both holding active loans in CHF as well as borrowers who already repaid their loans in CHF) filed a lawsuit against the Bank, the impact of the legal risk would increase by approximately PLN 68.4 million (while other relevant assumptions remain constant) as compared to 31 December 2021, of which PLN 51.9 million would reduce gross carrying amount of the loans, and PLN 16.5 million would increase the “Provisions for legal proceedings”.

The bank estimates that part of borrowers with CHF indexed loans will not decide to sue the Bank or sign a settlement with the Bank in the future. In the Bank's opinion this will be influenced by the following factors: clients' expectations regarding future changes in the CHF/PLN exchange rate, clients' expectations regarding future costs of PLN loans, changes in jurisprudence in CHF loan cases, tax solutions regarding settlements, costs and duration of court proceedings, individual factors (in particular the loan repayment period and the current amount of debt).

Probability of losing the case

The Bank believes that since the current line of jurisprudence in CHF cases is inconsistent, the probability of losing court cases must, to a large extent, be based on professional judgement supported by external legal opinion until Polish Supreme Court and the CJEU address all the legal uncertainties (in particular, whether the abusive clauses may be replaced by another way of determining the foreign exchange rate pursuant to provisions of law, or whether, in the absence of the possibility of replacing the abusive clause by a provision of law, the contract may be binding on the parties in its remaining scope and whether banks may receive a compensation for usage of the principal granted).

Since, in the opinion of the Bank, the number of final verdicts is not statistically representative (too few binding verdicts have been issued by courts in cases related to mBank) the assumption of probability of losing in court takes also into account expert judgements of the Bank supported by an external legal opinions about the future trends in the court verdicts as well as upcoming verdicts of the Supreme Court and CJEU. As of 31 December 2021 the Bank assumes probability of losing in court at the level of 50% (as of 31 December 2020: 50%), basing on its own judgement supported by the external legal opinion. If the assumed probability of losing in court changed by +/- 1 percentage point and all other relevant assumptions remained constant, the impact of the legal risk would change by +/- PLN 54.7 million, of which PLN 50.3 million would change gross carrying amount of the loans, and PLN 4.4 million would change the "Provisions for legal proceedings".

The projected loss rate

The projected loss rate was calculated using the probabilities of different verdicts that may be issued. As currently there is still no homogenous line of verdicts taken by the courts the Bank took into account three possible losing scenarios: (i) the contract remains valid but the indexation mechanism is eliminated, which transforms a loan indexed to CHF into a PLN loan subject to the interest rate of the loan indexed to CHF, (ii) the contract is invalid in whole because deleting the exchange rate clause would be too far-reaching change (based on assumption that this clause defines the main subject matter of the contract), and (iii) the contract remains a mortgage indexed to CHF, but the FX clause is substituted by the fixing rate of the NBP. Under scenario (ii), the Bank takes into account two versions of the invalidity, assuming that the parties settle accounts in a formula similar to the settlement on a net basis. The first version assumes that the consumer is obliged to return the disbursed capital together with the remuneration for using it, and the second assumes that the consumer is only obliged to return the capital without remuneration. The Bank assumed the probability of each of these scenarios at the same level.

Each of these scenarios is associated with a different level of predicted losses for the Bank. The Bank calculated the average level of loss weighted with the probabilities of occurrence of the given scenario in case of negative final and binding judgement, with invalidity scenario assumed to be most probable. The probabilities of those scenarios applied by the Bank has been based on the assessment of the Bank consulted with the legal advisor. As of 31 December 2021 the average loss rate was equal to 76.5% of gross carrying amount of active loans and 33.7% of total value of the loan granted for repaid loans, (as of 31 December 2020 62.8% and 21.8% respectively).

If the assumed weighted average loss changed by +/- 1 percentage point and all other relevant assumptions remained constant the impact of the legal risk would change by +/- PLN 37.1 million, of which PLN 32.9 million would change gross carrying amount of the loans, and PLN 4.2 million would change the "Provisions for legal proceedings".

Methodology of calculation the impact of the legal risk related to the class action case

In the second half of 2021, the Bank recognised the impact of the legal risk related to a class action case in the total amount of PLN 363.0 million. The recognition of additional costs for class action case was preceded by an analysis of the chances of litigation in the light of the current case law and guidelines of the Court of Appeal for the District Court re-examining the case, supported by an opinion of the law firm handling the case. The increased likelihood of an unfavourable verdict, particularly one invalidating the loan agreements covered by the proceedings, justified the creation of a provision up to the amount of the claim.

Methodology of calculation settlement program costs

As at 31 December 2021, the Bank recognised the impact of legal risk in the amount of PLN 1 009.8 million to cover the costs of future settlements. The amount corresponds to 34% of the maximum cost of settlements under the formula adopted in the currently running pilot described above. This represents the management's estimate that reflects the intention towards future voluntary settlements or, in case it is not fully used for that purpose, to cover currently unforeseen cost related to legal risks of CHF portfolio.

In the bank's opinion, the future level of acceptance of settlements depends on a number of factors, the most important of which are:

- financial terms of the offer,
- further development of the court judicature in the CHF cases, in particular the resolution of the issue of application of dispositive provisions in place of clauses deemed abusive, the bank's right to reimbursement of the costs of using the capital made available to the client in case the agreement is deemed invalid, admissibility of declaring the loan agreement invalid,
- duration of court proceedings in CHF cases,
- changes in interest rates for PLN loans,
- changes in the CHF/PLN exchange rate,
- tax solutions as regards settlements.

In the absence of historical market data on settlement programs, the ongoing pilot program and a significant level of uncertainty as to the final shape of the jurisprudence in CHF credit cases the exact impact of the above mentioned factors, as of 31 December 2021 is difficult to estimate.

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For the purpose of determining the value of the provision as of 31 December 2021, the bank assumed that the maximum level of the offer acceptance will not exceed 34% of active contracts. If the assumed level of the offer acceptance changed by +/- 1 percentage point and all other relevant assumptions remained constant the impact of the legal risk would change by +/- PLN 29.7 million which would change gross carrying amount of the loans.

35. Off-balance sheet liabilities

Off-balance sheet liabilities of the Bank comprise: loan commitments, guarantees and other financial facilities, other liabilities.

The amounts and dates by which the Bank will be obliged to realise its off-balance sheet financial liabilities by granting loans or other monetary services are presented in the table below.

Loan commitments, guarantees and other financial facilities and other commitments

31.12.2021	Nominal amount of off-balance sheet commitments and financial guarantees under IFRS 9 impairment				Provisions on off-balance sheet commitments and financial guarantees under IFRS 9 impairment			
	Stage 1	Stage 2	Stage 3	POCI	Stage 1	Stage 2	Stage 3	POCI
Loan commitments	30 580 113	424 899	50 803	8 910	50 339	14 576	24 555	1 166
Guarantees and other financial facilities	6 998 437	245 546	309 900	2 523	35 692	1 153	225 860	(1 507)
Other commitments	2 541	-	-	-	-	-	-	-

31.12.2020	Nominal amount of off-balance sheet commitments and financial guarantees under IFRS 9 impairment				Provisions on off-balance sheet commitments and financial guarantees under IFRS 9 impairment			
	Stage 1	Stage 2	Stage 3	POCI	Stage 1	Stage 2	Stage 3	POCI
Loan commitments	29 733 554	1 278 390	23 064	5 523	44 598	36 829	5 510	2 495
Guarantees and other financial facilities	6 996 852	918 829	121 128	36 166	20 630	6 134	80 055	25 940
Other commitments	22 789	-	-	-	-	-	-	-

The following table presents the Bank's off-balance sheet commitments granted and received as well as nominal value of open positions of derivative transactions of the Bank as at 31 December 2021 and as at 31 December 2020.

Guarantees are presented in the table below based on the earliest contractual maturity date.

31.12.2021	up to 1 year	from 1 to 5 years	more than 5 years	Total
Contingent liabilities granted and received	**27 864 414**	**13 716 685**	**5 170 155**	**46 751 254**
Commitments granted	**23 440 287**	**10 398 850**	**4 784 535**	**38 623 672**
Financing	20 182 907	7 525 067	3 356 751	31 064 725
loan commitments	*20 182 907*	*7 525 067*	*3 356 751*	*31 064 725*
Guarantees and other financial facilities	3 254 839	2 873 783	1 427 784	7 556 406
guarantees and standby letters of credit	*3 254 839*	*2 873 783*	*1 427 784*	*7 556 406*
Other commitments	2 541	-	-	2 541
Commitments received	**4 424 127**	**3 317 835**	**385 620**	**8 127 582**
- Financial commitments received	464 840	-	-	464 840
- Guarantees received	3 959 287	3 317 835	385 620	7 662 742
Derivative financial instruments (nominal value of contracts)	**313 428 962**	**452 048 970**	**49 824 400**	**815 302 332**
Interest rate derivatives	199 338 323	429 996 786	48 872 035	678 207 144
Currency derivatives	107 205 767	21 934 729	917 185	130 057 681
Market risk derivatives	6 884 872	117 455	35 180	7 037 507
Total off-balance sheet items	**341 293 376**	**465 765 655**	**54 994 555**	**862 053 586**

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31.12.2020	up to 1 year	from 1 to 5 years	more than 5 years	Total
Contingent liabilities granted and received	**27 310 390**	**12 374 467**	**6 067 654**	**45 752 511**
Commitments granted	**24 230 279**	**9 242 902**	**5 663 114**	**39 136 295**
Financing	21 087 057	6 723 710	3 229 764	31 040 531
loan commitments	*21 087 057*	*6 723 710*	*3 229 764*	*31 040 531*
Guarantees and other financial facilities	3 120 433	2 519 192	2 433 350	8 072 975
guarantees and standby letters of credit	*3 120 433*	*2 519 192*	*2 433 350*	*8 072 975*
Other commitments	22 789	-	-	22 789
Commitments received	**3 080 111**	**3 131 565**	**404 540**	**6 616 216**
- Financial commitments received	33 019	426 410	-	459 429
- Guarantees received	3 047 092	2 705 155	404 540	6 156 787
Derivative financial instruments (nominal value of contracts)	**210 863 420**	**405 382 233**	**41 776 440**	**658 022 093**
Interest rate derivatives	107 207 677	379 885 595	40 212 220	527 305 492
Currency derivatives	100 016 459	25 451 079	919 765	126 387 303
Market risk derivatives	3 639 284	45 559	644 455	4 329 298
Total off-balance sheet items	**238 173 810**	**417 756 700**	**47 844 094**	**703 774 604**

The nominal values of derivatives are presented in the Note 19.

As at 31 December 2021, commitments received by the Bank in the amount of PLN 8 127 582 thousand (31 December 2020: PLN 6 616 216 thousand), related mainly to guarantees received as collateral of loans and advances granted.

36. Pledged assets

Assets may be pledged as collateral for repo or sell/buy back transactions, derivative contracts with other banks. Collateral may be also placed due to stock market derivatives such as futures, options and participation in stock market.

Collateral may be placed in different form (e.g. cash, securities and pledged assets).

Similarly, customers establish collateral on their assets to secure the transaction with the Bank. If securities are subject to collateral (in buy/sell back transaction) they can be re-pledged in the opposite transaction (sell/buy back).

Moreover the Bank accepts collaterals in the form of properties (esp. real estates) related to credit type transactions like mortgage loans, credit lines, banking guarantees.

The table below presents the breakdown of the measures possible to pledge by the main items of the statement of financial position of mBank. Treasury securities are the main component of the Bank's liquidity collateral that can be eligible to pledge.

31.12.2021	Assets			Fair value of collateral received in kind of securities related with buy/sell back transactions			Assets available for pledge (3+6)
	Total assets	Pledged assets	Eligible for pledge assets	Received	Reused	Available for pledge	
	1	2	3	4	5	6	7
Debt securities (Note 19, 20, 21 and 22), including:	53 359 531	2 649 157	48 199 334	5 941 696	128 964	5 812 732	54 012 066
- NBP bills	*8 495 243*	*-*	*8 495 243*	*-*	*-*	*-*	*8 495 243*
- Government bonds	*36 234 523*	*2 079 125*	*34 155 397*	*5 941 696*	*128 964*	*5 812 732*	*39 968 129*
- Mortgage bonds	*1 055 151*	*-*	*-*	*-*	*-*	*-*	*-*
- Other non-treasury securities	*7 574 614*	*570 032*	*5 548 694*				*5 548 694*
Cash collaterals (due to derivatives transactions) (Note 22)	974 889	974 889	-	-	-	-	-
Other assets	137 539 399	-	-	-	-	-	-
Total	**191 873 819**	**3 624 046**	**48 199 334**	**5 941 696**	**128 964**	**5 812 732**	**54 012 066**

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31.12.2020	Assets			Fair value of collateral received in kind of securities related with buy/sell back transactions			Assets available for pledge (3+6)
	Total assets	Pledged assets	Eligible for pledge assets	Received	Reused	Available for pledge	
	1	2	3	4	5	6	7
Debt securities (Note 19, 20, 21 and 22), including:	51 944 836	3 967 830	46 094 707	6 357 913	474 210	5 883 703	51 978 410
- NBP bills	*149 997*	-	149 997	-	-	-	149 997
- Government bonds	*44 082 273*	*3 967 830*	40 114 443	*6 357 913*	*474 210*	*5 883 703*	45 998 146
- Mortgage bonds	*550 331*	-	-	-	-	-	-
- Other non-treasury securities	*7 162 235*	-	*5 830 267*	-	-	-	5 830 267
Cash collaterals (due to derivatives transactions) (Note 22)	785 131	785 131	-	-	-	-	-
Other assets	118 015 040	-	-	-	-	-	-
Total	**170 745 007**	**4 752 961**	**46 094 707**	**6 357 913**	**474 210**	**5 883 703**	**51 978 410**

The value of treasury securities presented as pledged assets, except for collaterals due to sell/buy back transactions, includes Bank's collateral of liabilities due to the fixed interest rate loans received from the EIB, collateral for the guaranteed deposits fund under the Bank Guarantee Fund (BFG) and collateral for the payment commitment to the BFG guarantee fund and forced restructuring fund.

37. Registered share capital

The total number of ordinary shares as at 31 December 2021 was 42 384 884 shares (31 December 2020: 42 367 040 shares) of PLN 4 nominal value each. All issued shares were fully paid up.

REGISTERED SHARE CAPITAL (THE STRUCTURE) AS AT 31 DECEMBER 2021						
Share type	Share type	Share type	Share type	Share type	Share type	Registered in
ordinary bearer*	-	-	9 989 000	39 956 000	fully paid in cash	1986
ordinary registered*	-	-	11 000	44 000	fully paid in cash	1986
ordinary bearer	-	-	2 500 000	10 000 000	fully paid in cash	1994
ordinary bearer	-	-	2 000 000	8 000 000	fully paid in cash	1995
ordinary bearer	-	-	4 500 000	18 000 000	fully paid in cash	1997
ordinary bearer	-	-	3 800 000	15 200 000	fully paid in cash	1998
ordinary bearer	-	-	170 500	682 000	fully paid in cash	2000
ordinary bearer	-	-	5 742 625	22 970 500	fully paid in cash	2004
ordinary bearer	-	-	270 847	1 083 388	fully paid in cash	2005
ordinary bearer	-	-	532 063	2 128 252	fully paid in cash	2006
ordinary bearer	-	-	144 633	578 532	fully paid in cash	2007
ordinary bearer	-	-	30 214	120 856	fully paid in cash	2008
ordinary bearer	-	-	12 395 792	49 583 168	fully paid in cash	2010
ordinary bearer	-	-	16 072	64 288	fully paid in cash	2011
ordinary bearer	-	-	36 230	144 920	fully paid in cash	2012
ordinary bearer	-	-	35 037	140 148	fully paid in cash	2013
ordinary bearer	-	-	36 044	144 176	fully paid in cash	2014
ordinary bearer	-	-	28 867	115 468	fully paid in cash	2015
ordinary bearer	-	-	41 203	164 812	fully paid in cash	2016
ordinary bearer	-	-	31 995	127 980	fully paid in cash	2017
ordinary bearer	-	-	24 860	99 440	fully paid in cash	2018
ordinary bearer	-	-	13 385	53 540	fully paid in cash	2019
ordinary bearer	-	-	16 673	66 692	fully paid in cash	2020
ordinary bearer	-	-	17 844	71 376	fully paid in cash	2021
Total number of shares			**42 384 884**			
Total registered share capital				**169 539 536**		
Nominal value per share (PLN)		**4**				

* As at the end of the reporting period

In 2021, the National Depository of Securities (KDPW) has registered 17 844 shares of mBank, which were issued as part of the conditional increase in the share capital of the Bank by issuance of shares with no subscription rights for the existing shareholders in order to enable beneficiaries of the incentive programmes to take up shares in mBank. As a result of the above registration, in 2021 mBank's share capital increased by PLN 71 376.

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Commerzbank AG is a shareholder holding over 5% of the share capital and votes at the general meeting and as at 31 December 2021 it held 69.25% of the share capital and votes at the general meeting of mBank S.A.

The changes in the ownership structure of Bank's material shares packages

On 25 November 2021, the Bank received from Nationale-Nederlanden Powszechne Towarzystwo Emerytalne S.A. (Nationale-Nederlanden PTE) notification of a reduction in the share of funds managed by Nationale-Nederlanden PTE in the number of votes at the General Meeting of mBank S.A. below 5% as a result of the sale of mBank S.A. shares in transactions on the Warsaw Stock Exchange (WSE), settled on 23 November 2021. As a result of this transaction, the funds managed by Nationale-Nederlanden PTE held a total of 2 110 771 shares of mBank S.A., which constituted 4.981% of the share capital of mBank S.A. and entitled to 2 110 771 votes at the general meeting of mBank S.A.Before the transaction, the funds managed by Nationale-Nederlanden PTE held a total of 2 138 948 shares of mBank S.A., which constituted 5.047% of the share capital of mBank S.A. and entitled to 2 138 948 votes at the general meeting of mBank S.A.

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.

The increase of share premium in 2021 and 2020 results from the issue of shares under incentive programmes described under Note 43.

39. Retained earnings

Retained earnings include: other supplementary capital, other reserve capital, general banking risk reserve, profit (loss) from the previous years and profit for the current year.

Other supplementary capital, other reserve capital and general banking risk reserve are created from profit for the current year and their aim is described in the by-laws or in other regulations of the law.

	31.12.2021	**31.12.2020**
Other supplementary capital	9 216 652	9 216 652
Other reserve capital	33 979	30 329
General banking risk reserve	1 115 143	1 115 143
Profit from the previous year	2 098 482	2 005 435
Profit (loss) for the current year	(1 215 353)	93 047
Total retained earnings	**11 248 903**	**12 460 606**

According to the Polish legislation, each bank is required to allocate 8% of its net profit to a statutory undistributable other supplementary capital until this supplementary capital reaches 1/3 of the share capital.

In addition, the Bank transfers some of its net profit to the general banking risk reserve to cover unexpected risks and future losses. The general banking risk reserve can be distributed only on consent of shareholders at a general meeting.

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40. Other components of equity

	31.12.2021	31.12.2020
Exchange differences on translating foreign operations	**2 506**	**(2 297)**
Unrealized gains (foreign exchange gains)	34 267	30 841
Unrealized losses (foreign exchange losses)	(31 761)	(33 138)
Cash flow hedges	**(495 965)**	**405 680**
Unrealized gains	-	500 839
Unrealized losses	(612 303)	-
Deferred income tax	116 338	(95 159)
Valuation of debt instruments at fair value through other comprehensive income	**(956 540)**	**17 728**
Unrealized gains on debt instruments	11 503	254 555
Unrealized losses on debt instruments	(1 099 039)	(166 538)
Deferred income tax	130 996	(70 289)
Actuarial gains and losses relating to post-employment benefits	**(10 619)**	**(17 328)**
Actuarial gains	1 024	-
Actuarial (losses)	(14 134)	(21 393)
Deferred income tax	2 491	4 065
Share of other comprehensive income of entities under the equity method	**(11 842)**	**16 268**
Share of other comprehensive income of subsidiaries and associates	(11 842)	16 268
Reclassification to investment properties	**11 436**	**-**
Gains on reclassification to investment properties	14 118	-
Deferred income tax	(2 682)	-
Total other components of equity	**(1 461 024)**	**420 051**

41. Dividend per share

On 24 March 2021, the 34th Annual General Meeting of mBank S.A. adopted a resolution regarding the distribution of the net profit for 2020. The net profit of mBank S.A. in the amount of PLN 93 047 thousand was left undivided.

42. Explanatory notes to the statement of cash flows

Cash and cash equivalents

For the purposes of the cash flow statement cash and cash equivalents include the following balances with maturities of less than three months.

	31.12.2021	31.12.2020
Cash and balances with the Central Bank (Note 18)	12 087 608	3 939 298
Loans and advances to banks (Note 22)	335 348	265 834
Total cash and cash equivalents	**12 422 956**	**4 205 132**

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Supplementary information to the cash flow statement

Explanation of differences between the change in the balances resulting from the balance sheet and the change disclosed in the cash flows from operating activities

	Year ended 31 December	
	2021	**2020**
Loans and advances to banks - change in the balance of the statement of financial position	**(349 072)**	**(3 508 141)**
Exclusion of a change in the balance of cash and cash equivalents	69 514	(76 620)
Total change in loans and advances to banks	**(279 558)**	**(3 584 761)**
Financial assets held for trading and hedging derivatives - change in the balance of the statement of financial position	**(462 481)**	**914 143**
The difference between the interest accrued and paid in cash in the period	2 849	61 817
Valuation included in other comprehensive income	(1 113 142)	350 037
Total change in financial assets held for trading and hedging derivatives	**(1 572 774)**	**1 325 997**
Loans and advances to customers change in the balance of the statement of financial position	**(9 065 354)**	**(4 010 845)**
The difference between the interest accrued and paid in cash in the period	37 109	(241 856)
Total change in loans and advances to customers	**(9 028 245)**	**(4 252 701)**
Financial assets at fair value through other comprehensive income - change in the balance of the statement of financial position	**(754 804)**	**(13 339 642)**
Valuation included in other comprehensive income	(1 175 553)	(5 735)
The difference between the interest accrued and paid in cash in the period	(214 265)	(587 030)
Total change in financial assets at fair value through other comprehensive income	**(2 144 622)**	**(13 932 407)**
Debt securities measured at amortised cost - change in the balance of the statement of financial position	**(680 414)**	**(4 717 628)**
The difference between the interest accrued and paid in cash in the period	(73 131)	-
Total change in debt securities measured at amortised cost	**(753 545)**	**(4 717 628)**
Other assets - change in the balance of the statement of financial position	**(115 471)**	**(282 201)**
Balances unrealised in cash recognised in the income statement	-	3 042
Exclusion of change in cash flows from financing activity	160 633	(91 047)
Total change of other assets	**45 162**	**(370 206)**
Amounts due to other banks - change in the balance of the statement of financial position	**795 715**	**1 443 504**
The difference between the interest accrued and paid in cash in the reporting period	31 482	14 358
Exclusion of change in cash flows from financing activity	-	193 144
Total change in amounts due to other banks	**827 197**	**1 651 006**
Amounts due to customers - change in the balance of the statement of financial position	**22 127 957**	**15 841 047**
The difference between the interest accrued and paid in cash in the reporting period	9 203	(375 510)
Exclusion of change in cash flows from financing activity	1 448 151	591 117
Exchange differences	(52 516)	-
Exclusion of increase in lease liabilities	(320 745)	-
Amounts due to customers - change in the balance of the statement of financial position	**23 212 050**	**16 056 654**
Debt securities issued - change in the balance of the statement of financial position	**348 458**	**2 973 168**
The difference between the interest accrued and paid in cash in the reporting period	(7 699)	(343 746)
Exchange differences	(114 185)	-
Exclusion of change in cash flows from financing activity	(289 289)	143 042
Total change in debt securities issued	**(62 715)**	**2 772 464**
Changes in other liabilities - change in the balance of the statement of financial position	**386 348**	**635 669**
Valuation of incentive programmes recognised in income statement (Note 12)	10 487	10 159
Exclusion of tax liabilities of certain financial institutions	-	(10 943)
Actuarial gains and losses relating to post-employment benefits recognised in other comprehensive income (Note 17)	8 283	(7 698)
Exclusion of change in cash flows from investing activity	39 218	-
Exclusion of liabilities classified as held for sale	(7 425)	-
Total change in other liabilities (including liabilities classified as held for sale) and provisions	**436 911**	**627 187**

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Interests received and paid from operating activities

	Year ended 31 December	
	2021	**2020**
Interest income, including:		
Loans and advances to banks	105 139	120 540
Loans and advances to customers	2 828 652	3 222 396
Debt securities	770 080	973 437
Interest income on derivatives classified into banking book	103 776	61 011
Interest income on derivatives concluded under hedge accounting	296 857	216 971
Other interest income	18 014	275 355
Total interest income	**4 122 518**	**4 869 710**
Interest expense, including:		
Settlements with banks due to deposits received	(31 482)	(17 596)
Settlements with customers due to deposits received	(71 868)	(547 535)
Security deposit received in relation with the guarantee granted to secure underwriting of securities	-	(59 417)
Issuance of debt securities in issue	(80 189)	(16 157)
Other interest expense	(42 461)	(32 029)
Total interest expense	**(226 000)**	**(672 734)**

Cash flows from investing activities

In 2021 and 2020, cash flows from investing activities were related to the acquisition, sale and increase of shares in subsidiaries as well as dividends received by the Bank. In 2020, cash flows from investing activities includes the inflow related to the reduction of BDH Development Sp. z o.o. (BDH) share capital related to the redemption of shares and the proceeds from the sale of shares in BDH. Other cash flows from this activity relate to settlements in connection with the purchase of intangible assets and fixed assets.

Cash flows from financing activities

Cash flows from financing activities mainly relate to the inflows from issue of debt securities issued by the Bank, inflows from the issue of subordinated liabilities and settlements due to long-term loans received from other banks (Note 29) and the European Investment Bank (Note 29).

The following table presents the change in liabilities as part of financial activities.

	As at 01.01.2021	Cash flows	Change not connected with cash flows	As at 31.12.2021
Loans and advances to other customers (Note 29)	3 254 591	(1 363 406)	15 436	1 906 621
Lease liabilities (Note 29)	748 497	(89 901)	295 400	953 996
Debt securities in issue (Note 29)	6 335 165	289 289	59 169	6 683 623
Subordinated liabilities (Note 29)	2 578 327	(54 535)	100 664	2 624 456
Total liabilities from financing activities	**12 916 580**	**(1 218 553)**	**470 669**	**12 168 696**

	As at 01.01.2020	Cash flows	Change not connected with cash flows	As at 31.12.2020
Loans and advances to banks (Note 29)	189 900	(199 137)	9 237	-
Loans and advances to other customers (Note 29)	2 980 294	(5 591)	279 888	3 254 591
Lease liabilities (Note 29)	465 790	(111 846)	394 553	748 497
Debt securities in issue (Note 29)	3 361 997	(143 042)	3 116 210	6 335 165
Subordinated liabilities (Note 29)	2 500 217	(76 145)	154 255	2 578 327
Liabilities due to the deposit related to guarantee of eurobonds issue (Note 29)	5 097 329	(479 271)	(4 618 058)	-
Total liabilities from financing activities	**14 595 527**	**(1 015 032)**	**(663 915)**	**12 916 580**

In the change not related to cash flows exchange differences and accrued interest were included.

The total cash outflow from leases (including cash flow related to short-term lease contracts, low-value asset lease contracts that are not short-term contracts and variable components of lease liabilities that are disclosed in cash flows from operating activities) amounted to PLN 92 383 thousand (in 2020: PLN 114 519 thousand).

43. Share-based incentive programmes

2014 Incentive Programme for the Management Board Members of the Bank

On 31 March 2014 the Supervisory Board in accordance with the recommendation of Remuneration Committee of the Supervisory Board adopted a Regulation of the Incentive Programme in mBank S.A., which replaced the Regulation of the Incentive Programme in mBank S.A. dated at 7 December 2012.

On 2 March 2015 the Supervisory Board extended the duration of the program from 31 December 2018 to 31 December 2021.Under the program the Management Board Members have the right to bonus, including non-cash bonus paid in Bank's shares.

The net ROE of mBank Group and the monthly remuneration of the member of the Board as at 31 December form the basis for acquisition by Members of the Management Board of the right to bonus and for calculation of the amount of bonus for a given financial year. Equivalent of 50% of the base amount calculated based on ROE constitutes the so-called first part of the bonus. In regard to the remaining 50% of the base amount, the Remuneration Committee of the Supervisory Board can grant the second part of the bonus if it decides that a given Member of the Management Board achieved the annual/multi-year business and development objective. The decision of granting the second part of the bonus is the sole responsibility of Remuneration Committee of the Supervisory Board, which according to its own judgement and decision confirm MBO achievement taking into account the situation on financial markets in the last/previous financial period.

The sum of the first and the second part of bonus is the base bonus of the member of the Board for a given financial period. 40% of the base bonus constitutes non-deferred bonus and is paid in the year of determination of base bonus as follows: 50% in form of cash payment and 50% in Bank's shares or bonds with pre-emptive rights to acquire shares. 60% of the base bonus is deferred bonus and is paid in three equal tranches in the next three consecutive years after the year of determining the base bonus as follows: 50% of each of the deferred tranches in form of cash payment and 50% of each of the deferred tranches in form of non-cash payment in Bank's shares or bonds with pre-emptive rights to acquire shares.

The Supervisory Board on the basis of recommendation of Remuneration Committee can make a decision to suspend in whole or reduce the amount of deferred tranche due to the later assessment of the performance of the Member of the Management Board over a period of time longer than one financial year (i.e. for the period of at least 3 years), which takes into account the business cycle of the Bank as well as the risk related to the bank's operations, but only when the actions or omissions of the Member of the Management Board had a direct and adverse impact on the Bank's financial result and market position within the assessment period and when at least one of the elements included in the assessment card was not fulfilled.

Remuneration Committee of the Supervisory Board can make a decision on suspending in whole or decreasing the non-deferred and deferred bonus amount for a given financial year, including deferred tranches not paid out yet, in a situation where one of the conditions of Article 142, paragraph 1 of the Banking Law Act, in particular in paragraph 2. Suspending in whole or decreasing the non-deferred and deferred bonus, as well as any deferred tranche by the Remuneration Committee of the Supervisory Board can also apply to the non-deferred and deferred bonus, including deferred tranche not paid out yet after expiry or termination of the management contract.

Under the program described above, for 2017 was awarded for the last time. The last settlements fall on 2021.

Cash Part of the Bonus

50% of the base amount constitutes bonus cash payment. It is recognised as a liability to employees and charged to the income statement in the correspondence to liability to employees.

Share-Based Payments Settled in mBank S.A. Shares

50% of the base amount constitutes bonus payment settled in mBank S.A. shares. The cost of payments settled in shares is recognised in the income statement in the correspondence with other reserve capital.

This is equity-settled share-based program.

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The table below presents change in the number and weighted average exercise prices of share options related to the 2014 incentive programme for the Management Board of mBank.

	31.12.2021		31.12.2020	
	Number of options	Weighted average exercise price (in PLN)	Number of options	Weighted average exercise price (in PLN)
Outstanding at the beginning of the period	**1 602**	**-**	**6 210**	**-**
Granted during the period	-	-	-	-
Forfeited during the period	-	-	-	-
Exercised during the period*	1 602	4	4 608	4
Expired during the period	-	-	-	-
Outstanding at the end of the period	**-**	**-**	**1 602**	**-**
Exercisable at the end of the period	**-**	**-**	**-**	**-**

* In 2021, the weighted average price of the shares was PLN 345.14 (in 2020: PLN 190.77).

Employee programme for key management staff of mBank Group of 2014

On 31 March 2014, the Supervisory Board of mBank adopted on the basis of recommendation of Remuneration Committee a resolution amending the rules of the employee programme, which replaced the incentive programme for key management staff of mBank Group from 2013.

The aim of the programme is to ensure growth in the value of a subsidiary's shares by linking the interest of the key staff of mBank Group with the interest of the subsidiary and its shareholders and implementing an mBank Group policy of variable components of remuneration of persons holding managerial positions in mBank Group.

On 2 March 2015, the Supervisory Board of mBank extended the duration of the program from 31 December 2020 to 31 December 2022 in accordance with the recommendation of the Remuneration Committee.

As part of the programme, bonds in tranche III, IV, V and VI were allocated to and acquired by the eligible persons. The last settlements of the above-mentioned Tranches were realized in 2017.

Beginning with Tranche VII the right to purchase bonds granted to the entitled person was divided into four parts, which may be realized respectively: I part – non-deferred bonds representing 50% of the 60% of the amount of discretionary bonus granted for a given financial year in the year of granting the right, and then another three equal parts – deferred bonds constituting 50% of the 40% of the amount of discretionary bonus granted for a given financial year on the lapse of 12, 24 and 36 months from the date of granting the rights. Beginning with Tranche VII the bonus for 2014 – 2017 was awarded. The last settlements are in 2021.

Cash Part of the Bonus

The bonus in the amount of 50% of the base amount for the year is cash payment. It is recognised as a liability to employees and charged to the income statement in the correspondence to the liability to employees.

Share-Based Payments settled in mBank S.A. shares

The bonus in the amount of 50% of the base amount constitutes a payment settled in mBank S.A. shares. The cost of payments settled in shares is recognised in the income statement in the correspondence with other reserve capital. This is equity-settled share-based program.

The table below presents change in the number and weighted average exercise prices of share options related to the 2014 incentive programme for key managers of mBank.

	31.12.2021		31.12.2020	
	Number of options	Weighted average exercise price (in PLN)	Number of options	Weighted average exercise price (in PLN)
Outstanding at the beginning of the period	**1 518**	**-**	**5 585**	**-**
Granted during the period	-	-	-	-
Forfeited during the period	107	-	-	-
Exercised during the period*	1 411	4	4 067	4
Expired during the period	-	-	-	-
Outstanding at the end of the period	**-**	**-**	**1 518**	**-**
Exercisable at the end of the period	-	-	**-**	**-**

* In 2021, the weighted average price of the shares was PLN 345.14 (in 2020: PLN 190.77).

2018 incentive programme for the Management Board Members and key staff of mBank Group – mBank Risk Takers

On 7 June 2018, the Supervisory Board, acting in line with the recommendation of the Remuneration Committee of the Supervisory Board and the decision of the Annual General Meeting of mBank S.A. of 9 May 2018, adopted the mBank S.A. Incentive Programme Rules.

The Programme replaced the existing programmes, that is the employee programme introduced by the resolution of the Extraordinary General Meeting of mBank S.A. of 27 October 2008, as amended, and the programme for the Management Board Members, introduced by the resolution of the Annual General Meeting of mBank S.A. of 14 March 2008, as amended. At the same time, the rights arising from bonds acquired under the replaced programmes are exercised under the rules of those programmes.

The new programme will be implemented from 1 January 2018 to 31 December 2028. Eligible persons under the programme include persons holding positions identified as having a material impact on the bank's risk profile pursuant to the Risk Takers Identification Policy, referred to as Risk Takers I or Risk Takers II, excluding Risk Takers II – Members of the Management Board of mBank Hipoteczny S.A., in which a different incentive programme is implemented.

Risk Taker I means a Member of the Management Board of the bank. Risk Taker II means a person holding a position identified as having a material impact on the bank's risk profile pursuant to the Risk Takers Identification Policy, including a person holding a position of a Management Board Member in an mBank Group subsidiary.

On the terms and conditions stipulated in the Rules and the Risk Takers Remuneration Policy, Risk Takers will be able to acquire warrants free of charge, and, by way of exercising the rights arising from the warrants, to acquire shares.

Bonus for Risk Takers I

The Supervisory Board determines the bonus amount for a given calendar year for each Management Board Member individually, based on the assessment of MBO achievement with respect to the period of at least 3 years, with the proviso that the bonus amount depends on the bonus pool. The bonus pool is a total of base amounts calculated for each Management Board Member. The base amount is calculated as a multiple of the base salary, which depends on the Economic Profit (EP); EP is calculated for the period of 3 years pursuant to the rules specified in the Risk Takers Remuneration Policy.

The bonus consists of the non-deferred part (40% of the bonus) and the deferred part (60% of the bonus).

Both the deferred part and the non-deferred part are divided into equal portions: 50% paid in cash and 50% paid in subscription warrants. The non-deferred part in cash is paid in the year when the bonus is granted. The other half of the non-deferred part (50%) is paid in the form of subscription warrants, not earlier than after the lapse of 12 months from the date on which the consolidated financial statements of mBank Group for a given calendar year, are approved.

The deferred part, both the cash portion and the subscription warrant portion, is paid in 5 equal annual tranches. In each tranche, the cash portion is paid once the consolidated financial statements of mBank Group for the previous calendar year have been approved, and the subscription warrant portion is paid not earlier than after the lapse of 12 months from the date on which the consolidated financial statements are approved.

Bonus for Risk Takers II

The bonus amount for a given calendar year is determined by the bank's Management Board for Risk Takers II (the bank's employees) or by a subsidiary's Supervisory Board for Risk Takers II (Members of the Management Board of an mBank Group subsidiary) on the basis of: assessment of MbO achievement for the period of the last three calendar years, the Economic Profit of mBank Group and the result of a business line/subsidiary/organisational unit.

The bonus consists of the non-deferred part (60% of the bonus) and the deferred part (40% of the bonus). Both, the deferred part and the non-deferred part are divided into equal portions: 50% paid in cash and 50% paid in subscription warrants. The non-deferred part in cash is paid in the year when the bonus is granted. The other half of the non-deferred part (50%) is paid in the form of subscription warrants, not earlier than after the lapse of 12 months from the date on which the consolidated financial statements of mBank Group for a given calendar year, are approved.

The deferred part, both the cash portion and the subscription warrant portion, is paid in 3 equal annual tranches. In each tranche, the cash portion is paid once the consolidated financial statements of mBank Group for the previous calendar year have been approved, and the subscription warrant portion is paid not earlier than after the lapse of 12 months from the date on which the consolidated financial statements are approved.

In case the bonus amount determined for a Risk Taker II for a given calendar year does not exceed one-third of their total annual remuneration or PLN 200 thousand, the bonus may be paid in cash in a non-deferred form based on a decision of mBank's Management Board with regard to employees of the Bank or by the Supervisory Board of a subsidiary with regard to members of the management boards of mBank Group subsidiaries.

The deferred bonus part for Risk Takers I and Risk Takers II is assessed in terms of its determination and payment. The Supervisory Board of mBank with respect to the Management Board, Management Board of mBank with respect to the bank's employees or the Supervisory Board of an mBank Group subsidiary with respect to Members of the subsidiary's Management Board, may decide to withhold the full amount or to reduce the amount of a deferred tranche if it concludes that in a time horizon longer than one financial year, i.e. a period of at least 3 years, the Risk Taker had a direct and negative impact on the financial result or the market position of the bank/subsidiary/group, violated the rules and standards adopted in mBank Group or directly contributed to significant financial losses, where at least one of the scorecard components has not been met or any of the premises stipulated in Article 142 especially (2) of the Banking Law Act has occurred.

If the circumstances referred to above occur at the stage of determining the Risk Taker bonus amount, the Supervisory Board of mBank/the Supervisory Board of the subsidiary/the Management Board of mBank may decide not to grant a bonus for a given calendar year or to reduce it.

Moreover, a Risk Taker I or Risk Taker II may be obliged, under the rules and within the time limit determined by the decision of the Supervisory Board of mBank/the Supervisory Board of the subsidiary/the Management Board of mBank, to return the bonus granted and paid for a given calendar year (i.e. the non-deferred part and all deferred parts) if he/she has violated rules and standards adopted in mBank Group, has materially violated the generally applicable law or has directly contributed to significant financial losses being the consequence of his/her deliberate adverse actions to the detriment of mBank Group/the subsidiary or has contributed to financial sanctions being imposed on the bank/subsidiary by supervisory bodies under a final and non-appealable decision.

The decision determining the occurrence of the said events may be taken by the end of the calendar year when the last tranche of the deferred part of the bonus granted for the year in which the event occurred is paid.

In the case of a resolution of the General Meeting of mBank S.A. on payment of dividend for a given year, a Risk Taker I and a Risk Taker II to whom the bonus has been granted within the deferred or non-deferred part is entitled to a cash equivalent, regardless of the bonus, pursuant to the rules specified in the Risk Takers Remuneration Policy, in connection with the deferral of the portion paid in subscription warrants.

The bonus under the aforesaid programme was granted to Risk Takers I and Risk Takers II for 2018 and 2019.

On 17 December 2020 the Supervisory Board, in accordance with a recommendation of the Remuneration Committee of the Supervisory Board, decided to amend the Risk Takers Remuneration Policy, bearing in mind the need to align the Policy with new Directive (EU) 2019/878 of the European Parliament and of the Council of 20 May 2019 amending Directive 2013/36/EU as well as the recommendation of the Polish Financial Supervision Authority on variable remuneration components at banks communicated in the letter dated 17 April 2020 regarding measures expected to be taken by banks in response to the COVID-19 pandemic outbreak. In particularly justified cases when there is a need to mitigate the risk connected with maintaining a sound capital base of the bank, enabling it to effectively respond to the economic situation in Poland arising from, for example, the Covid-19 pandemic, the Supervisory Board with regard to Risk Takers I and mBank's Management Board with regard to Risk Takers II may adopt a resolution to pay the cash tranche in whole or in part (both the non-deferred and deferred tranche) in the form of subscription warrants, starting from the bonus for 2020. In 2021, bonus for 2020 for Risk Takers II was awarded entirely in subscription warrants. In addition, pursuant to the resolution of the Supervisory Board, a variable remuneration was awarded to Risk Takers I in the form of subscription warrants. Payments will be made in accordance with the provisions of the Risk Takers Remuneration Policy. The execution of the first tranche is scheduled for 2022.

Starting from the bonus for 2021, the deferral period for the cash tranche and the tranche awarded in the form of subscription warrants will be extended: from three to five years for Risk Takers II being members of senior management (applicable to Managing Directors and members of the management boards of mBank Group subsidiaries) and from three to four years for the remaining Risk Takers.

In case the bonus amount determined for a Risk Taker II (excluding Risk Takers II being members of senior management: Managing Directors and members of the management boards of mBank Group subsidiaries) for a given calendar year does not exceed one-third of their total annual remuneration or PLN equivalent of EUR 50 000 (as at the date of the decision awarding the bonus), the bonus may be paid in whole in cash in a non-deferred form based on a decision of mBank's Management Board.

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The table below presents changes in the number of warrants for shares in relation to 2018 incentive programme for Management Board and key managers of mBank Group – mBank's Risk Takers.

	31.12.2021		31.12.2020	
	Number of warrants	Weighted average exercise price (in PLN)	Number of warrants	Weighted average exercise price (in PLN)
Outstanding at the beginning of the period	**33 264**	**-**	**17 067**	**-**
Granted during the period	79 297	-	24 195	-
Forfeited during the period	220	-	-	-
Exercised during the period*	14 831	4	7 998	4
Expired during the period	-	-	-	-
Outstanding at the end of the period	**97 510**	**-**	**33 264**	**-**
Exercisable at the end of the period	**-**	**-**	**-**	**-**

* In 2021, the weighted average price of the shares was PLN 345.14 (in 2020: PLN 190.77).

Summary of the Impact of the Programmes on the Bank's balance sheet and income statement

Share-Based Payments Settled in Shares

The table below presents changes in other reserve capital generated by the above mentioned incentive programmes for share-based payments settled in mBank S.A. shares.

	31.12.2021	31.12.2020
Incentive programs		
As at the beginning of the period	**30 329**	**27 320**
- value of services provided by the employees	10 487	10 159
- settlement of exercised options	(6 837)	(7 150)
As at the end of the period	**33 979**	**30 329**

Cash Payments

The cost of the cash part of the programmes is presented in Note 12.

44. Transactions with related entities

mBank S.A. is the parent entity of mBank S.A. Group and Commerzbank AG is the ultimate parent of the Group as well as the direct parent of mBank S.A.

All transactions between the Bank and related entities were typical and routine transactions concluded on terms, which not differ from arm's length terms, and their nature, terms and conditions resulted from the current operating activities conducted by the Bank. Transactions concluded with related entities as a part of regular operating activities include loans, deposits and foreign currency transactions.

The Bank provides standard financial services to the Bank's key management personnel, Members of the Supervisory Board of the Bank and close members of their families, which include maintaining bank accounts, taking deposits, granting loans or other financial services. In the Bank's opinion, these transactions are concluded on market terms.

Pursuant the Banking Law, the extension of a loan, cash advance, bank guarantee or other guarantee to the Members of the Management Board and Supervisory Board of the Bank, persons holding managerial positions at the Bank as well as at entities related financially or organisationally therewith, is governed by the by-laws adopted by the Supervisory Board of mBank S.A.

The by-laws set out detailed rules and debt limits for loans, cash advances, bank guarantees, and other guarantees in relation to aforementioned persons and entities which are consistent with the Bank's internal regulations defining the competences of granting credit decisions concerning retail and corporate clients of the Bank. A decision to grant a loan, cash advances, bank guarantee or other guarantee to a Member of the Management Board and Supervisory Board of the Bank, person holding managerial position at the Bank or an entity related financially or organisationally therewith in excess of the limits set by the Banking Law is taken by the resolution of the Management Board and by the resolution of the Supervisory Board.

The terms and conditions of such loans, cash advances, bank guarantees or other guarantees, including in particular those related to interest rates as well as fees and commissions, cannot be more advantageous than the terms and conditions offered by the Bank to its retail or corporate clients, respectively.

The table below presents the values of transactions between the Bank and Members of the Supervisory Board and the Management Board of mBank, key executive management of mBank, Members of the Supervisory Board and the Management Board of Commerzbank and other related persons and entities, as well as with transactions with other Commerzbank AG Group entities. The amounts of transactions include assets, liabilities and related costs and income as at 31 December 2021 and 31 December 2020 and for the respective periods then ended are as follows

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	Members of Supervisory Board, Management Board and key management personnel of mBank as well as Supervisory Board and Management Board of Commerzbank AG		Other related persons *		mBank's subsidiaries		Commerzbank AG		Other companies of the Commerzbank AG Group excluding mBank subsidiaries	
As at the end of the period	**31.12.2021**	**31.12.2020**	**31.12.2021**	**31.12.2020**	**31.12.2021**	**31.12.2020**	**31.12.2021**	**31.12.2020**	**31.12.2021**	**31.12.2020**
Statement of Financial Position										
Assets	3 669	2 104	1 833	748	20 331 269	17 964 178	1 204 403	773 702	37	2 806
Liabilities	18 585	10 214	4 156	5 829	556 352	801 682	2 884 929	2 590 735	73 658	69 810
Income Statement										
Interest income	52	42	41	32	189 072	232 490	33 504	49 832	138	400
Interest expense	(2)	(89)	-	(1)	(320)	(70 986)	(21 547)	(36 916)	(20)	(197)
Commission income	56	38	9	10	20 784	17 382	6 101	6 025	258	49
Commission expense	-	-	-	-	(217 814)	(177 850)	-	-	-	-
Other operating income	-	-	15	-	12 804	7 798	3 522	1 578	-	-
Overhead costs amortisation and other operating expenses	-	(22)	-	-	(4 522)	(6 304)	(5 192)	(6 488)	-	-
Contingent liabilities granted and received										
Commitments granted	669	743	145	234	2 763 259	2 791 357	1 564 733	1 721 547	3 514	7 409
Commitments received	-	-	-	-	-	-	1 895 575	1 911 651	-	-

** Other related persons and entities include: close family members of Members of the Supervisory and the Management Board of mBank, key executive management of mBank, Members of the Supervisory Board and the Management Board of Commerzbank, entities controlled or jointly controlled by above mentioned persons*

The item Contingent liabilities – Commitments granted includes the guarantee granted to subsidiary mBank Hipoteczny S.A in the amount of PLN 565 211 thousand (31 December 2020: PLN 609 909 thousand), which secures the risk of repayment of the credit portfolio granted by the subsidiary to the clients of commercial real estate sector. Additionally, the Bank recognised also the submitted deposit related to the aforementioned guarantee, in the same amount.

Management Board of mBank S.A.

As at the end of 2021 the Management Board functioned with the following composition:

1. Cezary Stypułkowski – President of the Management Board,
2. Andreas Böger – Vice-President of the Management Board, Chief Financial Officer,
3. Krzysztof Dąbrowski – Vice-President of the Management Board, Head of Operations and IT,
4. Cezary Kocik – Vice-President of the Management Board, Head of Retail Banking,
5. Marek Lusztyn – Vice-President of the Management Board, Head of Risk
6. Adam Pers – Vice-President of the Management Board, Head of Corporate and Investment Banking.

In 2021, there were no changes to the composition of the management board of mBank S.A.

Changes in the composition of the Supervisory Board of mBank S.A

As at the end of 2021 the Supervisory Board functioned with the following composition:

1. Agnieszka Słomka-Gołębiowska – Chairwoman,
2. Bettina Orlopp – Vice-Chairwoman,
3. Armin Barthel,
4. Tomasz Bieske,
5. Marcus Chromik,
6. Mirosław Godlewski,
7. Aleksandra Gren,
8. Fred Arno Walter.

In 2021 there were following changes in the composition of the Supervisory Board of mBank S.A.:

On 15 March 2021 Ms. Sabine Schmittroth resigned from membership in the Bank’s Supervisory Board with the effective date of 25 March 2021.

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On 25 March 2021 Mr. Fred Arno Walter was appointed as a member of the Bank's Supervisory Board.

On 27 August 2021 Mr. Jörg Hessenmüller resigned from membership in the Bank's Supervisory Board with the effective date of 30 September 2021.

On 24 September 2021 Ms. Bettina Orlopp was appointed as a Vice-Chairwoman of the Bank's Supervisory Board with the effective date of 1 October 2021.

On 25 October 2021 Mr. Armin Barthel was appointed as a member of the Supervisory Board of mBank S.A.

Supervisory Board and Management Board Remuneration

The table below presents the information on the salaries, bonuses and benefits paid and due to the Members of the Management Board of the Bank who were performing their functions at the end of 2021 and at the end of 2020, remuneration of the former Management Board Members and remuneration of Supervisory Board Members.

Renumeration paid (in PLN)	2021	2020
mBank Management Board		
Basic salary	11 892 665	12 291 821
Other benefits	1 423 271	1 561 942
Bonus for previous year	-	1 560 000
Deferred bonus	1 278 316	1 380 230
Remuneration of the former Management Board Members		
Bonus for previous year	-	1 359 355
Other benefits	3 210	185 897
Bonus for previous year	-	200 000
Deferred bonus	491 000	774 834
Compensation (no competition)	2 228 000	309 951
mBank Supervisory Board		
Basic salary	1 466 378	1 381 624

The total compensation of members of the Management Board consists of: basic salary, bonuses, termination payments of management agreement, prohibition of competitiveness payment, insurance costs and accommodation costs.

The above mentioned benefits are short-term employee benefits.

The total remuneration received in 2021 by Bank's Management Board members was PLN 14 594 thousand (2020: PLN 19 101 thousand).

In accordance with the Bank's remuneration system, the members of the Management Board of the Bank may be eligible to receive bonuses for the year 2021, which would be paid out in 2022. Therefore, a provision was created for the payment of a cash bonus for 2021 for the members of the Management Board, which amounted to PLN 2 313 thousand as of 31 December 2021 (31 December 2020: PLN 1 714 thousand). The final decision concerning the level of the bonus will be taken by the Remuneration Committee of the Supervisory Board by 3 March 2022.

In 2021 and 2020, the members of the Management Board of mBank S.A. did not receive compensation for their role as members of the management boards and supervisory boards of the Bank's related companies.

The total compensation of Members of the Supervisory Board, the Management Board and other key executive management of the Bank that perform their duties in 2021 amounted to PLN 21 796 thousand (2020: PLN 26 888 thousand).

Detailed information on the remuneration of individual Members of the Management Board and the Supervisory Board, as well as the composition of the Management Board and the Supervisory Board was presented in the Management Board Report on the Performance of mBank S.A. Group in 2021 in item 13.7. "Composition, powers and procedures of the Management Board and the Supervisory Board".

Information regarding proprietary position in Bank shares by Members of the Management Board and by Members of the Supervisory Board

As at 31 December 2021, the Bank shares were held by four Members of the Management Board: Mr. Cezary Stypułkowski – 25 230 shares, Mr. Andreas Böger – 1 646 shares, Mr. Krzysztof Dąbrowski – 892 shares and Mr. Cezary Kocik – 256 shares.

As at 31 December 2020, the Bank shares were held by six Members of the Management Board: Mr. Cezary Stypułkowski – 23 250 shares, Mr. Andreas Böger – 819 shares, Mr. Frank Bock – 766 shares, Mr. Krzysztof Dąbrowski – 1 682 shares and Mr. Cezary Kocik – 2 161 shares and Mr. Adam Pers – 158 shares.

45. Acquisitions and disposals

<u>Sale of shares in Tele-Tech Investment sp. z o.o.</u>

On 15 July 2021, mBank S.A. signed a conditional agreement for the sale of shares in the subsidiary Tele Tech Investment Sp. z o.o. and bonds issued by this company. After fulfilling the conditions precedent, on 19 July 2021, the Bank sold 100% of shares in the subsidiary and all bonds held by the Bank issued by that subsidiary.

<u>Liquidation of mFinance France S.A.</u>

In relation to substitution of the liabilities of mFinance France S.A. to mBank S.A., described in detail in the Note 29, starting from December 2020, mBank ceased to consolidate this company. The substitution process was completed in October 2020. On 4 November 2020, the Extraordinary General Meeting of shareholder of mFinance France S.A., adopted a resolution to open the liquidation process of the company and to appoint the liquidator. Company was removed from the French register of enterprises on 4 June 2021.

<u>Sale of BDH Development Sp. z o.o.</u>

On 16 December 2020, mBank S.A. and Archicom Polska S.A signed an agreement, on the basis of which mBank sold 100% of shares in share capital of BDH Development Sp. z o.o.

46. Capital adequacy

One of the bank's main tasks is to ensure an adequate level of capital. As part of the capital management policy, the bank creates a framework and guidelines for the most effective planning and use of the capital base, which:

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

The capital management policy in mBank is based on:

- maintenance of an optimal level and structure of own funds, assuring capital adequacy above the established minimum requirement (including risk appetite at approved level) as well as ensuring coverage against all material risks identified in mBank's activity,
- effective use of the capital base, guaranteeing achievement of expected returns, including return on regulatory capital and IFRS equity.

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 I capital ratio (calculated as a quotient of Common Equity Tier I capital to the total risk exposure amount), the Tier I ratio (calculated as a quotient of Tier I capital to the total risk exposure amount) and the total capital ratio (calculated as a quotient of own funds and the total risk exposure amount) at least on the level required by the supervision authority.

The strategic goals of mBank are aimed at maintaining the total capital ratio as well as the Tier I ratio and the Common Equity Tier I capital ratio above the level required by the supervision authority. This allows to maintain business development while meeting the supervisory requirements in the long perspective.

Capital ratios

The adequacy assessment of the capital base, including among others: the calculation of capital ratios and the leverage ratio, the own funds and the total capital requirement in mBank was made according to the following regulations:

- the Regulation (EU) No 575/2013 of the European Parliament and of the Council of 26 June 2013 on prudential requirements for credit institutions and investment firms and amending Regulation (EU) No 648/2012 (CRR Regulation);
- the Commission Implementing Regulation (EU) No 680/2014 of 16 April 2014 laying down implementing technical standards with regard to supervisory reporting of institutions according to Regulation (EU) No 575/2013 of the European Parliament and of the Council with further amendments (ITS Regulation);
- the Banking Act of 29 August 1997 (Dz.U. from year 2002 No 72, item 665) with further amendments;
- the Act on Macroprudential Supervision of the Financial System and Crisis Management of 5 August 2015 (Dz.U. 2015 item 1513);
- the Regulation of the Minister of Development and Finance of 25 May 2017 on the higher risk weight for exposures secured by mortgages on real estate,
- Regulation of the Minister of Development and Finance of 1 September 2017 regarding the systemic risk buffer.

As a result of the Act on Macro-prudential Supervision over the Financial System and Crisis Management in the Financial System (the Act) that entered into force in 2015 and transposed the CRD IV provisions to the Polish prudential regulations, as of 31 December 2021 Bank was obliged to ensure adequate own funds to meet conservation buffer of 2.5% of total risk exposure amount (31 December 2020: 2.5%).

As of the end of 2021 and 2020 the countercyclical capital buffer rate set for relevant exposures in Poland according with the article 83 of the Act amounted to 0%. mBank specific countercyclical capital buffer calculated in accordance with the provisions of the Act as the weighted average of the countercyclical buffer rates that apply in the countries where the relevant credit exposures of the Bank are located, amounted to 5 b.p. as of 31 December 2021 (31 December 2020: 4 b.p.). The value of the indicator was predominantly affected by the exposures of mBank’s foreign branches in the Czech Republic and Slovakia, where the countercyclical buffer rates at the end of 2021 were 0.5% and 1.0% (31 December 2020: 0.5% and 1.0%, respectively).

In 2016 the Bank received an administrative decision of the PFSA that identified mBank as other systemically important institutions (O-SII) and imposed a capital buffer of the total risk exposure amount. Pursuant to the PFSA decision of 29 October 2020 the Bank was obliged to maintain the capital buffer of 0.50% of the total risk exposure, calculated in accordance with article 92(3) of the Regulation, to be maintained on individual and consolidated levels. The value of the buffer specified in the administrative decision applies as of 31 December 2021.

Starting from 1 January 2018 the Regulation of the Minister of Development and Finance with regard to systemic risk buffer entered into force. The Regulation introduced systemic risk buffer of 3% of the total risk exposure amount applied to all exposures located in Poland. Due to the exceptional socio-economic situation that arose after the outbreak of the global COVID-19 pandemic, this requirement was lifted by repealing the Regulation of the Minister of Finance, which has been in force since 19 March 2020.

Consequently, the combined buffer requirement set for the mBank as at the end of 2021 amounted to 3.05% of the total risk exposure amount (at the end of 2020: 3.04%).

Additionally, as a result of risk assessment carried out in 2021 by the PFSA within the supervisory review and evaluation process (SREP), in particular with regard to the evaluation of risk related to the portfolio of foreign exchange retail mortgage loans, the Bank received an individual recommendation to maintain own funds on the individual level to cover additional capital requirement of 2.45% for total capital ratio and 1.83% (2020: 3.24% and 2.43%, respectively) for Tier I capital. Additional capital requirement set by PFSA in 2021 encompasses also additional risk factors related to the FX mortgage loan portfolio such as operational risk, market risk or risk of collective default of borrowers.

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During 2021 and 2020 capital ratios on the individual level were above the required values taking into account the abovementioned components.

mBank	31.12.2021		31.12.2020	
Capital ratio	**Required level**	**Reported level**	**Required level**	**Reported level**
Total capital ratio	13.50%	19.01%	14.28%	22.95%
Tier I ratio	10.88%	16.23%	11.47%	19.59%

The stand-alone leverage ratio, calculated in accordance with the provisions of the CRR Regulation and Commission Delegated Regulation (EU) 2015/62 of 10 October 2014, amending Regulation (EU) No 575/2013 of the European Parliament and of the Council with regard to the leverage ratio, including transitional definition of Tier I capital, at the end of 2021 amounted to 6.53% (at the end of 2020: 8.20%).

Own Funds

In accordance with the CRR Regulation, own funds consist of Common Equity Tier I capital, Additional Tier I capital and Tier II capital, however items that could be treated as Additional Tier I capital are not identified within mBank.

Common Equity Tier I capital of mBank contains:

- paid up capital instruments and the related share premium accounts,
- previous years retained earnings,
- independently reviewed interim profits,
- accumulated other comprehensive income,
- other reserves,
- funds for general banking risk,
- items deducted from a Common Equity Tier I capital (fair value gains and losses arising from the institution's own credit risk related to derivative liabilities, value adjustments due to the requirements for prudent valuation, intangible assets, AIRB shortfall of credit risk adjustments to expected losses, own CET1 instruments, regulatory adjustments relating to accumulated other comprehensive income and intangible assets, and net impairment losses).

Tier II capital of mBank contains: capital instruments and the related share premium accounts (subordinated liabilities with specified maturity and excess of provisions over the expected AIRB recognised losses in case of its occurrence).

The own funds of mBank as of 31 December 2021 amounted to PLN 15 849 040 thousand (as of 31 December 2020 it was PLN 17 633 169 thousand). Additionally the Common Equity Tier I capital of mBank as of 31 December 2021 amounted to PLN 13 529 356 thousand (as of 31 December 2020 it was PLN 15 049 829 thousand).

Total risk exposure amount (TREA)

The total risk exposure amount contains:

- risk weighted exposure amounts for credit risk, counterparty credit risk, dilution risk and free deliveries,
- risk exposure amount for market risk, containing position risk, foreign exchange risk and commodities risk,
- risk exposure amount for operational risk,
- risk exposure amount for credit valuation adjustment,
- other risk exposure amounts containing amounts resulted from application of supervisory floor.

As at 31 December 2021 the AIRB approach was applied to the calculation of own funds requirements for credit and counterparty credit risk for the following portfolios:

- mBank corporate portfolio,
- mBank retail mortgage loan portfolio,
- mBank real estate-related specialized lending exposure (IRB slotting approach),
- mBank retail non-mortgage exposures (conditional consent),
- mBank retail microenterprises mortgage loan portfolio (conditional consent),
- bank exposures (conditional consent).

In case of portfolios with conditional consent to the application of AIRB approach, mBank applies supervisory floor, which means that where the own funds requirement for credit risk calculated under AIRB approach is lower than the own funds requirement for credit risk calculated under standardised approach, it is necessary to supplement it up to the level of the own funds requirement for credit risk calculated under standardised approach.

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With regard to retail mortgage exposures (microenterprises) and portfolio of commercial bank exposures, high significance conditions specified by the banking supervision have been met, and the Bank is waiting for formal confirmation by the banking supervision.

In the process of calculating the total standalone capital ratio during 2021, mBank implemented PFSA supervisory restrictions (multipliers) related to the recommendation following the implementation of the New Default Definition and the new LGD model for the retail loan portfolio. These limitations were taken into account in the process of calculating the total risk exposure amount at the end of 2021. In addition, in accordance with the update of the CRR requirements, mBank implemented in 2021 the standard method of calculating exposures for counterparty credit risk.

The total risk exposure amount of mBank as of 31 December 2021 amounted to PLN 83 376 287 thousand (31 December 2020: PLN 76 829 190 thousand), including PLN 73 238 781 thousand of risk-weighted exposure amount for credit risk, counterparty credit risk and supervisory floor (31 December 2020: PLN 67 650 959 thousand).

ICAAP and internal capital

The ICAAP (Internal Capital Adequacy Assessment Process) implemented in mBank aims at adjusting own funds to the level and the profile of risk arising from mBank’s and mBank Group’s operations.

These resources are at safe level. The value of Bank’s internal funds in regulatory approach is substantially higher than value required to cover the total Bank’s capital requirement calculated in line with CRR regulation. Similarly, in the economic approach, the capital resources in a form of own funds or risk coverage potential, are substantially higher that internal capital estimated for Bank in line with Regulation of the Minister of Finance, Funds and Regional Policy of 27 July 2021 on the detailed manner of estimation of internal capital and the bank's review of the strategy and procedures for the estimation and ongoing maintenance of internal capital.

The internal capital of Bank as at 31 December 2021 amounted to PLN 6 206 163 thousand (at 31 December 2020: 6 331 147 thousand).

CAPITAL ADEQUACY	31.12.2021	31.12.2020
Common Equity Tier I Capital	**13 529 356**	**15 049 829**
Total Own Funds	**15 849 040**	**17 633 169**
Risk weighted exposure amounts for credit, counterparty credit, dilution risk and free deliveries:	73 238 781	67 615 425
- under standardised approach	*20 084 295*	*17 460 813*
- under AIRB approach	*53 149 683*	*50 146 497*
- risk exposure amount for contributions to the default fund of a CCP	*4 803*	*8 115*
Total risk exposure amount for position, foreign exchange and commodities risks	1 111 589	881 925
Total risk exposure amount for operational risks	8 656 577	8 052 824
Total risk exposure amount for credit valuation adjustments	369 340	243 482
Other risk exposure amounts	-	35 534
Total risk exposure amount	**83 376 287**	**76 829 190**
Common Equity Tier I capital ratio	**16.23%**	**19.59%**
Total capital ratio	**19.01%**	**22.95%**
Internal capital	**6 206 163**	**6 331 147**

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OWN FUNDS	31.12.2021	31.12.2020
Own funds	**15 849 040**	**17 633 169**
TIER I CAPITAL	**13 529 356**	**15 049 829**
Common Equity Tier I Capital	**13 529 356**	**15 049 829**
Capital instruments eligible as CET1 Capital	3 593 878	3 586 897
Paid up capital instruments	169 474	169 330
Share premium	3 424 404	3 417 567
Retained earnings	883 128	2 051 957
Previous years retained earnings	2 098 481	2 005 433
Profit or loss eligible	(1 215 353)	46 524
Accumulated other comprehensive income	(1 461 025)	420 050
Other reserves	9 250 632	9 246 982
Funds for general banking risk	1 115 143	1 115 143
Adjustments to CET1 due to prudential filters	(71 317)	(57 062)
Fair value gains and losses arising from the institution's own credit risk related to derivative liabilities	(5 472)	(2 496)
(-) Value adjustments due to the requirements for prudent valuation	(65 845)	(54 566)
(-) Intangible assets	(683 698)	(481 264)
(-) Other intangible assets gross amount	(720 387)	(503 931)
Deferred tax liabilities associated to other intangible assets	36 689	22 667
(-) IRB shortfall of credit risk adjustments to expected losses	(60 879)	-
Cash flow hedging instruments adjustments	495 965	(405 680)
CET1 capital elements or deductions - other	467 529	(427 194)
Additional Tier I capital	**-**	**-**
TIER II CAPITAL	**2 319 684**	**2 583 340**
Capital instruments and subordinated loans eligible as T2 capital	2 319 684	2 422 757
AIRB Excess of provisions over expected losses eligible	-	160 583

CREDIT RISK	31.12.2021	31.12.2020
Risk weighted exposure amounts for credit risk, counterparty credit risk, dilution risk and free deliveries	**73 238 781**	**67 615 425**
Standardised approach	**20 084 295**	**17 460 813**
SA exposure classes excluding securitisation positions	20 084 295	17 460 813
Central governments or central banks	1 529 441	573 464
Regional governments or local authorities	15 495	25 942
Public sector entities	6 320	9 280
Institutions	262 190	196 323
Corporates	6 648 536	5 950 546
Retail	2 706 126	2 924 798
Secured by mortgages on immovable property	2 187 885	1 214 778
Exposures in default	207 841	375 174
Items associated with particular high risk	103 368	71 129
Equity	6 401 663	6 052 244
Other items	15 430	67 135
AIRB approach	**53 149 683**	**50 146 497**
AIRB approaches when own estimates of LGD and/or Conversion Factors are used	50 246 503	47 329 005
Institutions	1 218 320	887 040
Corporates - SME	4 542 716	5 965 598
Corporates - Specialised Lending	3 868 520	5 668 264
Corporates - Other	14 034 271	16 841 422
Retail - Secured by real estate SME	1 415 787	1 104 980
Retail - Secured by real estate non-SME	6 786 934	5 186 155
Retail - Other SME	5 593 470	3 131 975
Retail - Other non-SME	12 786 485	8 543 571
Other non-credit obligation assets	2 903 180	2 817 492
Risk exposure amount for contributions to the default fund of a CCP	**4 803**	**8 115**

As of 31 December 2021 mBank included transitional provisions regarding the temporary treatment of unrealized gains and losses measured at fair value through other comprehensive income in connection with the COVID-19 pandemic, contained in the regulation of the European Parliament and of the Council (EU) 2020/873 of 24 June 2020 amending Regulations (EU) No 575/2013 and (EU) 2019/876 as regards certain adjustments in response to the COVID-19 pandemic ("transitional provisions") in the calculation of own funds, capital ratios and leverage ratio for the first time.

The measures reported as of 31 December 2021 calculated taking into account the transitional provisions as well as measures as of 31 December 2021 calculated without taking into account the transitional provisions are presented below.

31 December 2021	Measures reported	Measures calculated without taking into account transitional provisions
Common Equity Tier I capital (PLN thousand)	13 529 356	13 061 828
Tier I capital (PLN thousand)	13 529 356	13 061 828
Own funds (PLN thousand)	15 849 040	15 381 512
Common Equity Tier I ratio (%)	16.23	15.67
Tier I capital ratio (%)	16.23	15.67
Total capital ratio (%)	19.01	18.45
Leverage ratio (%)	6.53	6.32

47. Events after the balance sheet date

On 24 February 2022 Russia invaded Ukraine, therewith starting large scale war activities in Ukraine. The international community reacted with implementation of sanctions against Russia. As of the date of approving of these financial statements it cannot be predicted how the armed conflict as well as the international reaction to it will further develop.

The mBank Group does not have direct operations in Ukraine nor in Russia. The Group's credit exposure towards Ukrainian and Russian institutions, companies and natural persons is not material and as of 31 December 2021 represented 0.031% of the total credit exposure of mBank Group.

These financial statements of mBank for the year 2021 do not require any adjustments due to the above events.

The Bank is closely monitoring the development of the situation related to the armed conflict in Ukraine, as well as is analyzing its potential negative consequences to the overall client portfolio of the Bank. A reliable assessment of the impact on the Bank future operations and an estimate of the impact on the future financial statements of mBank are at this stage not yet possible, as these are highly dependent on the further development of the war in Ukraine, the reaction of international community as well as the impact of those on the Polish economy and the clients of mBank.