



Disclosure regarding capital adequacy of  
**HSBC Bank Polska S.A.**  
**as at 31 December 2016**

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## 1. Introduction

This document implements the Information Policy of HSBC Bank Polska S.A regarding disclosure of qualitative and quantitative information on capital adequacy subject to disclosure, in accordance with Regulation (EU) No 575/2013 of the European Parliament and Council of 26 June 2013 on prudential requirements for credit institutions and investments firms.

Unless otherwise stated, all the data presented in this document are as of 31 December 2016 and provided in PLN thousands, and pertain to stand-alone capital requirements.

The process of calculation of capital requirements as of 31 December 2016 included the data regarding the Bank only – due to lack of subsidiaries it is not necessary to calculate capital requirements based on consolidated balance sheet.

## 2. Risk management objectives and strategies

To a varied degree, all activities of the Bank pertain to risk assessment, evaluation, acceptance and management.

The risk management structure implemented at all levels of the organisation ensures a conservative profile of the Bank's risk aligned with the approved risk appetite and the Bank's strategy.

Based on its Risk Management Framework, the Bank operates a Risk Management System that is formalised, transparent and centralised.

The following chart presents the structure and organisation of the Bank's risk management



**Supervisory Board** of the Bank performs general control over the Bank's risk management and defines its credit activities policy.

The Bank's **Management Board** is responsible for the effectiveness of the Risk Management System, in particular by approving policies and procedures that regulate the management of all significant risk types as identified by the entities responsible for risk management. The Bank's Management Board divides the activities of the Bank thus ensuring independence of the function of measurement, monitoring and control of risk from the operational activity giving rise to that risk.

**Members of the Bank's Management Board** are directly responsible for the management of different types and areas of risk, according to the assigned responsibilities and take part in sessions of committees accountable for management of particular risk types.

**Risk Management Committee and ALCO Committee** bear executive accountability for on-going risk monitoring, evaluation and management, with particular attention paid to risk policy, risk appetite and reviews of significant concentration risks.

**Top executive managers** from particular business lines are responsible for day-to-day risk management activities.

The **Risk Management Committee** is accountable for:

- Setting directions and problem-solving as regards risk policy and risk management;
- Reviewing all significant risks that systematically impact the Bank's activities in order to ensure adequate controls that facilitate effective management of such risks and attainment of returns corresponding to such risks;
- Considering key risk exposures, both current and prospective, in light of the dynamically changing economic and political environment;
- Reviewing information that facilitates identification of specific institutional risks;
- Exercising control and monitoring the management of significant risks;
- Promoting an appropriate risk culture:
  - Demonstrating the ethical code and the values of HSBC Group;
  - Communicating the goals, objectives and responsibilities;
  - Sharing information and knowledge as well as
  - Promoting responsibility and professional competence.

The **ALCO Committee** is accountable for:

- Providing direction and ensuring tactical follow-through to create an evolving balance sheet structure to meet a site's performance objectives within prescribed risk parameters;
- Controlling of the balance sheet structure risks management processes;
- Internal Capital Adequacy Assessment Process;
- Coordinating liquidity and capital risk management process (including stress-testing);
- Reviewing overall sourcing and allocation of funding;
- Forward looking and determining the most likely banking environment for asset/liability forward planning and review contingency scenarios;
- Evaluating alternative rate, pricing and portfolio mix scenarios; reviewing asset/liability distributions and maturities;
- Ensuring that all regulatory requirements are respected.

## **Risk Management process and procedures**

The Bank's risk management is implemented based on the policies and procedures for risk identification, measurement, monitoring and control developed in writing and approved by the Bank's Management Board. These procedures are subject to regular verification so as to align them with the Bank's changing risk profile and the changing economic environment in which the Bank operates.

Identification and measurement of risks resulting from the Bank's commercial activity match the profile, scale and complexity of the risks. The methods (models) applied for risk estimation, with their accompanying assumptions in particular, are subject to periodic internal reviews.

The principles of the Bank's risk management take into account the key risks such as: credit risk and counter-party risk, concentration risk, operational risk, business risk, liquidity risk, compliance risk or market risk such as interest rate or currency exchange risks.

### **Credit risk**

Credit risk is uncertainty pertaining to a customer's failure to meet a contractual obligation to repay a loan i.e. capital and interest within a specified period of time.

The key objective of the Bank's credit policy is to implement a credit risk management framework that makes it possible to maximise the profitability of credit activities, to a degree that corresponds with the required risk level and the quality of the banking book.

Credit Risk Line manages all aspects of credit risk for corporate and retail banking as well as monitoring operational risk across all departments of the Bank.

The Bank's day-to-day risk management process includes the following:

- 1) Assessment of credit exposure against plans and parameters defined in "Risk Appetite" and its principles;
- 2) Building a high level of credit risk awareness among the Bank's employees and among the employees of the Bank's cooperating partners. This is effected through organisation of training courses and implementation of incentive-based remuneration systems oriented to maintain high-quality of credit applications and the generated credit portfolio;
- 3) development and updates of internal processes and procedures in order to meet the planned objectives pertaining to the quality of the credit portfolio;
- 4) monitoring of credit risk at the level of particular credit products offered by the Bank, sector concentration, concentration of large credit exposures and at the level of particular employees who are crucial to the credit process (sales staff and employees who make credit approval/refusal decisions);
- 5) quick response to threats that may lead to uncontrolled credit risk increase as well as on-going management of events that lead to commitment of a prohibited offence or to a suspicion of such an offence;
- 6) application of advanced statistical and expert methods in the credit risk assessment process;
- 7) assessment of credit risk based on the customer's rating and the type of product, its repayment period and information acquired from external sources such as the Loan Information Office (BIK) and investigative consultants;
- 8) periodic assessment of the quality and size of the Bank's credit portfolio, and introduction of possible changes to credit procedures and processes based on assessment results and

changes taking place on the credit market;

- 9) periodic assessment of the effectiveness of verification activities performed prior to loan granting and the effectiveness of debt collection, as well as introduction of possible changes to credit procedures and processes based on assessment results and changes taking place on the credit market.

The Bank applied the standardised approach to credit risk assessment in compliance with the Basel II framework. Every credit application is evaluated individually based on the creditworthiness of the Debtor and the proposed transaction structure (including the recommended collateral) and other risks that accompany the transaction. The expert CRR rating is treated solely as a useful tool for cross-comparison of the prospective Debtor's financial condition.

### **Settlement risk**

Settlement risk occurs when the Bank makes an irrevocable payment on behalf of the customer and the funds to cover the payment have not been credited to the customer's account or the funds on the customer's account may be transferred or paid out prior to debiting the customer's account with the payment amount. Settlement risk disappears when the transaction has been settled in full. If the customer does not settle the transaction, the settlement risk turns into credit risk. While settlement risk products are generally regarded as low risk products, they should be considered in the case of thorough and trustworthy customers.

Settlement risk may be:

- 1) Intra-day: it exists during one working day (including one-day overdrafts);
- 2) Short-term, for example risk associated with the traditional settlement cycle and currency exchange.

### **Market risk**

Market risk is the risk that the value of an asset or liability may change as a result of a change in market rates or prices. The principal market risk factors could be interest rates, foreign exchange rates, credit spreads and equity prices. Bank's main exposure is towards fx risk and interest rate, which was described in section 10 of this Information.

The key objective of market risk management in the Bank is to ensure full awareness and thorough understanding of Bank's market risk exposure and efficient managing of market risk while maintaining a market profile consistent with risk appetite.

Main types of market risk that are recognized in Bank's activities are:

- a. Foreign exchange (FX) risk – taken discretionally in expectation of additional gain due to change in market rates;
- b. Interest rate (IR) risk in trading book – taken discretionally via positions in bonds/bills, IRS or fx derivatives (fx forward, fx swaps);
- c. Market risk component of the IR risk in banking book – partially it's a structural position resulting from offering banking products to customers (loans and advances, customer deposits) actively managed by BSM function.

Measures used in the Bank to quantify and control market risk aim at capturing all of the market risk exposures with respect to Bank's assessment of their materiality.

These measures include:

- a. Nominal values of positions (eg. Fx position);
- b. Present value of a basis point (PVBP);

- c. Value at Risk (VaR);
- d. Other measures used for the purpose of measuring the interest rate risk in the banking book.

In line with its statutory role Bank's Supervisory Board is responsible for alignment of market risk management policy to approved Bank's strategy and its supervision based on periodic information received from Bank's Management Board.

Bank's Risk Management Committee approves Bank's risk appetite for market risk in a formal RAS and monitors alignment of Bank's market risk exposure/profile with the Bank's risk appetite statement.

Management Board is responsible for ensuring an effective risk management system through regular update of Policy as well as more detailed Instructions that define processes and responsibilities for measuring, monitoring and reporting of market risk as well as ensuring their compliance with the Bank's strategy.

Overall responsibility for market risk management is delegated to ALCO.

### **Concentration risk**

Credit risk concentration occurs when a number of counterparties or engagements have comparable economic features or when such counterparties are engaged in similar types of activities or are active in the same geographical areas or industries. Consequently, any changes in economic, political environment and other factors influence these parties' combined contractual capacity in an identical way and risks associated with one counter party or a concentrated group of counter parties constitute a significant part of the portfolio.

The Bank applies a range of control mechanisms in order to limit excessive concentration of engagements in the Bank's portfolio in particular sectors, countries and customer groups. These mechanisms include portfolio thresholds, counterparty thresholds, approval and review controls as well as stress tests.

Concentration risk management is coordinated by the Risk Management Line. The Bank focuses on concentration risk generated mostly by large, individual credit engagements. The Bank calculates capital requirements resulting from concentration risk of large credit risk exposures and selected sectors of economy:

- The mechanism activating engagement in large entities is linked to overall credit facility and constitutes 10% of capital;
- Engagement in large sectors (defined as over 30% of the Corporate Banking Portfolio) pertains to selected sectors.

### **Liquidity risk**

Liquidity risk means a risk of a failure to meet obligations as they come due or loss of ability to fund increases in assets, both in the course of daily banking operations and in other expected conditions causing necessity to suffer unacceptable losses.

The Bank continues the policy of ensuring a strong and stable management of liquidity position of assets, liability and off-balance commitments in a manner that ensures balancing cashflows, taking into account diverse stress scenarios, in a manner that ensures repayment of potential debt at the moment of its due date.

Liquidity risk at the operational level is managed by the Bank's Global Markets Line; the Line also takes into account information from the Finance Line regarding the expected cashflows and proximity to the thresholds approved by the Bank's Management Board.

The process of liquidity risk management is supervised by the Assets & Liability Management Committee.

The Bank manages the risk by assessing a number of metrics and by setting appropriate internal and regulatory thresholds.

### **Operational risk**

Operational risk is defined as the risk of loss resulting from inadequate or failed internal processes, people and systems or from external events, including legal risk. Legal risk includes, but is not limited to, exposure to fines, penalties, or punitive damages resulting from supervisory actions, as well as private settlements.

The operational risk management strategy is to have in place accurate and robust framework which provides an effective and efficient approach to govern and oversee the organisation and monitor and mitigate operational risk in order to deliver HBPL strategy. The Operational Risk Management Framework is to ensure that the bank manages its operational risk in cost effective manner, with targeted levels of operational risk consistent with bank's risk appetite.

The Bank perceives the areas below as the key sources of operational risk:

- system failure – the Bank applies a significant number of systems to support its customer offer,
- human error / process error – historic operational risk events prove that some operational processes are still imperfect or fail due to human error,
- internal fraud – despite our expectation that internal fraud events (historically linked to retail activities) will decrease in quantity and volume, the Bank may still expect such risk events to materialise.
- outsourcing risks – the extent of outsourcing is assessed by the Bank as significant and, consequently, risk events are expected to materialise in this area.

The Bank monitors and controls operational risk profile for all areas of activity based on the results of risk assessment with Key Risk Indicators, Risk Assessment and Control, explanation of loss-generating incidents and root cause analysis of such incidents.

The Bank's operational risk is managed by the designated department – Operational Risk and Internal Control Department (ORIC) which is responsible for the end to end oversight and verification of the appropriateness of operational risk management within the Businesses/Functions, including key control monitoring activity. On a monthly basis ORIC also reports any operational risk and internal control weaknesses to RMC.

On periodical basis ORIC presents Supervisory Board with information on effectiveness of Operational Risk and Internal Control framework. On-going operational risk management is the accountability of the Bank's management at all organizational levels, with oversight executed by the relevant Business Risk Control Managers (*BRCM*).

Executive oversight of operational risk and internal control management is provided by the Risk Management Committee (RMC). The Committee formally holds a monthly meeting and, among other responsibilities, is accountable for promoting risk awareness and proactive management of operational risk by communicating the HSBC Group's operational risk and controls management framework, and overseeing translation into local policies and procedures.

After risk identification, the next step is assessment of its impact on the Bank. This takes into account two aspects of risk: absolute level of risk and risk exposure.

This methodology facilitates documentation of Key Risk profiles discussed during sessions of Risk Management Committee. Subsequently, Risk and Control Assessment is prepared in order to mitigate the identified risk.

Operational risk and loss-generating event registration and reporting are performed in a dedicated IT system. All losses are thoroughly explained so as to define their causes and prevent re-occurrence.

Moreover, the Bank operates a counter-fraud system. The system centralises the prevention, detection and analysis tasks for the Information Security Management and Bank Fraud Risk Department. The assumption behind the system's operation is also that there will be close cooperation among the Bank's branches i.e. exchange of information that may become useful for elimination of events with fraud characteristics, as well as close cooperation with the local judicial authorities. Additionally, through the Department's activities the Bank implements its information security and business continuity risk policy and strategy. Both areas demand strict procedures and control tools, regular process reviews and awareness-building among the Bank's employees.

### **Business risk**

Business risk is a potential adverse impact on profit and capital resulting from the Bank not meeting its strategic goals as specified in its annual operational plan (ROP), due to unexpected changes in the business and regulatory environments, exposure to economic cycles and technological change.

The Bank manages and limits this risk by planning its activity and performing stress tests in order to ensure that the Bank's business model and its planned activities are secured by appropriate resources (capital resources in particular) in the commercial, economic and risk environment. The aim of business risk management is to ensure that potential exposure of the Bank's business plans to risk is identified at an early stage so that proactive limiting action can be taken.

Business risk is primarily managed by business lines Directors. The Bank's Board is accountable for oversight of the process. ALCO is also responsible for risk monitoring to the extent in which the risk negatively impacts the assets/liabilities structure.

### **Compliance risk**

Compliance risk is defined as potential negative consequences of lack of compliance of the Bank's activity with the binding legal regulations, internal regulations and the approved code of conduct. The Bank manages compliance risk through a clear structure of its organisational processes, specified and defined in separate internal regulations. The impact of negative compliance risk events is covered by Tier 2 capital cushion.

## **3. Information regarding own funds**

The Bank's own funds are composed of the following elements:

- 1)** Common Equity Tier 1 including capital instruments and share premium, retained earnings, accumulated other income, other supplementary capital, general banking risk funds;

- 2) Additional Tier 1 capital including equity instruments as specified in Art. 52 of Regulation 575/2013 and the associated share premium;
- 3) Tier 2 capital including equity instruments and subordinated debt.

All listed capitals are subject to adjustments due to deductions and applicable prudential supervision filters.

As of 31 December 2016 the Bank's own funds consist of Common Equity Tier 1 capital only. Detailed information on the particular elements of the Bank's own funds as of 31 December 2016 are presented in the table below (in accordance with Regulation No 1423/2013, Appendix 6).

Common Equity Tier 1 capital: instruments and reserves		Amount at disclosure date PLN'k
1	Capital instruments and the related share premium accounts	481 658
2	Retained earnings	0
3	Accumulated other comprehensive income	-747
4	Funds for general banking risk	0
5	<b>Common Equity Tier 1 capital before regulatory adjustments</b>	480 912
Common Equity Tier 1 capital: regulatory adjustments		
1	Intangible assets	-4 103
2	Regulatory adjustments relating to unrealized gains and losses pursuant to Article 467 and 468	-268
2a	of which: filter for unrealized loss	-268
2b	of which: filter for unrealized gain	0
3	<b>Total regulatory adjustments to Common equity Tier 1</b>	-12 493
4	<b>Common Equity Tier 1 capital</b>	468 418
Additional Tier 1 capital: instruments		0
Additional Tier 1 capital before regulatory adjustments		0
Tier 2 capital: instruments and provisions		
1	<b>Total regulatory adjustments to Tier 2 capital</b>	0
2	<b>Tier 2 capital</b>	0
3	<b>Total capital</b>	468 418
4	<b>Total risk weighted assets</b>	2 972 946
Capital ratios and buffers		
1	Common Equity Tier 1 (as a percentage of risk exposure amount)	15,76
2	Tier 1 ( as a percentage of risk exposure amount)	15,76
3	Total capital (as a percentage of risk exposure amount)	15,76

4	Institution specific buffer requirement ( CET1 requirement in accordance with article 92 (1)(a) plus capital conservation and countercyclical buffer requirements, plus systemic risk buffer, plus the systemically important institution buffer, expressed as a percentage of risk exposure amount)	5,75
4a	of which: capital conservation buffer requirement	1,25
4b	of which: countercyclical buffer requirement	0
4c	of which: systemic risk buffer requirement	0
4d	of which: Global Systemically Important Institution or Other Systemically Important Institution buffer	0

### **Capital instruments and related share premium**

Capital instruments and related share premium include paid up capital instruments, share premium and other supplementary capital as at 31 December 2016.

<b>Capital instruments and the related share premium accounts</b>	<b>PLN'k</b>
Paid up capital instruments	393 207
Share premium	19 149
Other supplementary capital	69 302
<b>Total</b>	<b>481 658</b>

HSBC Bank Polska S.A.'s equity instruments are formed by the Bank's share capital amounting to PLN 393 207 million.

As at 31 December 2016, the shareholder of 100% of shares is HSBC Bank Plc.

The key features of the capital instruments are presented in the table below.

<b>Capital instruments main features template</b>		
1	Issuer	HSBC Bank Polska SA
2	Unique identifier	Not applicable
3	Governing law of the instrument	Polish
	<i>Regulatory treatment</i>	-
4	Transitional CRR rules	Common Equity Tier 1
5	Post-transitional CRR rules	Common Equity Tier 1
6	Eligible at solo/(sub-)consolidated/ solo& (sub-)consolidated	Eligible at solo
7	Instrument type	share (series A-I, L-Z), Art. 28 CRR preference share with priority on voting rights (series J i K), Art. 28 CRR

8	Amount recognised in regulatory capital (currency in million, as of most recent reporting date)	series A 50 000,00 series B 600 000,00 series C 380 000,00 series D 25 000,00 series E 7 945 000,00 series F 6 000 000,00 series G 4 000 000,00 series H 5 000 000,00 series I 6 100 000,00 series J 6 300 000,00 series K 10 000 000,00 series L 12 000 000,00 series M 10 000 000,00 series N 15 000 000,00 series O 30 000 000,00 series P 14 000 000,00 series R 10 807 000,00 series T 110 000 000,00 series U 25 000 000,00 series W 100 000 000,00 series Z 20 000 000,00
9	Nominal amount of instrument	1,00 PLN
9a	Issue price	Depending on the series
9b	Redemption price	Not applicable
10	Accounting classification	Equity
11	Original maturity date	series A 16.03.1990 series B 31.05.1991 series C 31.05.1991 series D 20.02.1992 series E 14.01.1994 series F 06.10.1997 series G 30.12.1997 series H 22.07.1998 series I 22.07.1998 series J 11.05.1999 series K 28.12.1999 series L 27.10.2000 series M 11.01.2001 series N 25.09.2001 series O 23.01.2003 series P 18.02.2004 series R 29.10.2004 series T 16.05.2006 series U 10.07.2009 series W 23.06.2010 series Z 31.05.2012
12	Perpetual or dated	Not applicable
13	Original date of issuance	Not applicable
14	Issuer call subject to prior supervisory approval	Not applicable
15	Optional call date, contingent call dates and redemption amount	Not applicable
16	Subsequent call dates, if applicable	Not applicable
	<i>Coupon/ dividends</i>	Not applicable
17	Fixed or floating dividend/coupon	Not applicable
18	Coupon rate and any related index	Not applicable

19	Existence of dividend stopper	Not applicable
20a	Fully discretionary, partially discretionary or mandatory (in terms of timing)	Not applicable
20b	Fully discretionary, partially discretionary or mandatory (in terms of amount)	Not applicable
21	Existence of step up or other incentive to redeem	Not applicable
22	Noncumulative or cumulative	Not applicable
23	Convertible or non-convertible	Not applicable
24	If convertible, conversion trigger(s)	Not applicable
25	If convertible, fully or partially	Not applicable
26	If convertible, conversion rate	Not applicable
27	If convertible, mandatory or optional conversion	Not applicable
28	If convertible, specify instrument type convertible into	Not applicable
29	If convertible, specify issuer of instrument it converts into	Not applicable
30	Write-down features	Not applicable
31	If write-down, write-down trigger(s)	Not applicable
32	If write-down, full or partial	Not applicable
33	If write-down, permanent or temporary	Not applicable
34	If temporary write-down, description of write-up mechanism	Not applicable
35	Position in subordination hierarchy in liquidation (specify instrument type immediately senior to instrument)	Not applicable
36	Non-compliant transitioned features	Not applicable
37	If yes, specify non-compliant features	Not applicable

### **Share premium**

Share premium is the excess amount over the par value remaining after issue costs are covered minus the loss amount covered from the Bank's reserve fund; share premium is used to cover possible operational losses.

### **Other supplementary capital**

Other supplementary capital is created from retained earnings, based on the principles set out in the Articles of Association.

### **Accumulated other comprehensive income**

Accumulated other comprehensive income presents unrealised gain and loss on debt and equity instruments classified as available for sale i.e. government bonds and money bills held in the Bank's portfolio.

The table below presents the structure of accumulated other income as of 31 December 2016.

Unrealised gains and losses	PLN'k
Unrealised gain	670
Unrealised loss	-1 417
Total	-747

## ADJUSTMENTS

### Intangible assets

Pursuant to Art. 37 of CRR Regulation, intangible assets are reducing Tier 1 capital amount. As at 31 December 2016, the amount of intangible assets was PLN 4 103 thousand.

### Regulatory adjustments of unrealised gain and loss

Unrealised gain and loss on debt and equity instruments available for sale are presented in own funds in accordance with the guidelines set out in Regulation (EU) No 575/2013 of the European Parliament and Council of 26 June 2013 and the guidelines from the Polish Financial Supervision Authority i.e.:

- 60% of unrealised gains is removed from own funds,
- 100% of unrealised loss is removed from own funds.

Adjustments amounted to PLN 268 thousand.

The Bank follows a prudential approach and assumes that the short-term capital is zero.

## 4. Information regarding compliance with capital requirements

Internal capital is the amount of the capital estimated by the Bank as necessary to cover all the identified significant risks arising from the banking activity.

The Bank adjusts the size of the stand-alone and consolidated own funds to the level and the type of the risk to which it is exposed, and the nature, scale and complexity of its operations. To this end, the Bank has developed and implemented the Internal Capital Adequacy Assessment Process (ICAAP) which serves to maintain own funds at the level appropriate to the profile and risk level of Bank operations.

Due to the fact that the effect of risk diversification was not taken into account in 2015, the Bank's internal capital was estimated at the level higher than the sum of capital requirements for different types of risks included in Pillar I. Additional values of the internal capital are estimated for:

- interest rate risk in the banking book;
- risk of large exposures and selected sectors of the economy;
- other significant risks.

In total, as of the end of 2016, the value of the internal capital amounted to PLN 245 208 thousand.

The Bank calculates total risk exposure resulting from the following categories of risk:

1. credit risk– the standard method;
2. operational risk – standardised method;
3. market risk;
  - a) general interest rate risk — calculated with the use of the maturity ladder approach;
  - b) foreign exchange risk – the basic approach;
4. large exposures over the threshold for large exposures;
5. CVA (Credit Valuation Adjustment) – the standard approach
6. settlement risk, delivery risk and late delivery risk — calculated with the use of the market valuation approach.

#### REGULATORY CAPITAL REQUIREMENTS STRUCTURE AS OF 31 DEC 2016

Regulatory capital requirements (%)	PLN'k
1. Credit risk and counterparty credit risk	212 899
2. Market risk	837
- position risk	837
- commodities risk	0
3. Foreign-exchange risk	0
4. Settlement risk	0
5. Operational risk	23 455
6. Credit Valuation Adjustment risk	644
Total capital requirements	237 836
Total capital	468 418
Total capital ratio	15,8

#### CAPITAL REQUIREMENT FOR CREDIT AND COUNTERPARTY RISK DIVIDED INTO EXPOSURE CLASSES AS OF 31 DEC 2016

Capital requirement for credit and counterparty risk	PLN'k
Exposure to central governments or central banks	0
Exposure to institutions	7 621
Exposures to corporates	159 001
Exposures secured by mortgages on immovable property	36 967
Exposure in default	7 904
Other items	1 406
TOTAL	212 899

Capital requirement for counterparty risk (presented in the total credit risk capital requirement) amounted to PLN 4 407 thousand as of 31 December 2016.

## 5. Exposure to credit risk

The Bank classifies receivables as doubtful and non-performing when it meets one of the two criteria:

- the debt repayment is late by more than 90 days;
- despite no delay in debt repayment or a delay of fewer than 90 days – analysis of the debtor indicates that the debt is unlikely to be paid in full amount; without execution of security.

The value of exposure in the tables below is to be understood as the value estimated in accordance with the guidelines set out in CRR Regulation for capital adequacy: balance sheet value (based on the Polish Accounting Standards) and the value of the balance sheet equivalent of contingent liabilities and off-balance transactions (estimated using the market valuation approach).

### GEOGRAPHICAL STRUCTURE OF EXPOSURE BY COUNTRY AS OF 31 DEC 2016

Exposure by country	PLN'k
Poland	5 501 616
UK	342 812
Other countries	227 826
<b>Total</b>	<b>6 072 254</b>

### TOTAL AND AVERAGE EXPOSURE AMOUNT FOR CREDIT AND COUNTERPARTY RISK BY EXPOSURE CATEGORIES

Counterparty type	Exposure classes	Exposure amount PLN'k	Average amount PLN'k
Central governments and central banks	Exposure to central governments or central banks	2 433 875	2 357 469
Institutions	Exposure to institutions	355 776	214 361
Corporates	Exposures to corporates	2 655 405	2 625 056
	Exposures secured by mortgages on immovable property	484 288	519 251
	Exposure in default	72 682	51 383
Retail	Exposures secured by mortgages on immovable property	16 542	17 044
	Exposure in default	-	-
Other	Other items	53 686	49 674
<b>Total</b>		<b>6 072 254</b>	<b>5 834 237</b>

\*Average exposure amounts have been calculated as arithmetic mean of the value of exposure on the last day of each calendar quarter.

### THE STRUCTURE OF EXPOSURES PER MATURITY, DIVIDED INTO CLASSES OF EXPOSURE

Exposure classes	Maturity ( years)						
	< 1		1-5		> 5		Total
	PLN'k	%	PLN'k	%	PLN'k	%	PLN'k
Exposure to central governments or central banks	1 691 569	69,50	742 306	30,50	-	0,00	2 433 875
Exposure to institutions	268 764	75,54	87 012	24,46	-	0,00	355 776
Exposures to corporates	1 152 298	43,39	1 331 268	50,13	171 839	6,47	2 655 405
Exposures secured by mortgages on immovable property	325 557	65,00	150 864	30,12	24 409	4,87	500 830
Exposure in default	2 377	3,27	52 900	72,78	17 405	23,95	72 682
Other items	-	0,00	53 686	100,00	-	0,00	53 686
<b>Total</b>	<b>3 440 565</b>	<b>56,66</b>	<b>2 418 036</b>	<b>39,82</b>	<b>213 653</b>	<b>3,52</b>	<b>6 072 254</b>

As of 31 December 2016 the Bank's exposure with recognised loss against Polish enterprises amounting to PLN 191 466 thousand. The table below presents the details of the reserve activities.

Provisions, opening balance	71 294
Created	14 661
Release	-15 036
Other adjustments	-29 204
Provisions, closing balance	41 715

### **Information concerning credit risk mitigation techniques**

According to approved policy, the Bank applies the simple method to reduce its credit risk by the way of replacing a counterparty risk weight with the weight of the risk of an instrument that fully or partially secures the credit exposure, according to appropriate regulations of Polish Financial Supervision Authority.

In the case of the simple method, banks' assets that are secured are assigned with an adequate risk weight for issuer/provider of security - funded and unfunded protection.

Under simple method partial collateralisation of credit exposure is acceptable in that case the unsecured part of receivables shall be assigned with a risk weight adequate to the debtor. However no settlement term mismatching is allowed.

Funded credit risk protection exists when the Bank has right for liquidation transfer or take-over or holding the asset or cash kept as security for credit transaction.

Unfunded protection takes place when reduction of Bank's credit exposure is a result of the third party obligation to repay the outstanding amounts. Unfunded protection techniques include:

- guarantees and counter-guarantees

- credit derivatives
- other types of credit risk protection (including insurances). Mortgage is not accounted for credit risk mitigant in standardized method, as already that type of security is taken into account in separate segment of credit exposure (secured by mortgages).

### **Information on the use of external creditworthiness rating**

The Bank uses external ratings by Moody's, S&P and Fitch Group in order to assess creditworthiness in the case of the following exposure categories:

- governments and central banks;
- institutions;
- corporates;
- securitisation positions;
- short-term claims against institutions and entrepreneurs;
- regional governments and local authorities;
- multilateral development banks.

## **6. Information on counterparty credit risk**

Counterparty's credit risk requirement is calculated with the use of the market valuation approach.

The Bank applies different counterparty risk collateral for the parties with whom the Banks enters into derivative transactions. The most frequently applied types of collateral are security deposits, blockades of settlement accounts or blockades of term deposits.

In case of thresholds on treasury transactions the Bank, as part of its credit decision, individually defines the amount of negative engagement acceptable for the customer (MtM) and the minimum transfer amount (MTA) based on the Bank's expertise, the customer's standing and the demand for FX risk hedging. Exceeding MtM / MTA thresholds in current valuations means it is necessary to implement a security deposit in the required amount.

As of end of 2016 the impact of collateral was immaterial from the perspective of the total capital requirement.

## **7. Information regarding operational risk**

HSBC Bank Polska S.A. applies the standardised approach to the calculation of capital requirements related to operational risk.

When applying this approach the Bank divides its operations into following business lines:

- brokerage,
- commercial banking,
- retail banking,

Key assumptions:

1. The Bank calculates the capital requirement related to operational risk based on its annual result.
2. The Bank's assumption is that the level of capital requirement remains unchanged throughout the financial year unless there are corrections to the report in the period of time preceding final approval of financial statement.

Capital requirement for operational risk amounted to PLN 23 454 thousands as of 31 December 2016.

Complete information on the amount of gross losses resulting from operational risk in 2016 divided by event categories and types is presented below:

Event Type Category I	Event Type Category II	Gross Loss (kPLN)	Mitigation Activities
Employment Practices and Workplace Safety	Employee Relations	394	Process improvement
Clients, Products & Business Practices	Product flaws	279	Product construction was updated.
Business disruption and system failures	Systems	0,07	Root causes analysis and system amendments implementation.
Execution, Delivery & Process Management	Transaction Capture, Execution & Maintenance	87	Procedures and processes improvements including control scope development.

## 8. Information regarding liquidity risk

Liquidity risk means a risk of a failure to meet obligations as they come due or loss of ability to fund increases in assets, both in the course of daily banking operations and in other expected conditions causing necessity to suffer unacceptable losses.

Liquidity risk management at the Bank is aimed at keeping a cushion of liquid assets allowing to ensure the ability to generate liquidity on appropriate dates and at optimum cost, and ensure a stable and adequately diversified funding base enabling sustainable development specified in strategic plans, while maintaining resilience to unexpected increases in funding needs.

In liquidity risk management, the Bank follows, in particular, the provisions of Capital Requirement Regulation (CRR), Commission Delegated Regulation (EU) 2015/61, LCR and NSFR (supervisory ratios), Resolution No 386/2008 of the Polish Financial Supervisory Authority, EBA and Basel Committee Guidelines and Recommendations of the Polish Financial Supervisory Authority.

The Management Board of the Bank assigns ALCO the executive responsibility for the ongoing risk monitoring, assessment and management and the effectiveness of liquidity and funding risk policies.

In order to effectively manage liquidity risk, ALCO delegates ongoing monitoring, daily reporting and operational management on specialised units: ALCM and BSM roles with the support of other organizational units, bearing in mind that strategic decisions on structural liquidity and funding remain collective responsibility of ALCO.

In the view of the Bank, the liquidity surplus is based only on unblocked debt securities. Furthermore, in order to reflect the actual amount of treasury bonds, the Bank applies haircuts compliant with the level accepted by the National Bank of Poland.

As at 31 December 2016, the liquidity surplus (PLN 2 334 752 k) comprised the following:

- cash (PLN 36 111 k);

- high quality treasury bonds and Central Bank bills (PLN 2 300 641 k).

The main source of funding of Bank's operations is the base of term liabilities and funds in the accounts of current corporate customers. Furthermore, the Bank obtained a long-term funding from intragroup entities, and in the event of stress scenarios, the Bank holds a stand-by line granted by the parent company.

As a part of the liquidity risk management, the Bank identifies, in particular, the most significant kinds of exposures to liquidity risks, and also develops a set of scenarios for the conducted stress tests (detailed monitoring of survival horizon in specific stress test scenarios allows to adequately adjust the contingency funding plan adopted by the Bank).

Furthermore the Bank monitors several early warning indicators in order to appropriately form the structure of balance sheet and liquidity surplus, not only in the context of adopted development plans (where liquidity premium is a significant element of the internal transfer pricing policy), but also in order to ensure resilience of the Bank to stress events.

### **Level of supervisory liquidity ratios and measures as at 31 December 2016**

**-M1: 1 194 887 kPLN**

**-M2: 168%**

**-M3: 2240%**

**-M4: 182%**

**-LCR: 151%**

### **Risk Assessment**

The ability of the Bank to meet its obligations both in short, medium and long terms is adequately secured by the portfolio of highly liquid assets (HQLA) held by the Bank. In the short term, the basic liquidity surplus may secure liquidity position also in the event of most stress tests considered by the Bank.

On the basis of stress test results, the Bank identified the main risk for the liquidity position as the outflow of corporate deposits accompanied by stress factors affecting the European banking system. The Bank is able to create an appropriate liquidity position in this scenario, however it will translate to a decrease in the net interest income.

In non-stress conditions the bank does not anticipate any threats to the net profit and own funds. Furthermore the Bank was provided with a currency funding on favourable conditions for the next 3 years.

The deposit base, comprised in half of core deposits in current accounts, enables a significant increase in credit portfolio. Long-term funding obtained from the parent company ensures the stability of balance sheet structure in foreign currencies.

## **9. Capital buffers**

As at end of 2016 Bank was obliged to keep the following additional capital buffers: conservation buffer and countercyclical buffer.

As at 31 December 2016 conservation capital buffer amounted to 1.25% of total risk exposure. Conservation capital buffer (mandatory for all banks) will be gradually increased in Poland to the target level of 2.5% in 2019.

Countercyclical capital buffer is set in order to reduce the systemic risk coming from the credit cycle. Bank calculates countercyclical buffer ratio using the levels set by competent authority in each country in which it has exposures.

Since 1st January 2016 countercyclical capital buffer is set at 0% for exposures in Poland. The level of the buffer is subject to change by the decision of the Ministry of Finance.

Bank calculates institution-specific countercyclical capital buffer based on exposure values in other countries and countercyclical capital buffer levels in a respective country.

As at 31 December 2016 institution specific countercyclical capital buffer rate for the Bank was at 0,003%.

### **Amount of institution-specific countercyclical capital buffer as at 31 December 2016**

		in kPLN
010	Total risk exposure amount	2 972 946
020	Institution specific countercyclical capital buffer rate (in %)	0,003
030	Institution specific countercyclical capital buffer requirement	93

### **Geographical distribution of credit exposures relevant for the calculation of the countercyclical capital buffer as at 31 December 2016**

2016								
		General credit exposures	Trading book exposures	Own funds requirements			Own funds requirements weights	Countercyclical capital buffer rate (in %)
		Exposure value for SA	Sum of long and short positions of trading book exposures for SA	of which: General credit exposures	of which: Trading book exposures	Total		
		010	030	070	080	100		
010	Breakdown by country:							
1	Polska	2 576 268	0	195 171	0	195 171	95,08	0
2	Wielka Brytania	87 087	0	5 906	0	5 906	2,88	0
3	Chiny	13 352	0	1 063	0	1 063	0,52	0
4	Stany Zjednoczone	11 018	0	756	0	756	0,37	0
5	Rosja	9 695	0	776	0	776	0,38	0
6	Włochy	9 000	0	144	0	144	0,07	0
7	Czechy	8 877	0	142	0	142	0,07	0
8	Kanada	4 537	0	73	0	73	0,04	0
9	Zjednoczone Emiraty Arabskie	4 271	0	68	0	68	0,03	0
10	Norwegia	4 171	0	334	0	334	0,16	1.50000

11	Japonia	3 200	0	51	0	51	0,02	0
12	Kuwejt	3 123	0	250	0	250	0,12	0
13	Francja	2 982	0	172	0	172	0,08	0
14	Szwajcaria	2 950	0	47	0	47	0,02	0
15	Hongkong	2 795	0	224	0	224	0,11	0.62500
16	Filipiny	2 185	0	35	0	35	0,02	0
17	Niemcy	1 117	0	52	0	52	0,03	0
18	Holandia	475	0	8	0	8	0,00	0
19	Australia	162	0	6	0	6	0,00	0
20	Republika Południowej Afryki	50	0	1	0	1	0,00	0
020	Ogółem	2 747 316	0	205 278	0	205 278	100	

As at 31 December 2016 systemic risk buffer in Poland was at 0%.

## 10. Information regarding interest rate risk in the banking book

Interest rate risk in the banking book is defined as the risk of loss arising from adverse changes in interest rates, which lead to a decrease in interest income, an increase in interest costs or reduce the net present value of positions sensitive to changes in interest rates (also hedging these positions). Interest rate risk arising from non-trading activity may come from the following sources:

- mismatch changes in interest rates of assets, liabilities and off balance sheet items (re-pricing risk);
- changes in the relationship between the yield curves that affect the determination of the interest rate instruments in the portfolio of the bank and cause changes in the relationship between interest rates on these instruments (basis risk);
- changing the relationship between interest rates for different maturities / maturity of the yield curve (yield curve risk);
- options related to the interest rate contained in banking products, for example prepayment option (option risk).

Interest rate risk in the banking book is measured:

- Using Present Value of Basis Point (PVBP);
- Value at Risk (VaR);
- Analysis of contractual gaps;
- Analysis of behavioural gaps;
- Simulations of net interest income (NII) with a minimum of the following scenarios:
  - +/- 50, +/- 100, +/- 200 basis points, sudden change,
  - +/-100, +/- 200 basis points, gradual change,
  - projected interest rate changes,
- Sensitivity of economic value assuming a sudden and unexpected change in interest rate by +/-200 basis points.

## 11. Information regarding exposures in equities included in the banking book

In 2015 the Bank did not hold any equities in the banking book.

## 12. Information regarding financial leverage

The table below presents the total exposure used to calculate the leverage ratio and its value as at 31 December 2016:

<b>Exposure</b>	in kPLN
Total exposure – fully loaded	5 615 761
Total exposure – transitional	5 625 178
<b>Capital</b>	
Tier I – fully loaded	468 686
Tier I – transitional	468 418
<b>Leverage ratio</b>	
Leverage ratio – fully loaded	8,35
Leverage ratio – transitional	8,33

### Split-up of on balance sheet exposures (excluding derivatives, SFTs and exempted exposures) as at 31 December 2016

<b>Total on-balance sheet exposures</b>	<b>5 028 650</b>
Trading book exposures	0
Banking book exposures, of which:	<b>5 028 650</b>
Exposures treated as sovereigns	2 433 875
Institutions	305 315
Secured by mortgages of immovable properties	462 520
Corporate	1 656 611
Exposures in default	116 643
Other exposures	53 686

In order to immunise the Bank against unexpected negative changes in the economy, the Bank defines its acceptable leverage ratio level, and its value is taken into account by the Bank's Assets & Liability Management Committee when analysing the structure and potential future demand for capital.

### Risk of excessive leverage

Risk of excessive leverage is defined as the risk resulting from Bank's vulnerability due to leverage or contingent leverage that may require unintended corrective measures to its business plan, including distressed selling of assets which might result in losses or in valuation adjustments to its remaining assets.

Risk of excessive leverage is monitored by calculating and analyzing leverage ratio measure Excessive leverage risk is managed and controlled by the Risk Management Committee and ALCO Committee.

### **13. Information regarding remuneration policy**

The Bank defines the following positions as managerial positions as stipulated by Resolution No 258/2011 of the Polish Financial Supervision Authority of 4 October 2011:

- Members of the Management Board;
- Head of the Global Markets;
- Head of the Commercial and Global Banking;
- Head of the Technology and Services;
- Chief Risk Officer;
- Head of the Finance;
- Head of Legal & Regulatory;
- Head of Internal Audit;
- Head of Regulatory Compliance;
- Head of Financial Crime Compliance;
- Head of Human Resources.

The Bank also established the principles for determining allocation and payment of the variable pay of employees having a material impact on the risk profile of the Bank. The criteria according to which the Bank determines whether the employee has a significant impact on the risk profile of the Bank, are included in the current Policy.

Variable pay shall be determined and granted on a discretionary basis for the given Evaluation Periods and on the basis of Balanced Scorecards for the respective evaluation periods.

In the case of persons being concurrently a Members of the Management Board, the decisions pertaining to the variable pay is at the discretion of the Bank's Supervisory Board, while in the case of the persons holding managerial positions or have a significant impact on the risk profile of the Bank, the decisions pertaining to the variable pay are at the discretion of the Members of the Board within supervised organizational units.

Variable pay for the persons holding managerial position or having a significant impact on risk profile is composed of:

- 1.** cash benefit – constituting 50% of the value of the variable pay;
- 2.** non-cash instrument – constituting 50% of the value of the variable pay.

The non-cash instrument is an instrument created for the purpose of the implementation of this Policy and shall correspond to the shares in such respect that its value shall change with the change of Indicators calculated for the subsequent financial years.

The non-cash instrument, after calculating its value based on variable Indicators, is paid out in monetary form.

The Bank has established the following metrics measures as the Indicators:

- Profit Before Tax (PBT);
- Cost Income Ratio (C/I);

- Return on Risk Weighted Assets (RORWA).

The value of the indicators shall be calculated based on audited financial statements for the subsequent financial years.

After a given Evaluation Period the Bank defines the value of the Indicators as of the last day of the Evaluation Period.

Prior to payment of the value of the non-cash Instrument the Bank does the following:

- 1) establishes the value of Indicators as of the end of the last financial year;
- 2) establishes the percentage of change for each Indicator;
- 3) calculates the arithmetic mean of the change (in percentage) for each Indicators;
- 4) calculates the value of the non-cash instrument by adjusting its value by the calculated arithmetic mean of change in Indicators.

Apart from the quantitative criteria determining the value of non-cash instrument, the Bank also applies quality criteria. In particular, the award of variable pay components is conditional and is subject to non-detection of events taking place after the Evaluation Period, which are:

- classified as High Risk in the Internal or Global Audit Reports, Compliance reports, ORIC reports relating to the supervised area;
- taking decision resulting in imposition of administrative and legal sanctions;
- taking decision or action that is inconsistent with internal procedures of the Bank or negatively and significantly affecting the Bank's risk profile or being recognized as unacceptable as per the Group Values & Behavior's standards.

In 2016 total sum of remuneration in the Bank were as below:

Remuneration costs in 2015	PLN'k
Global Markets Line	5 688,11
Commercial Banking and Global Banking Line	21 106,59
Risk Line	2 747,95
Finance Line	3 280,26
Support (HTS) Line	7 701,29
Human Resources Line	1 577,61
Legal Line	2 400,81
Others	1 556,38
Management Board	3 645,77
HSBC Bank Polska SA	<b>49 704,78</b>

In 2016 the total amount of variable pay for persons holding managerial positions in the Bank within the meaning of the Resolution No 258/2011 and the position having an impact on the risk profile of the Bank, was equal to 2 969k PLN therein:

- a) awarded: 60% of the sum;
- b) awarded with deferred payment: 30% of the sum;
- c) still not awarded: 40% of the sum.

Aggregated quantitative information on remuneration of persons holding management positions is presented below:

<b>I Management Board Members, direct reports to MB Members (regardless of the form of employment)</b>			
<b>NO</b>	<b>The information scope</b>	<b>Amount</b>	<b>Commentary</b>
1	Number of people	11	
2	Fixed remuneration - paid	5 911	Salaries, honorary, car allowance
3	Variable pay in 2016 r. as regards to the Resolution 258/2011 KNF, granted in 2016	2 553	
4	Granted non-deffered part, where		
4.1	Cash benefit	1 277	
4.2	Non-cash instrument	1 277	
5	Accrued but not granted part (to be settled within 3 next years)	1 787	
5.1	Cash benefit	511	
5.2	Non-cash instrument	1 277	Amount for the period of 2017-20
<b>II Other key persons</b>			
<b>NO</b>	<b>The information scope</b>	<b>Amount</b>	<b>Commentary</b>
1	Number of people	8	
2	Fixed remuneration - paid	2 676	Salaries, honorary, car allowance
3	Variable pay in 2016 r. as regards to the Resolution 258/2011 KNF, granted in 2016	419	
4	Granted non-deffered part, where		
4.1	Cash benefit	208	
4.2	Non-cash instrument	208	
5	Accrued but not granted part (to be settled within 3 next years)	291	
5.1	Cash benefit	83	
5.2	Non-cash instrument	208	Amount for the period of 2017-20

#### **14. Information regarding entered agreements for intra-group financial support**

As at 31 December 2016 Bank has not entered any agreement for intra-group financial support concluded in accordance with article 141t of the Banking Act.

## 15. Declaration of Management Board

The Management Board of HSBC Bank Polska SA declares that the arrangements described in the Disclosures are appropriate to the facts and the risk management systems are adequate with regard to the Bank's profile and strategy.

**Michał Mrożek**

President of the Management Board

  
signature

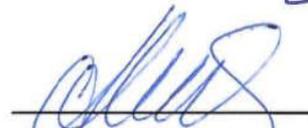
**Scott Solberg**

Member of the Management Board

  
signature

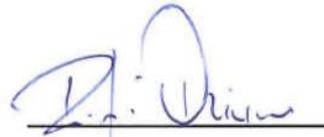
**Agata Mroczek**

Member of the Management Board

  
signature

**Rafał Dziura**

Member of the Management Board

  
signature

**Dariusz Kucharski**

Member of the Management Board

  
signature