KNF | KOMISJA NADZORU FINANSOWEGO

6 December 2022

KNF's stance on the dividend policy in 2023

During the session held 6 December 2022, the Polish Financial Supervision Authority (KNF) approved* its stance on the dividend policy of commercial banks, cooperative banks and affiliation banks, insurance undertakings, reinsurance undertakings, insurance-and-reinsurance undertakings, mutual fund management companies, universal pension fund management companies and brokerage houses in 2023. Each one of these sectors will receive recommendations in the form of a letter from the Chairman of KNF.

The direct aim of KNF's dividend policy is to ensure stability of the Polish financial sector through adaptation of the capital base of the supervised entities to the level of their risk and protection of the recipients of the financial services provided by such entities.

Commercial banks

KNF considers it necessary to adopt the following principles of the dividend policy of commercial banks in 2023:

1. An amount of up to 50% of the 2022 profit may be paid only by banks that meet the following criteria simultaneously:
    a) banks that are not implementing a remedial program[1],
    b) banks that are evaluated positively under the Supervisory Review and Evaluation Process (SREP) (final SREP score no lower than 2.5),
    c) banks that have a leverage ratio (LR) higher than 5%[2],
    d) banks that have a Tier I (CET1) core capital ratio no lower than the required minimum:
    4.5% + 56.25% x P2R requirement[3] + merged buffer requirement[4],
    e) banks that have a Tier I (T1) capital ratio no lower than the required minimum:
    6% + 75%*P2R requirement + merged buffer requirement,
    f) banks that have a total capital ratio (TCR) no lower than the required minimum:

[1] Remedial proceedings program / implemented remedial plan

[2] An obligation for banks to maintain a leverage ratio of at least 3% came into force on 28 June 2021. The 5% level required by KNF takes into account additional 2 p.p. of a conservative supervisory buffer, which a bank must fulfil to enable its payment of a dividend, if any (based on the fulfillment of additional criteria).

[3] Pillar II Requirement (P2R), that is an additional regulatory capital requirement; currently imposed for covering the foreign currency loan risk

[4] for the purposes of the dividend policy, increased by a 3 p.p. supervisory buffer

8% + P2R requirement + merged buffer requirement.

2. An amount of up to 75% of the 2022 profit may be paid only by banks that meet the criteria for the payment of 50% simultaneously, taking into account, as part of the capital criteria, the bank's sensitivity to an unfavorable macroeconomic scenario[5].

3. An amount of up to 100% of the 2022 profit may be paid only by banks that meet the criteria for the payment of 75% simultaneously and whose portfolio of receivables from the non-financial sector is of a good credit quality (the share of NPL, including debt instruments, is not greater than 5%).

The criteria specified in items 1-3 above shall be satisfied by the bank both on the standalone and on the consolidated level.

4. For banks having a material portfolio of foreign currency housing loans[6] the dividend yield shall be adjusted additionally in accordance with the following criteria:

    a) Criterion 1 – based on the percentage of foreign currency housing loans for households in the overall portfolio of receivables from the non-financial sector:

        - banks whose percentage exceeds 5% – adjust the dividend yield by 20 p.p.;
        - banks whose percentage exceeds 10% – adjust the dividend yield by 40 p.p.;
        - banks whose percentage exceeds 20% – adjust the dividend yield by 60 p.p.;
        - banks whose percentage exceeds 30% – adjust the dividend yield by 100 p.p.;

    b) Criterion 2 – based on the percentage of loans extended in 2007 and 2008 in their portfolio of foreign currency housing loans for households:

        - banks whose percentage exceeds 20% – adjust the dividend yield by 30 p.p.;
        - banks whose percentage exceeds 50% – adjust the dividend yield by 50 p.p.,

with the total adjustment value (max. 100%) being the sum of adjustments arising from both criteria.

KNF also considers it necessary that no other actions will be taken, in particular, actions falling outside the scope of their ongoing business and operating activity that could lead to lowering their own funds, without prior consultation with the regulatory authority. This applies also to any dividend payment from retained earnings and to any repurchase of treasury shares. KNF expects that each such operation will be preceded by a consultation with the regulatory authority and will be subject to its outcome.

[5] Bank's sensitivity to an unfavorable macroeconomic scenario, measured with the results of supervisory stress tests (P2G recommendation) defined as: relative change in CET1 calculated between the lowest CET1 level in the scenario's horizon and the CET1 on the test commencement, taking into account supervisory adjustments.
[6] banks that have in their portfolio receivables from the non-financial sector with the percentage of FX-denominated household mortgage loans exceeding 5%

Cooperative banks and affiliation banks

KNF considers it necessary to adopt the following principles of the dividend policy of cooperative banks and affiliation banks in 2023:

1. Affiliation banks should apply the general assumptions of the dividend policy – the same ones as in the case of other banks operating in the form of a joint stock company.

2. Dividend distribution is prohibited by cooperative banks with a C/I ratio above 85%, regardless of the criteria below.

3. Dividend distribution in other cooperative banks shall be based on the following principles:

   a) Up to 15% of net profit, provided that the following criteria are fulfilled simultaneously: banks not implementing corrective measures (those those not required to implement the remedial plans referred to in Article 141m of the Banking Law or the group remedial plans referred to in Article 141o of the Banking Law, and those that did not implement any of the remedial options defined in the remedial plan), banks with a final SREP score not lower than 2.5 (KNF master scale: 1 or 2), banks that have a leverage ratio (LR) higher than 5%, a total capital ratio (TCR) no lower than 12.0%, a Tier 1 (T1) capital ratio no lower than 10.0%, a CET1 common equity tier ratio no lower than 8.5% and that are not utilizing the option to reduce the basis for setting up special-purpose provisions.

   b) Up to 10% of net profit, provided that the following criteria are fulfilled simultaneously: banks not implementing corrective measures (those those not required to implement the remedial plans referred to in Article 141m of the Banking Law or the group remedial plans referred to in Article 141o of the Banking Law, and those that did not implement any of the remedial options defined in the remedial plan), banks with a final SREP score not lower than 2.5 (KNF master scale: 1 or 2), banks that have a leverage ratio (LR) higher than 5%, a total capital ratio (TCR) no lower than 12.0%, a Tier 1 (T1) capital ratio no lower than 10.0%, a CET1 common equity tier ratio no lower than 8.5%.

   c) Up to 5% of net profit, provided that the following criteria are fulfilled simultaneously: banks not implementing corrective measures (those those not required to implement the remedial plans referred to in Article 141m of the Banking Law or the group remedial plans referred to in Article 141o of the Banking Law, and those that did not implement any of the remedial options defined in the remedial plan), banks with a final SREP score not lower than 3.25 (KNF master scale: 1, 2 or 3), banks that have a leverage ratio (LR) higher than 5%, a total capital ratio (TCR) no lower than 10.5%, a Tier 1 (T1) capital ratio no lower than 8.5%, a CET1 common equity tier ratio no lower than 7.0%.

4. Regardless of the foregoing principles, in connection with the current geopolitical and economic situation and the possibility of deterioration of the banks' economic and financial standing in 2023, cooperative banks satisfying the criteria for dividend payment from the

2022 profit should consider retaining the profit in entirety and earmarking it to strengthen the capital base.

5. KNF will individually address those cooperative banks that do not meet the criteria to pay a dividend from their 2022 net profit.

Insurance undertakings, reinsurance undertakings and insurance-and-reinsurance undertakings

KNF considers it necessary to adopt the following principles of the dividend policy of insurance undertakings, reinsurance undertakings and insurance-and-reinsurance undertakings in 2023:

Dividend may be paid only by the undertakings that meet all of the following criteria for distributions from the 2021 and 2022 profits:

1. They received a good[7] or satisfactory[8] SREP risk score for 2021.

2. In the various quarters of 2022 they reported no shortage of own funds to cover the capital requirement (defined as the maximum of the minimum capital requirement (MCR) and the solvency capital requirement (SCR)).

3. In 2022, they were not covered by a short-term financial plan or the remedial plan referred to in Articles 312 and 313 of the Insurance and Reinsurance Activity Act of 11 September 2015.

4. As at 31 December 2022, own funds, without deducting the expected dividends, were at the level of at least 175% of the capital requirements for insurance undertakings, reinsurance undertakings, insurance-and-reinsurance undertakings operating in section I and at least 150% of the capital requirements for insurance undertakings, reinsurance undertakings, insurance-and-reinsurance undertakings operating in section II.

Insurance undertakings, reinsurance undertakings, insurance-and-reinsurance undertakings satisfying the above criteria may pay a dividend in the maximum amount of 100% of the profit generated in 2021 (taking into account dividends paid from the 2021 profit so far) and no more than 50% of the profit generated in 2022, however the coverage of capital requirements (after deducting the expected dividends from own funds) as at 31 December 2022, and for the quarter in which the dividend was paid, will be at the level of at least 175% for insurance undertakings, reinsurance undertakings, insurance-and-reinsurance undertakings operating in section I and at least 150% for insurance undertakings, reinsurance undertakings, insurance-and-reinsurance undertakings operating in section II.

[7] The risk score was given according to the macro scale (good score, i.e. 1.00 (from 1.00 to 1.74); satisfactory score, i.e. 2.00 (from 1.75 to 2.49); score raising concerns, i.e. 3.00 (from 2.50 to 3.24); unsatisfactory score, i.e. 4.00 (from 3.25 to 4)).
[8] ibidem

Insurance undertakings, reinsurance undertakings, insurance-and-reinsurance undertakings satisfying the above criteria, when deciding on the amount of the dividend, should take into account their capital needs within the period of 12 months from the approval date of the 2022 financial statements, which may result, among others, from changes in the market and legal environment, in particular from the high degree of uncertainty about the macroeconomic outlook for e.g. inflation rate, interest rates, foreign exchange rates, energy commodities or effects of the war caused by Russia's invasion of Ukraine.

Mutual fund management companies

KNF considers it necessary to adopt the following principles of the dividend policy of mutual fund management companies in 2023:

A. An amount of up to 75% of their 2022 net profit may be paid only by mutual fund management companies that meet the following criteria simultaneously:

   I. In 2022 and during the period from the outset of 2023 up to the date of adopting the resolution on distributing the 2022 profit, the mutual fund management company did not breach the regulations on statutory capital requirements.

   II. The mutual fund management company obtained the final SREP score of 1 or 2.

   III. The measures taken, including the method of profit distribution, will not lead to a reduction in the mutual fund management company's liquid assets minus the value of treasury shares below the level forming 170% of the capital requirement binding upon the management company. In turn, in respect of a mutual fund management company that manages defined date funds in accordance with the Employee Capital Accumulation Schemes Act, the profit distribution cannot at the same time lead to a reduction in the liquid assets held by that management company minus the value of treasury shares, below the level of 170% of the requirement stemming from Article. 59 sec. 1 item 2 of the Employee Capital Accumulation Schemes Act.

   IV. The profit distribution will not cause the capital requirements coverage ratio to fall below 1.5, where the capital requirements coverage ratio is computed as the quotient of the management company's equity and the capital requirements level in force.

B. An amount of up to 100% of their 2022 net profit may be paid only by mutual fund management companies that meet the following criteria simultaneously:

   I. The mutual fund management company satisfies criteria I–III listed in section A.

   II. The profit distribution will not cause the capital requirements coverage ratio to fall below 2, where the capital requirements coverage ratio is computed as the quotient of the management company's equity and the capital requirements level in force.

C. An amount exceeding 100% of their 2022 net profit taking into account the unpaid part of the net profit may be paid only by mutual fund management companies that meet the following criteria simultaneously:

   I. The mutual fund management company satisfies criterion I listed in section B.

   II. The mutual fund management company obtained the final SREP score of 1.

   III. The profit distribution will not cause the capital requirements coverage ratio to fall below 2.5, where the capital requirements coverage ratio is computed as the quotient of the management company's equity and the capital requirements level in force.

Additionally, when making the decision pertaining to the amount of the distribution, mutual fund management companies should take into account:

- their additional capital needs within a 12 month outlook from the time of approving the 2022 financial statements such that the method of profit distribution does not exert an influence on the ability to meet capital requirements in subsequent months,
- the amount of the financial result from the current year,
- claims reported by participants of the mutual funds against the management company in connection with improper management of mutual funds during the period from the date of adopting the last resolution on profit distribution.

The fulfillment of the said criteria is also required in the case of allocating net profit for the payment of a fee for the purchase of treasury shares of mutual fund management companies.

Universal pension fund management companies

KNF considers it necessary to adopt the following principles of the dividend policy of universal pension fund management companies in 2023:

A. An amount of up to 100% of their 2022 net profit may be paid only by universal pension fund management companies that meet the following criteria simultaneously:

   I. The management company has received a final SREP score of 1 (good) or 2 (satisfactory).

   II. In 2022 and during the period from the outset of 2023 up to the date of adopting the resolution on distributing profit, no situation has transpired in which the management company would fail to satisfy statutory capital requirements.

   III. As at 31 December 2022, the equity of a universal pension fund management company plus the value of the Indemnity Fund attributable to the management company represents no less than 1% of the net asset value of all pension funds managed by the management company.

IV. As at 31 December 2022, the liquid assets[9] of the management company plus the value of the Indemnity Fund attributable to the management company represents no less than 1% of the net asset value of all pension funds managed by the management company;

B. An amount exceeding 100% of their 2022 net profit may be paid only by universal pension fund management companies that meet the following criteria simultaneously:

I. The management company has received a final SREP score of 1 (good).

II. The management company satisfies criteria II-IV listed in section A.

III. The disbursement amount may not cause that in 2023 the amount of liquid assets of the management company plus the value of the Indemnity Fund attributable to the management company represents less than 1.75% of the net asset value of all pension funds managed by the management company.

Additional non-numerical criteria:

- The payment of a dividend may not lead to a reduction in equity or the value of liquid assets, as the case may be, plus the value of the funds in the Indemnity Fund attributable to the management company below the level specified in criterion III and criterion IV in section A as at the dividend payment date and within the 12 month outlook from the time of approving the 2022 financial statements, subject to criterion III in section B.

- When making the decision pertaining to the distribution of profit, the management company shall incorporate its additional capital needs within a 12 month outlook from the time of approving the 2022 financial statements associated with the management of target date funds in accordance with the Employee Capital Accumulation Schemes Act.

- When making the decision on the method of profit distribution, the management company shall take into account the claims reported by participants of the pension funds against the management company in connection with improper management of pension funds during the period from the date of adopting the last resolution on profit distribution.

Brokerage houses

KNF considers it necessary to adopt the following principles of the dividend policy of brokerage houses in 2023:

[9] The following are deemed to be liquid assets: securities issued by the State Treasury or National Bank of Poland, securities guaranteed or secured by the State Treasury or National Bank of Poland, receivables from an open-end pension fund by virtue of the fee charged to the contribution and the management fee, cash and other cash assets and other current financial assets.

A. An amount of up to 75% of their 2022 net profit may be paid by brokerage houses that meet the following criteria simultaneously:

   I. As at 31 December 2022, the entity fulfilled the following criteria:
      a) the ratio specified in Article 9(1)(a) of Regulation No 2019/2033 of the European Parliament and of the Council of 27 November 2019 on prudential requirements for investment firms and amending Regulations (EU) No 1093/2010, (UE) No 575/2013, (UE) No 600/2014 and (UE) No 806/2014 (OJ L 314 of 05.12.2019, as amended, hereinafter referred to as “Regulation No 2019/2033”), was at least 75%,
      b) the ratio specified in Article 9(1)(b) of Regulation No. 2019/2033 was at least 112.5%,
      c) the ratio specified in Article 9(1)(c) of Regulation No 2019/2033 was at least 175%.

   Entities that apply transitional provisions referred to in Part Nine of Regulation No. 2019/2033 for the purposes of the dividend policy shall set the aforementioned ratios without applying said transitional provisions.

   II. The SREP regulatory assessment score assigned in in 2022 was 1 or 2.
   III. In 2022 and up to the date of approving the financial statements and adopting the resolution on profit distribution for 2022, the entity in question has not violated the regulations regarding capital requirements set forth in Regulation 2019/2033 and the Financial Instruments Trading Act (Journal of Laws of 2022, Item 1500, as amended) and the regulations pertaining to the liquidity requirements set out in Regulation 2019/2033.

B. An amount not greater than 100% of the net profit generated in 2022 may be disbursed by those brokerage houses that meet the criteria listed in section A and met the criteria listed in section A item I also at the end of Q1, Q2 and Q3 2022.

C. An amount exceeding 100% of their 2022 net profit may be paid by brokerage houses that meet the following criteria simultaneously:

   I. The brokerage house meets the criteria enumerated in sections A items I and III and recorded a net profit for 2022.

   II. The SREP regulatory assessment score assigned in in 2022 was 1.

   III. For entities that adopt a resolution to pay a dividend:

      a) the ratio specified in Article 9(1)(a) of Regulation No 2019/2033 may not, as a result of adoption of the resolution to pay a dividend, drop below 150%,
      b) the ratio specified in Article 9(1)(b) of Regulation No 2019/2033 may not, as a result of adoption of the resolution to pay a dividend, drop below 187.5%,

c) the ratio specified in Article 9(1)(c) of Regulation No 2019/2033 may not, as a result of adoption of the resolution to pay a dividend, drop below 250%.

Entities that apply transitional provisions referred to in Part Nine of Regulation No 2019/2033 for the purposes of the dividend policy shall set the aforementioned ratios without applying said transitional provisions.

Satisfaction of the conditions referred to in condition C is required also in the case of applying for a permit to purchase treasury shares.

In the case of brokerage houses for which no SREP supervisory score was granted in 2022, criteria A II and C II do not apply.

In the case of brokerage houses which in 2022 obtained the permission of the Polish Financial Supervision Authority to include the current period's profit in Tier 1 capital, it is possible to pay a dividend in an amount not greater than the net profit for 2022, less the amount included in Tier 1 capital in accordance with this decision, subject to the fulfillment of the conditions referred to in items A or B.

Additionally, when making the decision pertaining to the amount of the dividend, brokerage houses shall take into account: their additional capital needs within a 12 month outlook from the time of approving the 2022 financial statements, and the current financial standing of the brokerage house at the time of approval of the financial statements and adoption of the resolution on distribution of the 2022 profit, in particular the amount of the recorded financial result of the brokerage house.

* The Polish Financial Supervision Authority vote on 6 December 2022 was attended by: J. Jastrzębski, R. Mikusiński, M. Mikołajczyk, K. Wiercioch, K. Budzich, A. Rożek, J. Wojtyła, P. Szałamacha, W. Dyduch, M. Tomczak. In the vote on the dividend policy of commercial banks, Polish Financial Supervision Authority member P. Szałamacha abstained from voting, while other members of the Polish Financial Supervision Authority voted in favor of adopting a resolution on this matter. Resolutions on other items regarding the dividend policy were adopted unanimously.