15 January 2019

KNF communication on the stance of the supervision authority regarding the dividend policy assumptions of commercial banks, cooperative and affiliating banks, insurance and reinsurance undertakings, brokerage houses, investment fund companies and general pension societies in 2019.

In its meeting held on 15 January 2019, the Polish Financial Supervision Authority (KNF) adopted unanimously the stance of the supervision authority regarding the dividend policy assumptions of commercial banks, cooperative and affiliating banks, insurance and reinsurance undertakings, brokerage houses, investment fund companies and general pension societies in 2019. The purpose of the dividend policy pursued by financial institutions in accordance with the KNF recommendations is to ensure a sustainable and secure development of the financial system. The situation of the Polish financial system is stable. KNF monitors, on a continuous basis, the capital ratios for specific entities in the system and, if necessary, takes appropriate preventive or development measures. Each sector will receive recommendations in the form of a letter from the Chairman of the KNF.

Commercial banks

It is recommended that a dividend from profit for previous year is paid out only by banks meeting all of the following criteria:

- they are not implementing a recovery programme[1];
- they have a positive evaluation

  (overall BION grade of no less than 2.5 – master-scale grade of 1 or 2);
- they have a leverage ratio (LR) of more than 5%;
- they have Common Equity Tier 1 (CET1) of not less than the required minimum increased by 1.5 pp.[2]:

  4.5% + 56%*add-on + combined buffer requirement[3] + 1.5%;
- they have Tier 1 capital (T1) of not less than the required minimum increased by 1.5 pp.[3]:

  6% + 75%*add-on + combined buffer requirement[4] + 1.5%;
- they have Total Capital Ratio (TCR) of not less than the required minimum increased by 1.5 pp.[3]:

  8% + add-on + combined buffer requirement[4] + 1.5%.

It is recommended that banks meeting all of the following criteria can pay out up to 75% of profit for the previous year.

Moreover, it is recommended that up to 100% of the profit generated for the previous year be paid out by banks meeting all of the above criteria, taking into account, within the capital criteria, the bank's sensitivity to an unfavourable macroeconomic scenario[4].

The dividend rate for banks engaged in currency loans[5] should also be adjusted as follows:

Criterion 1 – based on the share of household currency mortgage loans in the total portfolio of non-financial sector receivables:

- banks with a share above 10% – dividend rate adjustment by 20 pp.
- banks with a share above 20% – dividend rate adjustment by 30 pp.
- banks with a share above 30% – dividend rate adjustment by 50 pp.

[1]Recovery program/recovery program implementation
[2]1.5 pp – pursuant to Article 142 (4) of the Banking Law Act: when assessing the financial position of a bank, the Financial Supervision Authority (KNF) may take into account the bank's compliance with the own fund requirement as stipulated in Section 1(1), increased by 1.5 percentage points.
[3]Combined buffer requirement in the amount binding for 2019.
[4]The bank's sensitivity to an unfavourable macroeconomic scenario is measured on the basis of regulatory stress test results defined as the difference between TCR in the benchmark scenario and TCR in the shock scenario at the end of the period covered by the forecast (2020), taking into account any regulatory adjustments, reduced by the value of the conservation buffer in its target value (2.5%).
[5]Banks with a share of more than 5% of household currency mortgage loans in their portfolio of non-financial sector receivables.

Criterion 2 – based on the share of currency mortgage loans extended in 2007 and 2008 in the portfolio of household currency mortgage loans:

- banks with a share above 20% – dividend rate adjustment by 30 pp.
- banks with a share above 50% – dividend rate adjustment by 50 pp.

The adjustment criteria will be of less and less importance as the currency loan portfolio continues to depreciate.

The above criteria referring to payout of profit for the year preceding the decision should be met by banks both on an individual and a consolidated basis.

Cooperative and affiliating banks

With regard to affiliating banks it is recommended that the general terms of the dividend policy be applied, the same as for other banks operating as joint-stock companies.

It is recommended that a dividend:

A. of up to 100% of generated profit could be paid out only by cooperative banks meeting all of the following criteria: they are not implementing a recovery program, they have an overall BION grade of no less than 2.5 (master-scale grade of 1 or 2 as part of the Supervisory Review and Evaluation Process), they have a leverage ratio (LR) of more than 5%, total capital ratio (TCR) of no less than 15.0%, T1 capital of no less than 13.0%, Common Equity Ratio CET1 of no less than 11.5%, they do not apply the reduction to the basis for specific provisions.

B. of up to 75% of generated profit could be paid out only by cooperative banks meeting all of the following criteria: they are not implementing a recovery program, they have an overall BION grade of no less than 2.5 (master-scale grade of 1 or 2 as part of the Supervisory Review and Evaluation Process), they have a leverage ratio (LR) of more than 5%, total capital ratio (TCR) of no less than 15.0%, T1 capital of no less than 13.0%, Common Equity Ratio CET1 of no less than 11.5%.

C. Considering the proportionality principle and the legal and organisational nature of cooperative banks, a restricted dividend payout is recommended for two groups of cooperative banks:

1. Cooperative banks not implementing recovery programs, meeting the criterion of leverage ratio (LR) of more than 5%, Total Capital Ratio (TCR) of no less than the required minimum of 13.5%, Tier 1 capital ratio (T1) of no less than the required minimum of 11.5% and BION grade <=2.50, will be able to allocate to dividend payout as follows:
   - no more than 10% of net profit – for cooperative banks operating under institutional protection schemes,
   - no more than 5% of net profit – for all other cooperative banks.
2. Cooperative banks not implementing recovery programs, meeting the criterion of leverage ratio (LR) of more than 5%, with Total Capital Ratio (TCR) of no less than the required minimum of 13.5%, Tier 1 capital ratio (T1) of no less than the required minimum of 11.5% and BION grade between (2.50<BION<=3.25), will be able to allocate to dividend payout as follows:
   - no more than 2% of net profit.

Just as in previous years, individual measures will be taken by the KNF Office with regard to cooperative banks that do not meet the criteria of dividend payout from net profit for 2018.

Insurance and reinsurance undertakings

It is recommended that the dividend be paid out only by undertakings that meet all of the following criteria:

I. they received a BION risk grade “good” (1.00) or “satisfactory” (2.00) for 2017;

II. they did not reveal a shortage of own funds to cover the capital requirement (defined as the maximum of the minimum capital requirement (MCR) and solvency capital requirement (SCR)) in the subsequent quarters of 2018;

III. they were not subject to a short-term financial plan or recovery plan in 2018 as referred to in Article 312 and 313 of the Act of 11 September 2015 on Insurance and Reinsurance Activity;

IV. as at 31 December 2018, the value of their own funds not reduced by anticipated dividends was at least 175% of capital requirement levels for Branch I undertakings and at least 150% of capital requirement levels for Branch II undertakings.

Undertakings meeting the above criteria should restrict the dividend payout to 75% of 2018 profit, provided that the coverage of capital requirements should be at least 110% for the quarter in which the dividend is paid out.

At the same time, it is possible to pay out a dividend equal to the total 2018 profit (which means that payout of other equity components is not permitted), provided that the coverage of capital requirements (after deducting anticipated dividends from own funds) will be at least 175% for Branch I undertakings and at least 150% for Branch II undertakings, as at 31 December 2018 and for the quarter in which the dividend is paid out.

When deciding on the value of the dividend, the undertakings meeting the above criteria should take into account the additional capital needs in the 12 months following the approval of the financial statements for 2018, arising i.a. due to changes in the market or legal environment.

Brokerage houses

It is recommended that the dividend in 2019 be paid out only by the brokerage houses that meet all of the following criteria:

A. Dividend in the amount of no more than 75% of net profit for 2018:

I. for entities subject to capital adequacy rules under Regulation No. 575/2013 as at 31 December 2018:

- Common Equity Tier 1 amounted to at least 6%;
- Tier 1 capital amounted to at least 9%;
- Total Capital Ratio amounted to at least 14%;

II. for entities not subject to capital adequacy rules under Regulation No. 575/2013 as at 31 December 2018, the ratio representing the share of equity in total net assets is at least 50%:

III. the last assigned BION grade is 1 or 2;

IV. in 2018 and until the date of approving the financial statements and adopting the resolution on profit distribution for 2018, the entity did not infringe upon the capital requirement rules stipulated in Regulation No. 575/2013 and in the Act on Trading in Financial Instruments (Journal of Laws of 2017, Item 1768, as amended) or in the regulations on limits on large exposures.

B. Dividend in the amount of no more than 100% of net profit for 2018:

I. they meet all criteria listed under letter A;

II. for entities subject to capital adequacy rules under Regulation No. 575/2013, the criteria stipulated in Item A.I are met at the end of each quarter of 2018;

III. for entities not subject to capital adequacy rules under Regulation No. 575/2013, the criterion stipulated in Item A.II is met at the end of each quarter of 2018.

Moreover, when deciding on the value of the dividend, brokerage houses should take into account the additional capital needs in the 12 months following the approval of the financial statements for 2018.

Please note that brokerage houses obligated to maintain additional capital requirements under applicable provisions of law should increase the ratios stipulated in Item A.I by the value of such additional capital requirements.

Investment fund companies

Based on the analysis of the situation on the market for investment fund companies, taking into account the provisions in force, it is recommended that all of the following criteria be applied when deciding on the distribution of 2018 profit and its allocation in 2019:

I. there was no case of non-compliance with the statutory capital requirements in 2018 or in the period from the beginning of 2019 to the date of adopting the resolution on profit distribution;

II. any decisions regarding the profit distribution should take into account the additional capital needs in the 12 months following the approval of the financial statements for 2018, so that the manner of profit distribution does not affect the possibility of meeting capital requirements in the subsequent months, and consider the needs connected with the planned establishment and management of target-date funds pursuant to the Act of 4 October 2018 on Employee Capital Plans (Journal of Laws 2018, Item 2215, ("Employee Capital Plans Act"));

III. the decision on the manner of profit distribution should consider whether any claims have been raised against the company by shareholders of the investment funds since the last resolution on profit distribution on account of undue investment fund management;

IV. investment fund companies that meet the conditions stipulated in Items I–III and received an overall BION grade of 1 or 2 in the last Supervisory Review and Evaluation Process (BION) may allocate, in a manner other than by allocating net profit to creating or increasing the supplementary or reserve capitals or covering the loss from previous years:

  1. no more than 75% of net profit generated in 2018, provided that the profit distribution will not reduce the capital requirement coverage ratio below 1.5;

  2. more than 75% but no more than 100% of net profit generated in 2018, provided that the profit distribution will not reduce the capital requirement coverage ratio below 2

  – provided that the capital requirement coverage ratio is calculated as the product of the company's equity and the applicable capital requirement level.

V. the implemented measures, including profit distribution, may not lead to a decrease in value of the company's assets revealing the highest level of liquidity and security, calculated as the sum total of cash, securities issued by the State Treasury or the National Bank of Poland, shares in money market investment funds or in investments funds investing at least 85% of their assets in instruments issued, backed or guaranteed by the State Treasury, the National Bank of Poland or units of local self-government, reduced by the value of own shares below the level representing 150% of the company's capital requirement. However, in the case of an investment fund planning to establish and manage target-date funds under the Employee Capital Plans Act, profit distribution cannot reduce the value of liquid assets held by that society, as defined above, below the threshold of 150% of the requirement rising under Article 59(1)(1) of the Employee Capital Plans Act referring to the minimum level of liquid assets.

General pension societies

It is an essential condition recommended by the supervision authority that the general pension funds that decide to pay out dividend for 2019 meet all of the following criteria:

criterion I	the society received an overall BION grade of 1 (good) or 2 (satisfactory) for 2017;
criterion II	there was no case of the society's non-compliance with the statutory capital requirements in 2018 or in the period from the beginning of 2019 to the date of adopting the resolution on profit distribution;
criterion III	as at 31 December 2018, the society's equity, increased by the value of the Guarantee Fund attributable to the society, constituted at least 1.25% of the net asset value of the open-end pension fund managed by that society;
criterion IV	as at 31 December 2018, the society's liquid assets[6], increased by the value of the Guarantee Fund attributable to the society, constituted at least 1.25% of the net asset value of the open-end pension fund managed by that society;
criterion V	the society received a partial BION grade of 1 (good) or 2 (satisfactory) for "capital adequacy" for 2017.

Any general pension society meeting the above criteria should restrict the dividend value paid out in 2019 from 2018 profit or other equity components to no more than 100% of the profit generated in 2018. Moreover, the dividend payout should not reduce the value of equity or the value of liquid assets,

[6]The following are deemed as liquid assets: securities issued by the State Treasury or the NBP, receivables from open-end pension funds (OFE) related to premiums and management fees, cash and cash equivalents as well as other short-term financial assets.

increased by the value of funds attributable to the society under the Guarantee Fund below the threshold stipulated as criterion III and criterion IV.

Moreover, when deciding on dividend payout, the society should take into account the additional capital needs in the 12 months following the shareholder meeting's approval of the society's financial statements for 2018, in particular the needs connected with the establishment and management of target-date funds pursuant to the Act of 4 October 2018 on Employee Capital Plans (Journal of Laws, Item 2215). A society that already manages a voluntary pension fund should also consider the risk connected with this area of its activity and its potential impact on the financial result and capital position.