

## DESCRIPTION OF RISKS ASSOCIATED WITH FINANCIAL INSTRUMENTS OFFERED IN THE CORPORATE BANKING SEGMENT IN BANK MILLENNIUM S.A.

### This description of risks consists of:

- description of risks related to the execution of treasury transactions in Bank Millennium S.A. and description of investment services

### These descriptions include:

- general information on currency risk, interest rate risk and other risks specific to that type of instrument,
- identification of risks associated with that type of financial instrument including an explanation of leverage and its effects and the risk of losing the entire investment including the risks associated with insolvency of the issuer or related events, such as cancellation or conversion of debt.
- identification of the volatility of that type of financial instrument or limitations concerning the availability of the market for that type of instrument,
- identification of the possibility that the Client might assume, as a result of transactions in that kind of financial instrument, financial commitments and other additional obligations, including contingent liabilities, additional to the cost of acquiring the financial instrument;
- description of margin requirements or similar obligations applicable when investing in financial instruments of that type.
- Information on impediments or restrictions for divestment, for example as may be the case for illiquid financial instruments or financial instruments with a fixed investment term, including an illustration of the possible exit methods and consequences of any exit, possible constraints and the estimated time frame for the sale of the financial instrument before recovering the initial costs of the transaction in that type of financial instruments.

Treasury transactions are concluded according to the rules and in the manner specified in the following regulations: *“Regulations for concluding treasury transactions at Bank Millennium SA”* or *“Regulations on entering into spot and forward foreign exchange transactions and currency swap transactions”* or *“Regulations on entering into spot and forward foreign exchange transactions and currency swap transactions for natural persons operating a business and being Corporate Banking Client in Bank Millennium S.A.”* or *“Regulations of spot, forward financial transactions, transactions in securities and term deposits in Bank Millennium S.A.”* (each of those hereinafter separately referred to as *“Regulations”*).

The Bank's Exposure to the Client includes the following, as concluded by the Client:

- spot and forward foreign exchange transactions and currency swaps,
- currency options,
- forward rate agreements (FRA),
- interest rate swaps (IRS),
- currency interest rate swaps (CIRS),
- interest rate options.

The transactions specified above are subject to daily valuation.

### DEFINITION OF A DERIVATIVE

A derivative is a financial instrument in the form of a contract, the value of which depends on the price of another financial instrument (e.g. currency, interest rate or commodity) called the underlying instrument. In other words, a derivative “derives” from the underlying instrument. It is also said that a derivative is exposed to the underlying instrument.

Derivatives offer the possibility of replicating the payment profile of underlying instruments or modify it in accordance with the investor's needs. The main purpose for using derivatives is to protect the investor against changes in the price of the underlying instrument, and in particular against:

- an increase in the price of the underlying instrument,
- a decrease in the price of the underlying instrument,
- simultaneous increase and decrease in the price of the underlying instrument (protection against volatility of the underlying instrument).

There are currently many different types of derivatives on the market. The most popular ones are Forward/Futures, Options and Swaps, on currencies, interest rates and commodities. Derivatives are offered as tradable on exchanges and over-the-counter (OTC). All instruments offered by Bank Millennium are offered as over-the-counter instruments. In special cases, these are non-standard instruments, introduced into the Bank's offering specifically for the needs of investors who are parties to a specific transaction.

### I. CURRENCY RISK - GENERAL INFORMATION

The nature of currency risk can be defined as “uncertainty”, in particular the possibility of incurring a loss as a result of unfavorable changes in exchange rates. In practice, it means that the expected foreign income and expenditures, expressed in the domestic currency, or the value of assets and liabilities expressed in foreign currencies and owned by a company may change as a result of variation of exchange rates, where the direction and extent of the variations are difficult to predict.

Example:

On 1 July, Poland-based Company A enters into a sales agreement with a foreign Company B for the sale of goods in the amount of EUR 1,000,000. When the transaction is concluded, the EUR/PLN exchange rate is 3.9. The term of payment is 90 days. In absence of the currency risk, Company A would expect the amount receivable to be PLN 3,900,000 on 1 October. However, since the EUR/PLN exchange rate may change in the period from 1 July to 1 October, the value of receipts of Company A measured in PLN may change:

- If the EUR/PLN exchange rate increases, the receipts of Company A measured in PLN will be higher (for example, at the EUR/PLN exchange rate at 4.0, the receipts of Company A would be PLN 4,000,000);
- If the EUR/PLN exchange rate falls, the receipts of Company A measured in PLN will be lower (for example, at the EUR/PLN exchange rate at 3.8, the receipts of Company A would be PLN 3,800,000).

Currency risk in the short term may, for example, lead to a reduction in the amounts of realized receivables or an increase in liabilities translated into the domestic currency. In the long term, it could result in a threat of impairment of the expected future cash flows from the planned foreign transactions. It also affects individual balance sheet items which, when translated at the new exchange rate, may change their carrying amounts. As a result, currency risk may pose a significant threat to the current financial standing, expected cash flows and market value of the company. Its effects are therefore both dangerous and costly.

Currency risk is a multi-faceted and complex concept. It depends on the degree of currency exchange rate fluctuations and increases proportionally as they increase. Time is also an important factor. The longer the period between e.g. the date of incurring a foreign currency loan and the date of its repayment, the higher the risk, since it is more difficult to estimate the future exchange rate level.

The constantly fluctuating exchange rates have a significant influence on current business conditions and, as a result, they change the business conditions for importers, exporters, investors, lenders and borrowers, transnational companies and other entities whose activity, for various reasons, entails operations carried out on the currency market.

In a period, a number of economic, political and social factors affect the volatility of the exchange rate. Exchange rate volatility can be significant even in the short term. In the case of some currencies, convertibility may be suspended or a currency may be subject to an unexpected appreciation/depreciation in respect to other currencies.

### II. SPOT AND FORWARD FOREIGN EXCHANGE TRANSACTIONS/CURRENCY SWAPS

- 1. Identification of risks associated with that type of financial instrument including an explanation of leverage and its effects and the risk of losing the entire investment including the risks associated with insolvency of the issuer or related events, such as cancellation or conversion of debt.**

A Spot Foreign Exchange Transaction is an agreement between a Client and the Bank in which one of the parties undertakes to purchase and the other to sell a specified amount of a currency at a predetermined exchange rate. A Spot Foreign Exchange Transaction is settled within two business days of the Transaction Date.

A Forward Foreign Exchange Transaction is an agreement between a Client and the Bank in which one of the parties undertakes to purchase and the other to sell in the future a specified amount of a currency at a predetermined exchange rate.

The price is negotiated by the parties and may not be changed during the term of the contract. In the case of a forward purchase of the base currency, the Client bears the risk of a decrease in the exchange rate, which would result in a negative valuation of the position as compared to the current market rate. In the case of a forward sale of the base currency, the Client bears the risk of an increase in the exchange rate, which would result in a negative valuation of the position as compared to the current market rate.

A Currency Swap Transaction is a combination of two currency transactions – a Spot Foreign Exchange Transaction and an opposite Forward Foreign Exchange Transaction. Therefore, a currency swap is a contract in which two parties agree to exchange a specified amount of a currency for an equivalent amount in another currency for a specified period of time. The exchange rate as at the maturity date is determined when the transaction is concluded based on the interest rate differences between the two currencies. In the case of a Currency Swap Transaction, the Client bears the same exchange rate risk as in the case of Spot and Forward Foreign Exchange Transactions as described in the previous paragraph.

Leverage has always been strongly linked to trading in financial instruments. We will explain the nature of the leverage mechanism for both speculative and hedging transactions.

Speculation is nothing more than a bet on the future level of the exchange rate. The purpose of such activity is to earn profit from the concluded transactions, the direction of which proved to be consistent with the direction of exchange rate changes. In this context, foreign exchange transactions (excluding Spot Foreign Exchange Transaction) offer the possibility, as opposed to investing directly in a foreign currency (physical purchase of the currency in a settlement account), of using financial leverage, i.e. obtaining benefit from changes in the foreign exchange rate while investing capital representing just a small fraction of the notional value of the transaction (the level of margins or the level of encumbrance of the treasury limit, under which currency transactions can be concluded, are several times lower than the notional values of the contracts). However one should keep in mind that the use of leverage offers the opportunity of multiplying gains, but can also result in losses being multiplied. **For these reasons, speculative transactions are concluded primarily by entities professionally trading in financial instruments.**

Hedging involves the use of foreign exchange transactions (excluding Spot Foreign Exchange Transaction) to offset potential losses related to a natural exposure resulting from the business activity (e.g. an exporter's exposure to the appreciation of the domestic currency, an importer's exposure to the depreciation of the domestic currency). While in speculative transactions, the cash flows related to the transaction itself are of primary importance, hedging transactions cannot be considered in separation from the Client's natural exposure.

Example:

A Polish importer is exposed to depreciation of the domestic currency, e.g. against the USD. An increase of the USD/PLN rate will require the company to pay more for the goods purchased abroad. Therefore, the importer may be interested in hedging, by entering into a Forward Foreign Exchange Transaction by buying USD at a predetermined exchange rate on a specified future date.

In such a case, the potential losses resulting from an increase in the USD/PLN exchange rate will be offset by the profit from the Forward Foreign Exchange Transaction concluded with the Bank. Conversely, losses on the forward transaction will be offset by the fact that goods and services are purchased at a lower USD/PLN rate. However, if the notional value of the Forward Foreign Exchange Transaction exceeds the level of the Client's natural exposure, then an increase in the USD/PLN rate will generate additional profits for the Client, and a decrease in the USD/PLN rate will result in

unlimited losses. This results from the application of financial leverage resulting from a matching of the hedge to the natural exposure to a market risk factor.

By concluding Spot and Forward Foreign Exchange Transactions and Currency Swap Transactions, the Bank accepts credit risk, that is the risk of the Bank being unable to repay its liabilities when due, including the risk of the Bank's bankruptcy. As a result of this risk, the Bank may fail to make payments to the Client arising out of the terms of concluded transactions.

The Bank stipulates that the Client's receivables arising out of the Spot and Forward Foreign Exchange Transaction and from Currency Swap Transactions concluded on the basis of appropriate regulations are not covered by the protection measures within the meaning of the Act of 10 June 2016 on the Bank Guarantee Fund, the Deposit Guarantee Scheme and Mandatory Restructuring (the "BGF Act").

The Bank stipulates that the Bank's liabilities under Spot and Forward Foreign Exchange Transactions and Currency Swap Transactions concluded under relevant regulations may, where the conditions prescribed by law are satisfied, be subject to a debt cancellation or conversion measure according to the rules set forth in the BGF Act.

## 2. Identification of the volatility of that type of financial instrument or limitations concerning the availability of the market for that type of financial instrument.

The price of a Forward Foreign Exchange Transaction and a Currency Swap Transaction when it is concluded and the subsequent change in the market value are affected by the following factors: the current exchange rate level, the interest rate in the base currency for the period equal to the duration of the transaction, the interest rate in the quoted currency for the period equal to the length of the transaction, and the length of the transaction. It is also important to determine the extent to which the volatility of market parameters will influence the volatility of the Bank's exposure to the Client under the outstanding transactions (mark-to-market valuation). Swap points are the difference between the forward and spot exchange rates between the base and the quoted currencies, which is an expression of the difference in interest rates in the base currency and the quoted currency, for the period from the spot value date to the value date, and in the case of a currency swap transaction – for the period from the transaction date or from the date following the transaction date or from the spot value date of the spot transaction to the value date. Swap points are calculated according to the following formula:

$$PT = SPOT \times \left[ \frac{1 + \left[ i_Q \times \frac{D}{B_Q} \right]}{1 + \left[ i_B \times \frac{D}{B_B} \right]} - 1 \right]$$

where:

PT – swap points

SPOT – spot rate on the interbank market

$i_B$  – annual interest rate on the base currency over a year

$i_Q$  – annual interest rate on the quoted currency

D – number of days of transaction

$B_B$  – number of days in the year typical for the base currency (360 or 365)

$B_Q$  – number of days in the year typical for the quoted currency (360 or 365)

**The increase in the value of swap points** is affected by a decrease in market interest rates in the base currency and/or an increase in market interest rates in the quoted currency for a period corresponding to the length of the transaction. In the event that the Client enters into a forward foreign exchange transaction for the sale by the Client of the base currency for the quoted currency, the increase of swap points in relation to their level as at the transaction date has a negative impact on the valuation of the concluded transaction.

**A decrease in the value of swap points** is affected by an increase in market interest rates in the base currency and/or a decrease in market interest rates in the quoted currency for a period corresponding to the length of the transaction. In the event that the Client enters into a forward foreign exchange transaction for the purchase by the Client of the base currency for the quoted currency, the decrease of swap points in relation to their level as at the transaction date has a negative impact on the valuation of the concluded transaction.

Before concluding a transaction, the Client should make sure that the given currency pair is liquid and whether

there are limitations as to technical possibilities of opening or closing the position (terms of placing orders to execute a currency transaction during the Bank's business hours). The Client should take into account the risk of reduction or lack of liquidity on the financial market, which may result in a less favorable price for the transaction being negotiated.

There may be limited availability of the market for Forward Foreign Exchange Transactions and Currency Swap Transactions, which may affect their price. These limitations may in particular prevent Bank Millennium from ensuring the possibility of concluding and executing transactions to purchase and sell a financial instrument at any moment chosen by the Client.

## 3. Identification of the possibility that the Client might assume, as a result of transactions in that kind of financial instrument, financial commitments and other additional obligations, including contingent liabilities, additional to the cost of acquiring the financial instrument;

A Spot and Forward Foreign Exchange Transaction and a Currency Swap Transaction are settled by delivery of currency or by difference to the exchange rate of the opposite transaction. In the case of transactions featuring currency delivery, the Client undertakes to ensure that the account is covered by an amount equal to the nominal value of the transaction.

The choice of settlement method does not affect the value of the instrument at the time the transaction is concluded.

Conclusion of a Spot and Forward Foreign Exchange Transaction and a Currency Swap Transaction involves the Client incurring additional commitments associated with the requirement to maintain and replenish the margin in accordance with the terms and conditions set forth in the applicable regulations.

## 4. Description of margin requirements or similar obligations applicable when investing in financial instruments of that type.

Forward Foreign Exchange Transactions and Currency Swap Transactions are executed on the basis of a treasury limit or a margin in the form of an ownership transfer of cash. Transaction collateral (a margin or encumbrance of a treasury limit) is maintained until the transaction is correctly settled. Spot Foreign Exchange Transactions are executed on the basis of either a treasury limit or a blockade of funds on the Client's account on the Transaction date.

The valuation of the Bank's exposure to the Client depends, among other things, on changes in the exchange rate and may be subject to sudden changes (just as the exchange rate is). If the negative valuation exceeds the amount of the granted treasury limit and the margin established, the Client will be requested to replenish the collateral on the terms and conditions set forth in the Regulations. The amount needed to replenish the collateral may be significant in certain market conditions and constitute a significant burden for the Client. In case of a default on this obligation, the Bank will have the right, on the terms and conditions described in the Regulations, to an early closure and settlement of the Client's position and early termination of the contract. The settlement amount will become the Client's due and payable liability to the Bank.

## 5. Information on impediments or restrictions for disinvestment, for example as may be the case for illiquid financial instruments or financial instruments with a fixed investment term, including an illustration of the possible exit methods and consequences of any exit, possible constraints and the estimated time frame for the sale of the financial instrument before recovering the initial costs of the transaction in that type of financial instruments.

The Client has the right to an early, full or partial closure of a Cash or Forward Foreign Exchange Transaction or a Currency Swap Transaction only by concluding a closing transaction, that is a Cash or Forward Foreign Exchange Transaction on terms opposite to the terms of the transaction.

In each case, the terms of the closing transaction are agreed by the Parties to the transaction based on the current market conditions (with reference to the spot price and swap points) in effect on the date the Client concludes the closing transaction.

Example 1:

If the Client purchases base currency (e.g. USD) for quoted currency (e.g. PLN), concluding a closing transaction means that the Client should conclude a transaction to sell back the base currency (USD) for the

quoted currency (PLN) on the originally agreed value date.

If the closing rate, i.e. the rate, at which the Client sells back the USD for PLN, is higher than the agreed rate at which the Client purchases USD for PLN, the Client will close the transaction with a profit calculated as the difference between the rate at which the USD is sold back for PLN and the rate at which USD is purchased for PLN, multiplied by the nominal amount of the transaction to be closed.

Otherwise, if the closing rate, i.e. the rate, at which the Client sells back the USD for PLN, is lower than the agreed rate at which the Client purchases USD for PLN, the Client will close the transaction with a loss calculated as the difference between the rate at which the USD is purchased for PLN and the rate at which USD is sold back for PLN, multiplied by the nominal amount of the transaction to be closed.

Example 2:

If the Client sells base currency (e.g. USD) for quoted currency (e.g. PLN), concluding a closing transaction means that the Client should conclude a transaction to repurchase the base currency (USD) for the quoted currency (PLN) on the originally agreed value date.

If the closing rate, i.e. the rate, at which the Client repurchases the USD for PLN, is lower than the agreed rate at which the Client sells USD for PLN, the Client will close the transaction with a profit calculated as the difference between the rate at which the USD is sold for PLN and the rate at which USD is repurchased for PLN, multiplied by the nominal amount of the transaction to be closed.

Otherwise, if the closing rate, i.e. the rate, at which the Client repurchases the USD for PLN, is higher than the agreed rate at which the Client sells USD for PLN, the Client will close the transaction with a loss calculated as the difference between the rate at which the USD is repurchased for PLN and the rate at which USD is sold for PLN, multiplied by the nominal amount of the transaction to be closed.

The amount receivable or payable by the Client may be, by agreement of the Parties, subject to an early settlement by discounting it for the period from the originally agreed value date to the date of the closing transaction. In such a case, it will become a due and payable liability of the Client or the Bank on that date. The Bank stipulates that once concluded, a transaction cannot be cancelled and its parameters cannot be changed.

## 6. Other risks:

When entering into financial market transactions, the Client should also take into account other risks of legal, accounting, fiscal and operational nature that are independent of Bank Millennium.

With regard to forward foreign exchange transaction and currency swap transactions, the Bank provides the service of executing orders to purchase or sell financial instruments to the Client's account, in accordance with Article 69 sect. 2 pt. 2 of the Act on Trading in Financial Instruments.

## I.I. CURRENCY OPTIONS/EXOTIC CURRENCY OPTIONS

### 1. Identification of risks associated with that type of financial instrument including an explanation of leverage and its effects and the risk of losing the entire investment including the risks associated with insolvency of the issuer or related events, such as cancellation or conversion of debt.

European Currency Option is an instrument giving its purchaser the right to buy (if a Call Option is purchased) or sell (if a Put Option is purchased) an agreed amount of the base currency for the quoted currency at a predetermined Option exercise rate on a specified future date. For the purchase of this right, the Option buyer pays the seller (or the issuer or "writer" of the Option) an option premium. On the other hand, the Option seller is obligated to sell (if it sells a Call Option) or buy (if it sells a Put Option) an agreed amount of the base currency at a predetermined Option exercise rate on a specified future date.

The option premium is payable by the Option buyer within two business days of the transaction date and is not refundable if the buyer decides not to exercise the Option.

From the point of view of the Option exercise date, there are American Options and Bermuda Options in addition to European Options. American Option buyers may exercise their rights at any time before the Option

exercise date; for Bermuda Options, Option exercise dates are defined in advance.

The market risk profile resulting from an option transaction is asymmetrical for the Option buyer and the Option seller.

The **risk of the Option buyer** is limited to the amount of the option premium paid. In the case of a Call Option, if on the exercise date of the Option the base currency to quoted currency reference rate is lower than the agreed Option exercise rate, the Option buyer does not exercise its right and buys the base currency for the quoted currency at the current exchange rate. In the case of a Put Option, if on the exercise date of the Option the base currency to quoted currency reference rate is higher than the agreed Option exercise rate, the Option buyer does not exercise its right and sells the base currency for the quoted currency at the current exchange rate. In both these cases, the option premium paid previously is not refundable.

The base currency to quoted currency reference rate is the rate agreed upon by the parties on the transaction date. For European Options, unless the parties agree otherwise, the standard practice is to use the market rate of the base currency at 11.00 a.m. on the Option exercise date.

The Option buyer, by purchasing an Option, acquires the right to buy (if a Call Option is purchased) or sell (if a Put Option is purchased) the base currency for the quoted currency, and may resell this right fully or partially at any time, until the day preceding the Option exercise date, by selling an option of the same type (Call or Put, respectively), with the same Option exercise rate, the same Option exercise date and with a nominal value not exceeding the nominal value of the purchased Option. Such a transaction is referred to as an opposite transaction. The Option seller receives an option premium for the total or partial resale of the Option. If, in the period from the Option purchase date to the opposite transaction date, any factors occurred causing an increase in the value of the Option, the Option buyer will obtain a revenue equal to the difference between the option premium received on the sale of the Option and the option premium paid on account of the purchase of the Option. If, in the period from the Option purchase date to the opposite transaction date, any factors occurred causing a decrease in the value of the Option, the option premium received for the resale of Option may not fully compensate for the option premium paid on account of the purchase of the Option. Factors affecting the change in the Option value in the period from the transaction date to the Option exercise date are described in item 2 of this chapter.

Contrary to the Option buyer, the **Option seller** bears an unlimited risk of changes in the exchange rate if the market changes to its disadvantage on the Option exercise date. In the case of a Call Option, if on the Option exercise date the base currency to quoted currency reference exchange rate is higher than the Option exercise rate agreed by the parties on the transaction date, the Option seller will sell the agreed amount of the base currency for the quoted currency at the Option exercise rate that is lower than the reference rate, or settle the foreign exchange losses in the amount of the difference between the base currency to quoted currency reference rate and the Option exercise rate multiplied by the agreed nominal value of the transaction. In the case of a Put Option, if on the Option exercise date the base currency to quoted currency reference exchange rate is lower than the Option exercise rate agreed by the parties on the transaction date, the Option seller will buy the agreed amount of the base currency for the quoted currency at the Option exercise rate that is higher than the reference rate, or settle the foreign exchange losses in the amount of the difference between the Option exercise rate and the base currency to quoted currency reference rate multiplied by the agreed nominal value of the transaction.

#### Example:

A Polish importer is exposed to depreciation of the domestic currency, for example against the USD. An increase of the USD/PLN rate will require the company to pay more for the goods purchased abroad. Therefore, it may be interested in hedging the risk related to an increase in the exchange rate, by purchasing a European Call Currency Option. The purchase of a European Call Option gives the Client the right to purchase an agreed amount of the base currency (USD) for the quoted currency (PLN) on the agreed Option exercise date and at the agreed Option exercise rate. The Client pays the Bank an option premium for the purchase of the Option.

If the market USD/PLN exchange rate at 11.00 am on the Option exercise date is higher than the Option exercise rate then the Client decides to exercise the Option by purchasing USD for PLN at the Option exercise rate, i.e. cheaper than at the current USD/PLN rate. The Bank as the Option seller is obliged to sell the agreed amount of USD to the Client at the Option exercise rate. The operating losses incurred by the Client as a result of the increase in the USD/PLN exchange rate were offset by the profit earned on the exercise of the Currency Option.

If the market USD/PLN exchange rate at 11.00 am on the Option exercise date is lower than the Option exercise rate then the Client does not exercise the Option and purchases the currency cheaper, i.e. at the current USD/PLN rate.

Therefore, the Option exercise rate is nominally the maximum rate at which the Option buyer would purchase USD for PLN. In both cases (whether or not the Client exercises the Option), the economic result on the transaction should take into account the cost of the option premium paid by the Client in advance.

Currency options may also take the form of so-called **exotic currency Options**, which entail certain additional conditions as compared to the classic Call Options or Put Options (which are also referred to as vanilla Options). The main types of Exotic Options are: Barrier Options, Asian Options, and Binary Options.

In the case of Barrier Options, in addition to the Option exercise rate, the parties also agree on the level of the knock-in or knock-out barrier. A **knock-out barrier** is the base currency to quoted currency exchange rate agreed upon by the parties, above which the rights and obligations of the parties related to the option transaction are extinguished. Looking at the relationship between the knock-out barrier and the base currency to quoted currency spot exchange rate as at the transaction date, there are two types of knock-out barriers: up-and-out and down-and-out. In the case of an up-and-out barrier, on the transaction date the barrier rate is higher than the base currency to quoted currency exchange rate, while in the case of a down-and-out barrier, the barrier rate is lower than the base currency to quoted currency exchange rate on the transaction date.

A **knock-in barrier** is the base currency to quoted currency exchange rate set by the parties, above which the rights and obligations of the parties related to an option transaction come into force. Looking at the relationship between the knock-in barrier and the base currency to quoted currency spot exchange rate as at the transaction date, there are two types of knock-out barriers: up-and-in and down-and-in. In the case of an up-and-in barrier, on the transaction date the barrier rate is higher than the base currency to quoted currency spot exchange rate, while in the case of a down-and-in barrier, the barrier rate is lower than the base currency to quoted currency exchange rate on the transaction date.

Considering the duration of the barrier, a distinction is made between **American type barriers and European type barriers**. For an American barrier, the reference rate is the base currency to the quoted currency spot exchange rate as observed from the transaction date up to and including the Option exercise date. For a European type barrier, the reference rate is the base currency to quoted currency exchange rate on the Option exercise date. The type of reference rate is determined by the parties as they agree on the terms and conditions of the transaction.

For **Asian Options**, the reference rate is the arithmetic mean or geometric mean of the exchange rate observations made within the timeframe agreed upon by the parties. Exchange rate observations may be made on a daily, weekly, monthly basis, or in irregular intervals agreed by the parties on the transaction date.

In the case of **Binary Options**, the parties agree on a fixed amount of performance for the Option buyer in the event that it is to be exercised. The amount of the performance is agreed upon in advance on the transaction date.

The Client should bear in mind that the Options described above do not exhaust the full catalog of Exotic Options offered by the Bank.

Currency Options operate based on the financial leverage mechanism. As a result of the leverage, even the smallest movements in market prices affecting the valuation of Options may have a significant influence on the valuation of the whole transaction. Currency Option Transactions are executed on the basis of a treasury limit or a margin, which are encumbered with the amount corresponding to the risk weights adopted by the Bank.

In such a case, a Currency Option transaction is subject to a financial leverage mechanism. Relatively small changes in the exchange rate will have a significantly larger (positive or negative) impact on the valuation of the transaction.

Conclusion of Currency Options entails the Bank's credit risk, i.e. risk of the Bank being unable to meet its obligations on time, including the risk of the Bank's bankruptcy. As a result of this risk, the Bank may fail to make payments to the Client arising out of the terms of concluded transactions.

The Bank stipulates that the Client's receivables arising out of the Currency Options concluded on the basis of appropriate regulations are not covered by the protection measures within the meaning of the Act of 10 June 2016 on the Bank Guarantee Fund, the Deposit Guarantee Scheme and Mandatory Restructuring (the "BGF Act"). The Bank stipulates that the Bank's liabilities under Currency Options concluded under relevant regulations may, where the conditions prescribed by law are satisfied, be subject to a debt cancellation or conversion measure according to the rules set forth in the BGF Act.

## 2. Identification of the volatility of that type of financial instrument or limitations concerning the availability of the market for that type of financial instrument.

The price of a Currency Option (the option premium amount) at the time of concluding the transaction and the change in its theoretical value during the transaction are affected by the following market parameters:

- Relationship between the base currency to quoted currency exchange rate and the Option exercise rate. From the point of view of the above relationship we distinguish at-the-money-forward Options (where the exercise rate is equal to the forward rate), in-the-money Options (where the exercise rate is lower than the forward rate in the case of a Call Option and higher than the forward rate in the case of Put Option) and out-of-the-money Options (where the exercise rate is higher than the forward rate in the case of a Call Option and lower than the forward rate in the case of a Put Option). In the case of a Call Option, the Option price increases in inverse proportion to the increase in the Option exercise rate, in the case of a Put Option, it increases in proportion to the increase in the Option exercise rate.
- Implied volatility of an exchange rate quoted on a currency market. Implied volatility is based on the expectations of the currency market participants as to the future level of volatility and may differ from the actually recorded historical volatility. Both the Call Option price and the Put Option price increase directly in proportion to the increase in implied volatility.
- Interest rate in the base currency – the Call Option price increases in inverse proportion to the increase in the base currency interest rate for the period remaining until the Option exercise date, while the Put Option price – in direct proportion to the increase in the base currency interest rate for the period remaining until the Option exercise date.
- Interest rate in the quoted currency – the Call Option price increases in direct proportion to the increase in the quoted currency interest rate for the period remaining until the Option exercise date, while the Put Option price – in inverse proportion to the increase in the quoted currency interest rate for the period remaining until the Option exercise date.
- Length of the option transaction / time remaining until the Option exercise date – the price of both the Call Option and the Put Option increases in direct proportion to the increase in transaction length.

Before concluding a transaction, the Client should make sure that the given currency pair is liquid and whether there are limitations as to technical possibilities of opening or closing the position in Option transactions.

The Client should take into account the risk of reduction or lack of liquidity on the financial market, which may result in a less favorable price for the transaction being negotiated. There may be limited availability of the market for Currency Option transactions, which may affect their price. These limitations may in particular prevent Bank Millennium from ensuring the possibility of concluding and executing transactions to purchase and sell a financial instrument at any moment chosen by the Client.

## 3. Identification of the possibility that the Client might assume, as a result of transactions in that kind of financial instrument, financial commitments and other additional obligations,

**including contingent liabilities, additional to the cost of acquiring the financial instrument;**

If the Option transaction is exercised by the Option buyer, the Client undertakes to settle the spot foreign exchange transaction. Currency Option purchase or sale transactions are settled by delivery of currency or by difference to the current spot rate, unless the parties agree on a different reference rate in the contract. The choice of settlement method does not affect the value of the instrument at the time the transaction is concluded.

If an option transaction is settled by currency delivery then the Client undertakes to settle the currency transaction (ensure that funds are available on the account in the amount corresponding to the nominal value of the Option), the parameters of which result directly from the terms of the option transaction.

If an option transaction is settled by difference then the Client undertakes to provide, on the settlement date, an amount corresponding to the differential settlement amount.

The settlement method for an option transaction should be agreed by the parties on the transaction date. If no such agreement is made then the transaction will be settled by delivery of currency. Then, unless the Parties agree otherwise, the Client at its own risk will choose the moment of closing the spot foreign exchange transaction by concluding an opposite transaction (from the Option exercise date to the settlement date).

Conclusion of a currency option sale transaction by the Client involves the Client incurring additional commitments associated with the requirement to maintain and replenish collateral in accordance with the terms and conditions set forth in the applicable regulations.

**4. Description of margin requirements or similar obligations applicable when investing in financial instruments of that type.**

Currency Option transactions are carried out on the basis of a treasury limit, a blockade or a margin in the form of an ownership transfer of cash.

In a transaction where the Client purchases Currency Options, the transaction collateral (in the form of blockade of the agreed option premium amount on the Client's account on the transaction date or encumbrance of the treasury limit) is maintained until the correct settlement of the option premium.

In a transaction where the Client sells Currency Options, the transaction collateral (a margin or encumbrance of a treasury limit) is maintained until the correct settlement of the spot foreign exchange transaction resulting from the exercise of the Option.

The valuation of the Bank's exposure to the Client depends on changes in the market parameters specified in item 2 and may be subject to sudden changes. If the negative valuation exceeds the amount of the granted treasury limit and the margin established, the Client will be requested to replenish the collateral on the terms and conditions set forth in the Regulations. The amount needed to replenish the collateral may be significant in certain market conditions and constitute a significant burden for the Client. If case of a default on this obligation, the Bank will have the right, on the terms and conditions described in the Regulations, to an early closure and settlement of the Client's position and early termination of the contract. The settlement amount will become the Client's due and payable liability to the Bank.

**5. Information on impediments or restrictions for disinvestment, for example as may be the case for illiquid financial instruments or financial instruments with a fixed investment term, including an illustration of the possible exit methods and consequences of any exit, possible constraints and the estimated time frame for the sale of the financial instrument before recovering the initial costs of the transaction in that type of financial instruments**

The Client has the right to an early, full or partial closure of a Currency Option before the initially agreed exercise date only by concluding a closing transaction, that is a Currency Option on terms opposite to the terms of the transaction.

If the Client purchases a Currency Option, an opposite transaction involves the Client reselling a Currency Option with the same parameters in respect to the option type, option exercise rate and exercise date on the terms and conditions described in section I.II of this document. The nominal amount of the Option in the opposite transaction (resale transaction) may not exceed the nominal amount of the Option purchased by the Client.

In some cases, for example where the relationship between the Option exercise rate and the forward base currency to quoted currency exchange rate, irrespective of the elapse of time until the Option exercise date, indicates that the option has become an out-of-the-money option, the amount of the option premium received by the Client in connection with the closing transaction may be significantly lower than the option premium amount paid by the Client when purchasing the Option, i.e. the Client may not recover the option premium paid.

If the Client sells a Currency Option, an opposite transaction involves the Client repurchasing a Currency Option with the same parameters in respect to the option type, option exercise rate and exercise date, while the nominal amount of the Option in the opposite transaction (repurchase transaction) may not exceed the nominal amount of the Option sold by the Client.

In some cases, for example where the relationship between the Option exercise rate and the forward base currency to quoted currency exchange rate, irrespective of the elapse of time until the Option exercise date, indicates that the option has become an in-the-money option, the amount of the option premium paid by the Client in connection with the closing transaction may be significantly higher than the option premium amount received by the Client when selling the Option, i.e. the Client will incur a cost to close the transaction, which may constitute a significant burden for the Client.

In each case, the terms of the closing (opposite) transaction are agreed by the Parties to the transaction based on the market conditions in effect on the date the Client concludes the closing transaction, listed in detail in section I.II.2.

In each case, conclusion of a closing (opposite) transaction will entail an obligation on the part of the Option buyer to pay the agreed option premium amount. The Bank stipulates that once concluded, a Currency Option transaction cannot be cancelled and its parameters cannot be changed.

**6. Other risks.**

When entering into financial market transactions, the Client should also take into account other risks of legal, accounting, fiscal and operational nature that are independent of Bank Millennium.

With regard to currency option transactions, the Bank provides the service of executing orders to purchase or sell financial instruments to the Client's account, in accordance with Article 69 sect. 2 pt. 2 of the Act on Trading in Financial Instruments.

**II. INTEREST RATE RISK - GENERAL INFORMATION**

Like other market parameters, spot and forward interest rates can both rise and fall in line with changes occurring in the economy. The main factors influencing spot and forward interest rates are: the monetary policy pursued by the Central Bank, expectations as to future monetary policy developments, level of inflation, expectations as to future interest rates, the level of internal and external indebtedness of a country and other factors influencing the demand for money in the economy and the level of confidence in financial markets.

Any time a derivative interest rate transaction (FRA, IRS, CIRS) is concluded, changes in the spot and forward interest rates may have a significant positive or negative impact on the valuation of the financial instrument.

**III. FORWARD RATE AGREEMENT (FRA)**

**1. Identification of risks associated with that type of financial instrument including an explanation of leverage and its effects and the risk of losing the entire investment including the risks associated with insolvency of the issuer or related events, such as cancellation or conversion of debt.**

A forward rate agreement (FRA) is a transaction used to hedge the interest rate risk at an agreed future date. On the FRA transaction date, the parties agree on a fixed FRA rate at which they will settle the agreed nominal amount of FRA on a specified future date. The nominal FRA amount is only a reference used only to calculate interest payments for each of the parties to FRA.

The FRA buyer is the fixed rate payer in a given currency. The FRA rate agreed on the transaction date remains unchanged over the entire term of the transaction. The FRA buyer bears the risk that on the reference rate fixing date the variable reference rate will be lower than the FRA rate agreed when the transaction

was concluded. In such a case, the FRA buyer must expect a loss on the FRA period settlement date, resulting from the difference between the variable reference rate and the FRA rate, calculated on the nominal transaction amount for the FRA period.

The FRA seller is the variable reference rate payer in a given currency. The FRA rate agreed on the transaction date remains unchanged over the entire term of the transaction. The FRA seller bears the risk that on the reference rate fixing date the variable reference rate will be higher than the agreed FRA rate. In such a case, the FRA seller must expect a loss on the FRA period settlement date, resulting from the difference between the variable reference rate and the FRA exercise rate, calculated on the nominal transaction amount for the FRA period.

FRA transactions are carried out on the basis of a treasury limit or a margin, which are encumbered with the amount corresponding to the risk weights adopted by the Bank. In such a case, a FRA transaction is subject to a financial leverage mechanism. Relatively small changes in the level of spot and forward interest rates will have a significantly larger (positive or negative) impact on the valuation of the transaction.

**Example:**

In one month, a Company plans to take out a 9-month loan from its parent company in the amount of PLN 2,000,000, with a fixed nominal value over the entire lending period, on which interest will be charged on a quarterly basis, at a variable WIBOR 3M rate. Since the Company is expecting interest rates to rise, it makes a decision to hedge its interest rate risk over the entire lending period by buying a series of FRAs with the following parameters:

- FRA 1 x 4 – 4.29% p.a.
- FRA 4 x 7 – 4.34% p.a.
- FRA 7 x 10 – 4.58% p.a.

Currently, WIBOR 3M is at the level of 4.20% p.a.

The purchase of FRA 1 x 4 allows the Company to hedge the 3-month interest period starting in 1 month, the purchase of FRA 4 x 7 – the 3-month interest period starting in 4 months, and the purchase of FRA 7 x 10 – the 3-month interest period commencing in 7 months. In other words, by purchasing the series of FRAs, the Company may be certain that its interest expenses will amount to 4.29% p.a. in the first interest period, 4.34% p.a. in the second interest period and 4.58% p.a. in the third interest period, regardless of the actual level of the WIBOR 3M rate.

The FRA interest differential is settled on a quarterly basis, for each FRA separately. The interest differential on the 1 x 4 FRA will be settled within one month, the interest differential on the 4 x 7 FRA will be settled in four months, while the interest differential on the 7 x 10 FRA – in seven months. Since the hedged interest period is settled "in advance", the FRA interest differential is discounted to its present value. The reference rate level is set 2 business days before each 3-month interest period begins.

If the WIBOR 3M reference rate increases to 5.00% p.a. for the first FRA, the FRA interest differential amount will be due to the FRA buyer, i.e. the Company. The amount of the FRA interest differential will be calculated as  $(5.00\% \text{ p.a.} - 4.29\% \text{ p.a.}) * 2,000,000 * 90/365 = \text{PLN } 3501.37$ , discounted to present value at WIBOR 3M (5.00% p.a.) and paid to the Company's account in the amount of PLN 3,458.73.

The amount of interest on the loan will be calculated at WIBOR 3M, or 5.00% p.a., and transferred for repayment of the liability after the end of the interest period. The amount of the FRA interest differential paid out on as part of the settlement of FRA should compensate for the increase in WIBOR 3M from 4.29% p.a. (FRA rate) to 5.00% p.a.

Otherwise, if the WIBOR 3M reference rate drops to 3.60% p.a. for the first FRA, the FRA interest differential amount will be due to the FRA seller, i.e. the Bank. The FRA interest differential will be calculated as:  $(4.29\% \text{ p.a.} - 3.60\% \text{ p.a.}) * 2,000,000 * 90/365 = 3,402.74 \text{ PLN}$ .

The FRA interest differential will be discounted to present value at WIBOR 3M (3.60% p.a.) and charged to the Company's account in the amount of PLN 3,372.80. The amount of interest on the loan will be calculated at WIBOR 3M, or 3.60% p.a., and transferred for repayment of the liability after the end of the interest period. Interest differentials paid upon the settlement of the FRA are

supposed in a way to increase the cost of financing to 4.29% p.a.

The remaining two FRAs will be settled on the same principles.

The total cost of financing the liability is the combination of the FRA rate and the credit margin, if applicable. Please note that FRA only hedges changes in WIBOR without taking into account the credit margin.

Conclusion of FRAs entails the Bank's credit risk, i.e. risk of the Bank being unable to meet its obligations on time, including the risk of the Bank's bankruptcy. As a result of this risk, the Bank may fail to make payments to the Client arising out of the terms of concluded transactions.

The Bank stipulates that the Client's receivables arising out of the FRAs concluded on the basis of appropriate regulations are not covered by the protection measures within the meaning of the Act of 10 June 2016 on the Bank Guarantee Fund, the Deposit Guarantee Scheme and Mandatory Restructuring (the "BGF Act").

The Bank stipulates that the Bank's liabilities under the concluded FRA transactions may be subject to a debt cancellation or conversion measure according to the rules set forth in the BGF Act.

#### **2. Identification of the volatility of that type of financial instrument or limitations concerning the availability of the market for that type of financial instrument.**

The quotation of a FRA transaction at the time of its conclusion and the subsequent change of its market value are influenced by the following factors: the nominal amount and the currency of the transaction, current quotation of forward interest rates corresponding to the current length of the transaction and, in case of valuation of an existing transaction, additionally the agreed FRA rate.

The longer the transaction term, the higher the interest rate volatility and consequently the higher the risk of change in the value of the contract.

Additionally, before concluding a transaction, the Client should make sure that the given market is liquid and whether there are limitations as to technical possibilities of opening or closing the position (terms of placing orders to execute a transaction during the Bank's business hours). The Client should take into account the risk of reduction or lack of liquidity on the market, which may result in a less favorable price for the transaction being negotiated. These limitations may also prevent Bank Millennium from ensuring the possibility of concluding and executing transactions to purchase and sell a financial instrument at any moment chosen by the Client.

#### **3. Identification of the possibility that the Client might assume, as a result of transactions in that kind of financial instrument, financial commitments and other additional obligations, including contingent liabilities, additional to the cost of acquiring the financial instrument;**

Settlement of a FRA interest differential is a net settlement. The amount of the FRA interest differential is the difference between the variable reference rate for the given settlement period and the fixed FRA rate calculated on the nominal transaction amount for the given FRA period, discounted to the present value.

If the reference rate for a given settlement period is lower than the FRA exercise rate agreed on the transaction date then the settlement amount for the settlement period is due to the FRA seller.

If the reference rate for a given FRA period is higher than the FRA exercise rate agreed on the transaction date then the settlement amount is due to the FRA buyer.

Conclusion of a FRA transaction by the Client involves the Client incurring additional commitments associated with the requirement to maintain and replenish collateral in accordance with the terms and conditions set forth in the applicable regulations.

#### **4. Description of margin requirements or similar obligations applicable when investing in financial instruments of that type.**

FRA transactions are carried out on the basis of a treasury limit or a margin in the form of an ownership transfer of cash. Transaction collateral (a margin or encumbrance of a treasury limit) is maintained until the transaction is correctly settled.

The valuation of the Bank's exposure to the Client depends, among others, on changes in the level of spot

and forward interest rates and may be subject to sudden changes. If the negative valuation exceeds the amount of the granted treasury limit and the margin established, the Client will be requested to replenish the collateral on the terms and conditions set forth in the Regulations. The amount needed to replenish the collateral may be significant in certain market conditions and constitute a significant burden for the Client. If case of a default on this obligation, the Bank will have the right, on the terms and conditions described in the Regulations, to an early closure and settlement of the Client's position and early termination of the contract. The settlement amount will become the Client's due and payable liability to the Bank.

#### **5. Information on impediments or restrictions for disinvestment, for example as may be the case for illiquid financial instruments or financial instruments with a fixed investment term, including an illustration of the possible exit methods and consequences of any exit, possible constraints and the estimated time frame for the sale of the financial instrument before recovering the initial costs of the transaction in that type of financial instruments.**

The Client has the right to an early, full or partial closure of a FRA only by concluding a closing transaction, that is a FRA on terms opposite to the terms of the transaction. In each case, the terms of the closing transaction are agreed by the Parties to the transaction based on the current quotations of FRA rates in effect on the date the Client concludes the closing transaction.

##### **Example 1:**

Where the Client is a FRA buyer, conclusion of a closing (opposite) transaction means the sale of FRA by the Client for the originally agreed settlement date of the FRA period and with the same contractual settlement period of FRA.

If the FRA rate agreed for the closing transaction (i.e. the sale of FRA by the Client) is higher than the originally agreed FRA purchase rate, the Client closes the transaction with a profit calculated as the difference between the FRA rate in the Client's sale transaction and the FRA rate in the Client's purchase transaction for the FRA period, multiplied by the nominal amount of the FRA to be closed.

Otherwise, if the FRA rate agreed for the closing transaction (i.e. the sale of FRA by the Client) is lower than the originally agreed FRA purchase rate, the Client closes the transaction with a loss calculated as the difference between the FRA rate in the Client's purchase transaction and the FRA rate in the Client's sale transaction for the FRA period, multiplied by the nominal amount of the FRA to be closed.

In both cases, the FRA settlement amount is discounted to the FRA settlement date based on the rules described in the regulations.

##### **Example 2:**

In the case when the Client was a FRA seller, conclusion of a closing (opposite) transaction means the purchase of FRA by the Client for the originally agreed settlement date of the FRA period and with the same contractual settlement period of FRA.

If the FRA rate agreed for the closing transaction (i.e. the purchase of FRA by the Client) is lower than the originally agreed FRA sale rate, the Client closes the transaction with a profit calculated as the difference between the FRA rate in the Client's purchase transaction and the FRA rate in the Client's sale transaction for the FRA period, multiplied by the nominal amount of the FRA to be closed.

Otherwise, if the FRA rate agreed for the closing transaction (i.e. the purchase of FRA by the Client) is higher than the originally agreed FRA purchase rate, the Client closes the transaction with a loss calculated as the difference between the FRA rate in the Client's FRA purchase transaction and the FRA rate in the Client's FRA sale transaction for the FRA period, multiplied by the nominal amount of the FRA to be closed. In both cases, the FRA settlement amount is discounted to the FRA settlement date based on the rules described in the regulations.

The amount receivable or payable by the Client may be, by agreement of the Parties, subject to an early settlement by discounting it for the period from the originally agreed FRA settlement date to the date of the closing transaction. In such a case, it will become a due and payable liability of the Client or the Bank on that date.

The Bank stipulates that once concluded, a FRA transaction cannot be cancelled and its parameters cannot be changed.

#### **6. Other risks.**

When entering into transactions on the interest rate market, the Client should also take into account other risks of legal, accounting, fiscal and operational nature that are independent of Bank Millennium, including the risk related to the given benchmark unavailability and the possibility of determining an alternative benchmark, in accordance with applicable law, on the terms set out in the Regulations for concluding treasury transactions at Bank Millennium S.A..

## **II.II. INTEREST RATE SWAP (IRS)**

### **1. Identification of risks associated with that type of financial instrument including an explanation of leverage and its effects and the risk of losing the entire investment including the risks associated with insolvency of the issuer or related events, such as cancellation or conversion of debt.**

An interest rate swap transaction (otherwise known as an IRS or Interest Rate Swap) is, in its simplest case, a combination of two or more FRA contracts.

Economically, it is an agreement between parties to make periodic interest payments on specified future dates on a predetermined principal amount. Therefore, the nominal IRS amount is, as in the case of FRAs, just a reference and is used solely to calculate interest payments.

The payer of the IRS rate, otherwise known as the swap rate (fixed or variable), is referred to as the IRS buyer. The swap rate agreed on the transaction date remains unchanged over the entire term of the transaction. The IRS buyer bears the risk that, over the entire transaction period or its part, the variable reference rate falls below the agreed swap rate level. In such a case, the IRS buyer must expect a loss in a given settlement period, resulting from the difference between the variable reference rate and the swap rate calculated on the nominal transaction amount.

The payer of the variable reference rate is referred to as the IRS seller. The swap rate agreed on the transaction date remains unchanged over the entire term of the transaction. The IRS seller bears the risk that, over the entire transaction period or its part, the variable reference rate increases above the agreed swap rate level. In such a case, the IRS seller must consider the possibility of incurring a loss in the settlement period, resulting from the difference between the variable reference rate and the swap rate calculated on the nominal value of the transaction.

##### **Example**

On 1 January 2010, the Company took out a loan, under which it pays monthly interest based on a variable interest rate depending on the level of one-month WIBOR (WIBOR 1M) rate. The amount of the loan is PLN 20,000,000, and WIBOR 1M at the time of signing the loan agreement is at the level of 4.00% p.a. At such interest rate levels, the monthly interest expense for the Company, assuming 31 calendar days per month, will be, rounded off, PLN 67,945.21 (20,000,000 \* 4.00% \* 31/365). Due to the fact that market interest rates may change over the lending period, the amount of the Company's monthly interest charges, measured in PLN, may be as follows:

- If the WIBOR 1M rate rises, the Company's interest expense, measured in PLN, will be higher. For example, at the WIBOR 1M rate of 5.00% p.a., the Company's monthly interest expense, assuming 31 calendar days per month, would amount to PLN 84,931.51;
- If the WIBOR 1M rate falls, the Company's interest expense, measured in PLN, will be lower. For example, at the WIBOR 1M rate of 3.50% p.a., the Company's monthly interest expense, assuming 31 calendar days per month, would amount to roughly PLN 59,452.05.

To hedge against interest rate increases, the Company may enter into an IRS transaction with the Bank in which the Client undertakes to pay interest based on a fixed interest rate set when the transaction is concluded, for example 4.00% p.a., while the Bank undertakes to pay interest based on a variable interest rate (reference rate) – WIBOR 1M. On the transaction date, the parties agree on the reference rate observation dates and the settlement dates, where settlement is the swap of interest payments. Usually, the interest payment swap dates fall two business days after the reference rate is determined.

A single interest payment under IRS will be settled as follows, depending on the level of the reference rate:

- Case 1 – WIBOR 1M reference rate of 5.00% p.a., 31 calendar days per month. Since the fixed interest

rate (4.00% p.a.) in the IRS is lower than the reference rate (5.00% p.a.), the Bank will credit the Company's account with the amount equal to the difference between the reference rate and the IRS rate multiplied by the nominal value of the transaction for a given interest period, i.e.  $(5.00\% - 4.00\%) \times 20,000,000 \times 31/365 = \text{PLN } 16,986.30$ .

- Case 2 – WIBOR 1M reference rate of 3.00% p.a., 31 calendar days per month. Since the fixed interest rate (4.00% p.a.) in the IRS is higher than the reference rate (3.00% p.a.), the Bank will charge the Company's account with the amount equal to the difference between the IRS rate and the reference rate multiplied by the nominal value of the transaction for a given interest period, i.e.  $(4.00\% - 3.00\%) \times 20,000,000 \times 31/365 = \text{PLN } 16,986.30$ .

As the above example shows, the fixed IRS rate determines the maximum interest expense for the Company in the period when the transaction was concluded.

IRS transactions are executed on the basis of a treasury limit or a margin in the form of an ownership transfer of cash, which are encumbered with the amount corresponding to the risk weights adopted by the Bank. In such a case, an IRS transaction is subject to a financial leverage mechanism. Relatively small changes in the level of spot and forward interest rates will have a significantly larger (positive or negative) impact on the valuation of the transaction.

Conclusion of Interest Rate Swap Transactions entails the Bank's credit risk, i.e. risk of the Bank being unable to meet its obligations on time, including the risk of the Bank's bankruptcy. As a result of this risk, the Bank may fail to make payments to the Client arising out of the terms of concluded transactions.

The Bank stipulates that the Client's receivables arising out of the Interest Rate Swap Transactions (IRSs) concluded on the basis of appropriate regulations are not covered by the protection measures within the meaning of the Act of 10 June 2016 on the Bank Guarantee Fund, the Deposit Guarantee Scheme and Mandatory Restructuring (the "BGF Act").

The Bank stipulates that the Bank's liabilities under Interest Rate Swap Transactions (IRS) concluded under relevant regulations may, where the conditions prescribed by law are satisfied, be subject to a debt cancellation or conversion measure according to the rules set forth in the BGF Act.

#### 2. Identification of the volatility of that type of financial instrument or limitations concerning the availability of the market for that type of financial instrument.

The quotation of an IRS transaction at the time of its conclusion and the subsequent change in its market value are influenced by the current quotations of the following market parameters:

- transaction party (IRS purchase/sale),
- IRS nominal amount and currency,
- IRS length,
- current quotation of short-term interest rates (up to 1 year) in a given currency,
- current quotation of swap rates in a given currency for the date corresponding to the current transaction length,
- amortization schedule of the swap transaction,
- frequency of interest payment swaps,
- reference rate level,
- interest basis for the reference rate,
- interest basis for the swap rate.

Where a pending transaction is valued, the valuation is additionally influenced by the agreed IRS rate level.

The longer the transaction settlement period, the higher the interest rate volatility and consequently the higher the risk of change in the value of the contract.

Additionally, before concluding a transaction, the Client should make sure that the given market is liquid and whether there are limitations as to technical possibilities of opening or closing the position (terms of placing orders to execute a transaction during the Bank's business hours).

The Client should take into account the risk of reduction or lack of liquidity on the market, which may result in a less favorable price for the transaction being negotiated. These limitations may also prevent Bank Millennium from ensuring the possibility of concluding and executing transactions to purchase and sell a financial instrument at any moment chosen by the Client.

#### 3. Identification of the possibility that the Client might assume, as a result of transactions in that kind of financial instrument, financial commitments and other additional obligations, including contingent liabilities, additional to the cost of acquiring the financial instrument;

If an IRS transaction is settled in a given settlement period, all the settlements will be made on a net basis. The settlement amount is the difference between the variable reference rate for the given settlement period and the fixed swap rate calculated on the nominal transaction amount for the given settlement period. If the reference rate for a given settlement period is higher than the agreed swap rate then the settlement amount for the settlement period is due to the IRS Buyer. If the reference rate for a given settlement period is lower than the agreed swap rate then the settlement amount is due to the IRS Seller.

Conclusion of an IRS transaction by the Client involves the Client incurring additional commitments associated with the requirement to maintain and replenish collateral in accordance with the terms and conditions set forth in the applicable regulations.

#### 4. Description of margin requirements or similar obligations applicable when investing in financial instruments of that type.

IRS transactions are carried out on the basis of a treasury limit or a margin in the form of an ownership transfer of cash. Transaction collateral (a margin or encumbrance of a treasury limit) is maintained until the transaction is correctly settled.

The valuation of the Bank's exposure to the Client depends, among others, on changes in the level of spot and forward interest rates and may be subject to sudden changes. If the negative valuation exceeds the amount of the granted treasury limit and the margin established, the Client will be requested to replenish the collateral on the terms and conditions set forth in the Regulations. The amount needed to replenish the collateral may be significant in certain market conditions and constitute a significant burden for the Client. In case of a default on this obligation, the Bank will have the right, on the terms and conditions described in the Regulations, to an early closure and settlement of the Client's position and early termination of the contract. The settlement amount will become the Client's due and payable liability to the Bank.

#### 5. Information on impediments or restrictions for disinvestment, for example as may be the case for illiquid financial instruments or financial instruments with a fixed investment term, including an illustration of the possible exit methods and consequences of any exit, possible constraints and the estimated time frame for the sale of the financial instrument before recovering the initial costs of the transaction in that type of financial instruments.

The Client has the right to an early, full or partial closure and settlement of IRS transactions by offsetting mutual non-matured liabilities of the parties, i.e. by agreeing with the Bank and settling the IRS settlement amount.

The Bank is the calculating agent for the IRS settlement amount. The settlement amount is calculated based on the current valuation of the IRS transaction affected by the factors described in item II.II.2. Based on those factors, the Bank compares the present value of future liabilities of the payer of the IRS rate (fixed or variable) with the present value of future liabilities of the payer of the reference rate.

The IRS settlement amount is paid by the party, which has the higher value of future liabilities. This amount becomes due and payable on the agreed date of payment of the IRS settlement amount.

##### Example 1:

In an IRS transaction, if the Client is the fixed IRS rate payer and the present value of future liabilities calculated at the agreed IRS rate (the Client's liability) is higher than the present value of future liabilities calculated at the reference rate (the Bank's liability) then the Client is the party obliged to pay the IRS settlement amount. Otherwise, if the present value of future liabilities calculated at the agreed IRS rate (the Client's liability) is lower than the present value of future liabilities calculated at the reference rate (the Bank's liability) then the Bank is the party obliged to pay the IRS settlement amount.

##### Example 2:

In an IRS transaction, if the Bank is the fixed IRS rate payer and the present value of future liabilities calculated

at the agreed IRS rate (the Bank's liability) is higher than the present value of future liabilities calculated at the reference rate (the Client's liability) then the Bank is the party obliged to pay the IRS settlement amount.

Otherwise, if the present value of future liabilities calculated at the agreed IRS rate (the Bank's liability) is lower than the present value of future liabilities calculated at the reference rate (the Client's liability) then the Client is the party obliged to pay the IRS settlement amount.

The Bank reserves the right to adjust the IRS settlement amount by the amount of costs incurred to close the transaction on the interbank market (cost-to-close).

The Bank stipulates that once concluded, a transaction cannot be cancelled and its parameters cannot be changed.

#### 6. Other risks.

When entering into transactions on the interest rate market, the Client should also take into account other risks of legal, accounting, fiscal and operational nature that are independent of Bank Millennium, including the risk related to the given benchmark unavailability and the possibility of determining an alternative benchmark, in accordance with applicable law, on the terms set out in the Regulations for concluding treasury transactions at Bank Millennium S.A..

### II.III. CURRENCY INTEREST RATE SWAP (CIRS)

#### 1. Identification of risks associated with that type of financial instrument including an explanation of leverage and its effects and the risk of losing the entire investment including the risks associated with insolvency of the issuer or related events, such as cancellation or conversion of debt.

A Currency Interest Rate Swap (also known as the Currency Interest Rate Swap, CIRS or CCIRS) is an off-balance sheet swap of a loan denominated in one currency indexed to a fixed or variable interest rate, for a liability in another currency indexed to a fixed or variable interest rate.

Eight basic risk profiles can be distinguished in a CIRS transaction, depending on the direction of the transaction:

- **Swap of a loan in the base currency indexed to a variable interest rate in the base currency for a loan in the quoted currency indexed to a fixed interest rate in the quoted currency.** In this case, the Client bears: the risk of the base currency weakening versus the quoted currency as compared to the final exchange rate agreed in the CIRS (currency exchange rate risk), the risk of the interest rate falling in the base currency and the risk of the interest rate falling in the quoted currency (interest rate risk).
- **Swap of a loan in the base currency indexed to a variable interest rate in the base currency for a loan in the quoted currency indexed to a variable interest rate in the quoted currency.** In this case, the Client bears: the risk of the base currency weakening versus the quoted currency as compared to the agreed final exchange rate (currency exchange rate risk), the risk of the interest rate falling in the base currency and the risk of the interest rate increasing in the quoted currency (interest rate risk).
- **Swap of a loan in the base currency indexed to a fixed interest rate in the base currency for a loan in the quoted currency indexed to a fixed interest rate in the quoted currency.** In this case, the Client bears: the risk of the base currency weakening versus the quoted currency as compared to the final exchange rate agreed in the CIRS (currency exchange rate risk), the risk of the interest rate rising in the base currency and the risk of the interest rate falling in the quoted currency (interest rate risk).
- **Swap of a loan in the base currency indexed to a fixed interest rate in the base currency for a loan in the quoted currency indexed to a variable interest rate in the quoted currency.** In this case, the Client bears: the risk of the base currency weakening versus the quoted currency as compared to the final exchange rate agreed in the CIRS (currency exchange rate risk), the risk of the interest rate rising in the base currency and the risk of the interest rate rising in the quoted currency (interest rate risk).
- **Swap of a loan in the quoted currency indexed to a variable interest rate in the quoted currency for a loan in the base currency indexed to a fixed interest rate in the base currency.** In this case, the

Client bears: the risk of the base currency strengthening versus the quoted currency as compared to the final exchange rate agreed in the CIRS (currency exchange rate risk), the risk of the interest rate falling in the quoted currency and the risk of the interest rate falling in the base currency (interest rate risk).

- **Swap of a loan in the quoted currency indexed to a variable interest rate in the quoted currency for a base currency loan indexed to a variable interest rate in the base currency.** In this case, the Client bears: the risk of the base currency strengthening versus the quoted currency as compared to the final exchange rate agreed in the CIRS (currency exchange rate risk), the risk of the interest rate falling in the quoted currency and the risk of the interest rate rising in the base currency (interest rate risk).
- **Swap of a loan in the quoted currency indexed to a fixed interest rate in the quoted currency for a loan in the base currency indexed to a fixed interest rate in the base currency.** In this case, the Client bears: the risk of the base currency strengthening versus the quoted currency as compared to the final exchange rate agreed in the CIRS (currency exchange rate risk), the risk of the interest rate rising in the quoted currency and the risk of the interest rate falling in the base currency (interest rate risk).
- **Swap of a loan in the quoted currency indexed to a fixed interest rate in the quoted currency for a loan in the base currency indexed to a variable interest rate in the base currency.** In this case, the Client bears: the risk of the base currency strengthening versus the quoted currency as compared to the final exchange rate agreed in the CIRS (currency exchange rate risk), the risk of the interest rate rising in the quoted currency and the risk of the interest rate rising in the base currency (interest rate risk).

The initial and final CIRS exchange rates and the swap rates (floating or fixed interest rates) agreed when the transaction is concluded remain unchanged throughout the entire term of the transaction.

CIRS transactions are executed on the basis of a treasury limit or a margin in the form of an ownership transfer of cash, which are encumbered with the amount corresponding to the risk weights adopted by the Bank. In such a case, a CIRS transaction is subject to a financial leverage mechanism. Relatively small changes of the exchange rate and in the level of spot and forward interest rates will have a significantly larger (positive or negative) impact on the valuation of the Client's exposure.

#### Example:

The company took out a five-year investment loan of EUR 3,000,000 at the variable rate of EURIBOR 1M, with an intention to finance the interest expenses and the loan installments from export proceeds. EUR 1,000,000 remained outstanding (for one-off repayment in the full amount at the end of the lending period), maturing in 2 years. During the lending period however the Company changed the currency of its revenues from EUR to PLN, leaving a credit liability in EUR would expose the Company to the risk of increasing EUR/PLN exchange rate and the risk of increasing interest rates in EUR. In order to adjust the currency of the liability to the currency of income and at the same time secure the risk of interest rate increases in PLN, on 01.01.2010 the Company concluded a CIRS transaction with the Bank with the following parameters:

- Nominal amount in the base currency: EUR 1,000,000
- Nominal amount in the quoted currency: PLN 4,000,000
- Final CIRS exchange rate: EUR/PLN 4.00
- No initial swap of nominal amounts
- No amortization of the nominal amount
- CIRS maturity date: 31 December 2012
- Variable interest rate in the base currency: EURIBOR 1M + 1.50%.
- Interest basis for the interest rate in the base currency: act/360
- Variable rate payer in the base currency: Bank
- Fixed rate in the quoted currency in PLN: 4.70% p.a.
- Interest basis for the interest rate in the quoted currency: act/365
- Fixed rate payer in the quoted currency: Company
- Contractual length of the interest period: one month.

CIRS parameters have been selected in such a way as to reflect as fully as possible the parameters of the loan. Since the CIRS was concluded during the term of the

loan, there is no initial swap of nominal amounts. The parties swap nominal amounts of the CIRS – the Company buys EUR 1,000,000 at the 4.00 exchange rate – only upon maturity of the CIRS. Through the final swap of nominal amounts of the CIRS, the Company secured the exchange rate at which it would purchase EUR to repay the loan liability in 2 years at the level of 4.00.

In the successive monthly interest periods, the Bank and the Client swap their interest payments:

- the Client pays interest in PLN accruing on the nominal amount of PLN 4,000,000, at the fixed rate of 4.70% p.a. (act/365)
- the Bank pays interest in EUR accruing on the nominal amount of EUR 1,000,000, at the variable rate of EURIBOR 1M + 1.50% (act/360)

Assuming that the parameters of the CIRS fully reflect the parameters of the loan obligation (in particular: the nominal amount of the CIRS, the length of interest periods, the level and date of determining the interest rate in the base currency), the cash flows in EUR to the Company's account under CIRS will equal the cash flows arising from the interest liability in EUR that the Company transfers to the lending bank. In the example above, the credit margin on the EURIBOR 1M rate was also "swapped".

If the EUR/PLN exchange rate is higher than 4.00 on the loan repayment date (which is the same as the CIRS maturity date), the Company will recognize foreign exchange gains equal to the difference between the current rate and the final swap rate under CIRS, multiplied by the nominal amount of the CIRS. If the EUR/PLN exchange rate drops below 4.00 on the loan repayment date (which is the same as the CIRS maturity date), the Company will recognize foreign exchange losses equal to the difference between the final swap rate under CIRS and the current exchange rate, multiplied by the nominal amount of the CIRS.

If, in a given interest period during the term of the CIRS, the PLN interest rate remains above the level of 4.70% p.a. then the Company will recognize a positive interest differential in PLN in the interest period. If, during the term of the CIRS, the PLN interest rate remains below 4.70% p.a. then the Company will recognize a negative interest differential in PLN in the interest period.

Since the interest in EUR that the Client receives under the CIRS is accrued based on a variable interest rate, this income is not sensitive to the risk of the EUR interest rate. A possible rise in EURIBOR 1M results in an increase in interest income under CIRS and, at the same time, an increase in interest liability under the loan. A decrease in EURIBOR 1M results in a decrease in interest income under CIRS and at the same time a decrease in interest liability under the loan.

Interest payments resulting from a CIRS transactions may be settled on a net basis, without currency delivery. In such a case, the Company should translate the interest income amount from EUR to PLN at the current exchange rate.

It should be noted that conclusion of a CIRS does not amend the loan agreement in any way, so the transaction may be concluded with a Bank other than the lending bank.

Conclusion of Currency Interest Rate Swap Transactions entails the Bank's credit risk, i.e. risk of the Bank being unable to meet its obligations on time, including the risk of the Bank's bankruptcy. As a result of this risk, the Bank may fail to make payments to the Client arising out of the terms of concluded transactions.

The Bank stipulates that the Client's receivables arising out of the Currency Interest Rate Swap Transactions concluded on the basis of appropriate regulations are not covered by the protection measures within the meaning of the Act of 10 June 2016 on the Bank Guarantee Fund, the Deposit Guarantee Scheme and Mandatory Restructuring (the "BGF Act").

The Bank stipulates that the Bank's liabilities under Currency Interest Rate Swap Transactions concluded under relevant regulations may, where the conditions prescribed by law are satisfied, be subject to a debt cancellation or conversion measure according to the rules set forth in the BGF Act.

## 2. Identification of the volatility of that type of financial instrument or limitations concerning the availability of the market for that type of financial instrument.

The quotation of a CIRS transaction at the time of its conclusion is affected by the following market parameters:

- party to the transaction (base currency rate payer/quoted currency rate payer),
- nominal amount and currency,
- initial and final swap rate/rates for the nominal amount (base currency to quoted currency exchange rate),
- length of the transaction,
- current quotation of short-term interest rates (up to 1 year) for each transaction currency,
- current quotation of IRS rates for each transaction currency for the date corresponding to the current transaction length,
- schedule of changes in the nominal amount,
- contractual length of the interest period,
- variable interest rate in the base currency agreed in CIRS (variable/fixed),
- variable interest rate in the quoted currency agreed in CIRS (variable/fixed),
- interest basis for the interest rate in the base currency,
- interest basis for the interest rate in the quoted currency,

Where an existing CIRS is valued, the subsequent change of its market value is most significantly affected by the current level of the base currency to quoted currency exchange rate. In addition, the valuation of transactions is affected by changes in spot and forward interest rates in the base currency and the quoted currency. Therefore, the Client must take into account a possibility of a loss in a settlement period resulting from changes in both these parameters: the exchange rate or the interest rates.

Before concluding a transaction, the Client should make sure that the given market is liquid and whether there are limitations as to technical possibilities of opening or closing the position during the Bank's business hours. The Client should take into account the risk of reduction or lack of liquidity on the market, which may result in a less favorable price for the transaction being negotiated. These limitations may also prevent Bank Millennium from ensuring the possibility of concluding and closing early the CIRS transaction at any moment chosen by the Client.

## 3. Identification of the possibility that the Client might assume, as a result of transactions in that kind of financial instrument, financial commitments and other additional obligations, including contingent liabilities, additional to the cost of acquiring the financial instrument;

Settlement of an interest period under CIRS may take the form of currency delivery or differential settlements.

In case of a differential settlement, the Client will be obliged to perform a currency conversion of the amounts resulting from the swap of interest payments or from the schedule of changes in the nominal amount of the CIRS, unless the Parties resolve otherwise in the agreement. The settlement amount of an interest period is the difference between: the interest amount calculated using the variable/fixed interest rate in the base currency on the nominal amount in the base currency, for that interest period, translated into the quoted currency, and the interest amount calculated using the variable/fixed interest rate in the quoted currency on the nominal amount in the quoted currency, for that interest period.

Conclusion of a CIRS transaction by the Client involves the Client incurring additional commitments associated with the requirement to maintain and replenish collateral in accordance with the terms and conditions set forth in the applicable regulations.

## 4. Description of margin requirements or similar obligations applicable when investing in financial instruments of that type.

CIRS transactions are carried out on the basis of a treasury limit or a margin in the form of an ownership transfer of cash. Transaction collateral (a margin or encumbrance of a treasury limit) is maintained until the transaction is correctly settled.

The valuation of the Bank's exposure to the Client depends, among others, on changes in the exchange rate and the level of spot and forward interest rates and may be subject to sudden changes. If the negative valuation exceeds the amount of the granted treasury limit and the margin established, the Client will be requested to replenish the collateral on the terms and conditions set forth in the Regulations. The amount needed to replenish the collateral may be significant in certain market conditions and constitute a significant

burden for the Client. If case of a default on this obligation, the Bank will have the right, on the terms and conditions described in the Regulations, to an early closure and settlement of the Client's position and early termination of the contract. The settlement amount will become the Client's due and payable liability to the Bank.

**5. Information on impediments or restrictions for disinvestment, for example as may be the case for illiquid financial instruments or financial instruments with a fixed investment term, including an illustration of the possible exit methods and consequences of any exit, possible constraints and the estimated time frame for the sale of the financial instrument before recovering the initial costs of the transaction in that type of financial instruments.**

The Client has the right to an early, full or partial closure and settlement of CIRS transactions by offsetting mutual non-matured liabilities of the parties in the base currency and in the quoted currency, i.e. by agreeing with the Bank and settling the CIRS settlement amount.

The Bank is the calculating agent for the CIRS settlement amount. The settlement amount is calculated based on the current valuation of the CIRS transaction affected by the factors described in item II.III.2. Based on those factors, the Bank compares the present value of future liabilities (interest and amounts related to the swap of nominal amounts) of the payer of the CIRS rate in the base currency with the present value of future liabilities (interest and amounts related to the swap of nominal amounts) of the payer of the CIRS rate in the quoted currency. The present value of the future liabilities of the payer of the interest rate in the base currency is translated into the quoted currency based on the current (spot) exchange rate.

The CIRS settlement amount is paid by the party, which has the higher value of future liabilities expressed in the quoted currency. This amount becomes due and payable on the agreed date of payment of the CIRS settlement amount.

**Example 1:**

In a CIRS transaction, if the Client is the payer of the fixed rate in the base currency (e.g. EURIBOR) and the present value of future liabilities calculated at the interest rate in the base currency (including the swap of the nominal amounts of the CIRS) is greater than the present value of future liabilities calculated at the interest rate in the quoted currency (including the swap of the nominal amounts of the CIRS) then the Client is the party obliged to pay the CIRS settlement amount.

Otherwise, if the present value of future liabilities calculated at the interest rate in the base currency (including the swap of the nominal amounts of the CIRS) is lower than the present value of future liabilities calculated at the interest rate in the quoted currency (including the swap of the nominal amounts of the CIRS) then the Bank is the party obliged to pay the CIRS settlement amount.

**Example 2:**

In a CIRS transaction, if the Bank is the payer of the fixed rate in the base currency (e.g. EURIBOR) and the present value of future liabilities calculated at the interest rate in the base currency (including the swap of the nominal amounts of the CIRS) is greater than the present value of future liabilities calculated at the interest rate in the quoted currency (including the swap of the nominal amounts of the CIRS) then the Bank is the party obliged to pay the CIRS settlement amount.

Otherwise, if the present value of future liabilities calculated at the interest rate in the base currency (including the swap of the nominal amounts of the CIRS) is lower than the present value of future liabilities calculated at the interest rate in the quoted currency (including the swap of the nominal amounts of the CIRS) then the Client is the party obliged to pay the CIRS settlement amount.

The Bank reserves the right to adjust the CIRS settlement amount by the amount of costs incurred in connection with closing transactions on the interbank market (cost-to-close).

The Bank stipulates that once concluded, a transaction cannot be cancelled and its parameters cannot be changed.

**6. Other risks.**

When entering into transactions on the interest rate and currency markets, the Client should also take into account other risks of legal, accounting, fiscal and operational nature that are independent of Bank Millennium, including the risk related to the given benchmark unavailability and the possibility of

determining an alternative benchmark, in accordance with applicable law, on the terms set out in the Regulations for concluding treasury transactions at Bank Millennium S.A.

With regard to forward rate agreements (FRA), interest rate swaps (IRS) and currency interest rate swaps (CIRS), the Bank provides the service of executing orders to purchase or sell financial instruments on the Client's account, in accordance with Article 69 sect. 2 pt. 2 of the Act on Trading in Financial Instruments.

**II.IV. INTEREST RATE OPTIONS**

**1. Identification of risks associated with that type of financial instrument including an explanation of leverage and its effects and the risk of losing the entire investment including the risks associated with insolvency of the issuer or related events, such as cancellation or conversion of debt.**

Option instruments – Cap Options and Floor Options – are also used on the interest rate market as well as they are on the currency market. They are comparable to the Call Options and Put Options available on the currency market. A combination of these two Options, in which one Option is bought and the other sold, is called a Collar.

A Cap Option is a financial instrument that reduces the risk of increasing interest rates. The seller (or issuer) of a Cap Option guarantees that it will refund to the Option buyer the differences resulting from an increase in market interest rates: the difference between the upper limit of the interest rate as agreed in the contract (Cap exercise rate) and the market interest rate. Accordingly, the maximum actual financing cost will not exceed the base rate agreed in the option contract and the lender's margin. This way, a Cap Option buyer hedges against an increase in interest rates, while retaining the possibility of taking advantage of a possible decrease in their level. For the purchase of such rights, the buyer pays a premium to the seller within two working days of the transaction date.

A Floor Option is a financial instrument that reduces the risk of decreasing interest rates. The Floor Option seller guarantees that it will refund to the Option buyer the differences resulting from a decrease in market interest rates below the level stated in the Option – the difference between the lower limit of the interest rate as agreed in the contract (Floor exercise rate) and the market interest rate. Accordingly, the minimum actual return on investment cannot be lower than the base rate specified in the option contract. This way, a Floor Option buyer hedges against a decrease in interest rates, while retaining the possibility of taking advantage of a possible increase in their level. The Option buyer pays an option premium to the Option seller for this possibility.

The market risk profile resulting from an option transaction is asymmetrical for the Option buyer and the Option seller. The risk of the Option buyer is limited to the amount of the option premium paid. Contrary to the Option buyer, the Option seller bears an unlimited risk.

The reference rate for Cap and Floor transactions are the official rates published on the interbank market (WIBOR for PLN, EURIBOR for EUR LIBOR for USD, and for other currencies – reference rates appropriate for that currency).

**Example:**

On 1 January 2010, the Company took out a loan, under which it pays monthly interest based on a variable interest rate depending on the level of one-month WIBOR (WIBOR 1M) rate. The amount of the loan is PLN 1,000,000 and WIBOR 1M at the time of signing the loan agreement is at the level of 5.00% p.a. At such quotation levels, the monthly interest expense for the Company will be, rounded off, PLN 4,166.66 (1,000,000 x 5.00%/12). Due to the fact that market interest rates may change over the lending period, the amount of the Company's monthly interest charges, measured in PLN, may be as follows:

- If the WIBOR 1M rate increases, the Company's interest expense, measured in PLN, will be higher. For example, at the WIBOR 1M rate of 6.00% p.a., the Company's monthly interest expense would amount to PLN 5,000.
- If the WIBOR 1M rate falls, the Company's interest expense, measured in PLN, will be lower. For example, at the WIBOR 1M rate of 4.00% p.a., the Company's monthly interest expense would amount to roughly PLN 3333.33.

To hedge against interest rate increases, the Company may purchase a Cap Option settled at WIBOR 1M, with a nominal amount equal to the loan principal amount. On the transaction date, the parties set the Option exercise rate (let us assume 5.00%). The Company pays an option premium for the purchase of the Option. On the Option exercise date, the Option exercise rate will be compared to the reference rate, i.e. WIBOR 1M. The settlement of the Option, depending on the reference rate level, may be as follows:

- If WIBOR 1M is at the level of 6.00% p.a. then the Company will exercise the Cap option – the Bank will credit the Company's account with the amount resulting from the difference between the Option exercise rate and the reference rate, multiplied by the nominal amount of the transaction and adjusted by the time factor, or (6.00% - 5.00%) x 12 x 1,000,000 = 8333.33 PLN. This amount will compensate the Company for the loss resulting from the increased cost of financing.
- If WIBOR 1M is at the level of 4.00%, the Company will not exercise the Cap Option and will pay interest at the market rate of WIBOR 1M.

As the above example shows, the Option exercise rate determines the maximum interest expense for the Company in the period when the transaction was concluded. This expense should be additionally adjusted for the cost of the option premium paid by the Company when the transaction was concluded.

Interest rate options are leveraged. As a result of the leverage, even the smallest movements in market prices affecting the valuation of Options may have a significant influence on the valuation of the whole transaction.

Conclusion of Interest Rate Options entails the Bank's credit risk, i.e. risk of the Bank being unable to meet its obligations on time, including the risk of the Bank's bankruptcy. As a result of this risk, the Bank may fail to make payments to the Client arising out of the terms of concluded transactions.

The Bank stipulates that the Client's receivables arising out of the Interest Rate Options concluded on the basis of appropriate regulations are not covered by the protection measures within the meaning of the Act of 10 June 2016 on the Bank Guarantee Fund, the Deposit Guarantee Scheme and Mandatory Restructuring (the "BGF Act").

The Bank stipulates that the Bank's liabilities under Interest Rate Option transactions concluded under relevant regulations may, where the conditions prescribed by law are satisfied, be subject to a debt cancellation or conversion measure according to the rules set forth in the BGF Act.

**2. Identification of the volatility of that type of financial instrument or limitations concerning the availability of the market for that type of financial instrument.**

The price of an Interest Rate Option (the option premium amount) at the time of concluding the transaction and the change in its theoretical value during the transaction are affected by the following market parameters:

- The relationship between the current interest rate level and the Option exercise rate,
- Implied volatility of interest rates quoted on the market. Implied volatility is based on the expectations of the market participants as to the future level of volatility and may differ from the actually recorded historical volatility. Both the Cap Option price and the Floor Option price increase directly in proportion to the increase in implied volatility.
- Length of the option transaction / time remaining until the Option exercise date – the price of both the Cap Option and the Floor Option increases in direct proportion to the increase in transaction length.

Before concluding a transaction, the Client should make sure that the given market is liquid and whether there are limitations as to technical possibilities of opening or closing the option position.

The Client should take into account the risk of reduction or lack of liquidity on the financial market, which may result in a less favorable price for the transaction being negotiated. There may be limited availability of the market for Interest Rate Option transactions, which may affect their price. These limitations may in particular prevent Bank Millennium from ensuring the possibility of concluding and executing transactions to purchase and

sell a financial instrument at any moment chosen by the Client.

**3. Identification of the possibility that the Client might assume, as a result of transactions in that kind of financial instrument, financial commitments and other additional obligations, including contingent liabilities, additional to the cost of acquiring the financial instrument;**

If an Interest Rate Option transaction is settled in a given settlement period, all the settlements will be made on a net basis. The settlement amount is the difference between the variable reference rate for the given settlement period and the fixed Option exercise date calculated on the nominal transaction amount for the given settlement period. If the reference rate for a given settlement period is higher than the agreed Cap rate then the settlement amount for the settlement period is due to the Cap buyer. If the reference rate for a given settlement period is lower than the agreed Floor rate then the settlement amount is due to the Floor buyer.

Conclusion of an interest rate option sale transaction by the Client involves the Client incurring additional commitments associated with the requirement to maintain and replenish collateral in accordance with the terms and conditions set forth in the applicable regulations.

**4. Description of margin requirements or similar obligations applicable when investing in financial instruments of that type.**

Interest Rate Option transactions are carried out on the basis of a treasury limit or a margin in the form of an ownership transfer of cash. In a transaction where the Client purchases Interest Rate Options, the transaction collateral (blockade of the agreed Option Premium amount on the Client's account on the transaction date or encumbrance of the treasury limit) is maintained until the correct settlement of the option premium. In a transaction where the Client sells Options, the transaction collateral (a margin or encumbrance of a treasury limit) is maintained until the correct settlement of the transaction resulting from the exercise of the Option.

The valuation of the Bank's exposure to the Client depends, among others, on changes in the level of interest rates and may be subject to sudden changes. If the negative valuation exceeds the amount of the granted treasury limit and the margin established, the Client will be requested to replenish the collateral on the terms and conditions set forth in the Regulations. The amount needed to replenish the collateral may be significant in certain market conditions and constitute a significant burden for the Client. In case of a default on this obligation, the Bank will have the right, on the terms and conditions described in the Regulations, to an early closure and settlement of the Client's position and early termination of the contract. The settlement amount will become the Client's due and payable liability to the Bank.

**5. Information on impediments or restrictions for divestment, for example as may be the case for illiquid financial instruments or financial instruments with a fixed investment term, including an illustration of the possible exit methods and consequences of any exit, possible constraints and the estimated time frame for the sale of the financial instrument before recovering the initial costs of the transaction in that type of financial instruments**

The Client has the right to an early, full or partial closure of an Interest Rate Option before the initially agreed exercise date only by concluding a closing transaction, that is an Interest Rate Option on terms opposite to the terms of the transaction.

If the Client purchases an Interest Rate Option, an opposite transaction involves the Client reselling an Interest Rate Option with the same parameters in respect to: the Option type, option exercise rate and exercise date, while the nominal amount of the Option in the opposite transaction (resale transaction) cannot be higher than the nominal amount of the Option purchased by the Client.

In special cases, for example where the relationship between the Option exercise rate and the reference rate, irrespective of the elapse of time until the Option exercise date, indicates that the option has become an out-of-the-money option, the amount of the option premium received by the Client in connection with the closing transaction may be significantly lower than the option premium amount paid by the Client when purchasing the Option, i.e. the Client may not recover the option premium paid.

If the Client sells an Interest Rate Option, an opposite transaction involves the Client repurchasing an Interest Rate Option with the same parameters in respect to: the Option type, option exercise rate and exercise date, while the nominal amount of the Option in the opposite transaction (repurchase transaction) cannot be higher than the nominal amount of the Option sold by the Client. In special cases, for example where the relationship between the Option exercise rate and the reference rate, irrespective of the elapse of time until the Option exercise date, indicates that the option has become an in-the-money option, the amount of the option premium paid by the Client in connection with the closing transaction may be significantly higher than the option premium amount received by the Client in connection with the sale of the Option, i.e. in order to close the transaction, the Client will incur a cost that may constitute a significant burden for him.

In each case, the terms of the closing (opposite) transaction are agreed by the Parties to the transaction based on the market conditions in effect on the date the Client concludes the closing transaction, listed in detail in section I.II.2.

In each case, conclusion of a closing (opposite) transaction will entail an obligation on the part of the Option buyer to pay the agreed option premium amount. The Bank stipulates that once concluded, an Interest Rate Option transaction cannot be cancelled and its parameters cannot be changed.

**6. Other risks.**

When entering into financial market transactions, the Client should also take into account other risks of legal, accounting, fiscal and operational nature that are independent of Bank Millennium, including the risk related to the given benchmark unavailability and the possibility of determining an alternative benchmark, in accordance with applicable law, on the terms set out in the Regulations for concluding treasury transactions at Bank Millennium S.A..

With regard to interest rate option transactions, the Bank provides the service of executing orders to purchase or sell financial instruments to the Client's account, in accordance with Article 69 sect. 2 pt. 2 of the Act on Trading in Financial Instruments.

**III DEBT INSTRUMENTS**

**III.I TREASURY BONDS AND BILLS**

**1. Identification of risks associated with that type of financial instrument including an explanation of leverage and its effects and the risk of losing the entire investment including the risks associated with insolvency of the issuer or related events, such as cancellation or conversion of debt.**

A Client concluding transactions on the debt securities market should consider the credit risk and settlement risk associated with the issuer of the debt securities.

Treasury Bonds (also treasury Bills) are financial instruments issued by the State Treasury, based on the credit risk of the State Treasury, the price of which depends on the level of interest rates for the respective maturities. In the case of variable rate Bonds, a new coupon value will be determined in each interest period in accordance with the formula set forth in the Bond issue letter (usually the coupon is based on 6M WIBOR or on the yield of treasury Bills). On the other hand, fixed rate Bonds have a predetermined coupon amount and the coupon is usually paid once a year. Index-linked bonds may have a variable coupon, the amount of which depends on a specified macroeconomic index (very often it is an inflation index), or a fixed coupon and a variable nominal value indexed to an indexation factor.

Each of the three types of treasury Bonds mentioned above bears interest rate risk. In the case of variable rate bonds, an increase in the interest rate determining the coupon amount, e.g. WIBOR 6M, results in an increase of the coupon amount and therefore also increases the attractiveness of these securities, which causes their prices to go up. Accordingly, a decrease in the interest rate (WIBOR 6M) contributes to a decrease in the prices of such Bonds.

In the case of fixed rate Bonds, an increase in the interest rate corresponding to their maturity date results in a reduction of their prices and, accordingly, a decrease in the interest rate contributes to an increase in the prices of such Bonds.

For index-linked Bonds (e.g. ones linked to the inflation rate), a decrease in the real interest rate (e.g. an increase in the inflation rate with an unchanged nominal

interest rate) increases their prices. Correspondingly, an increase in the real interest rate results in a decrease in the prices of such Bonds.

In the case of debt securities with coupons, there is a **coupon reinvestment risk**, which may result in the inability to reinvest the coupon payments received at the originally assumed yield; as a result, the actual yield achieved on the debt securities held by the investor until maturity will differ from the yield assumed originally.

Since treasury Bills and Bonds are cash-based instruments, the leverage mechanism does not apply to investments in these instruments.

Investment in treasury Bonds is associated with the **issuer's credit risk** (in this case, the risk of the State Treasury), i.e. the risk of losing the capacity to settle its liabilities on time. This risk may result in the issuer defaulting on coupon payments or on redemption of the bonds.

**2. Identification of the volatility of that type of financial instrument or limitations concerning the availability of the market for that type of financial instrument.**

An investment in treasury Bills and Bonds entails the **risk of valuation of the concluded transaction on the settlement date and during its term**.

On the settlement day, the price at which the transaction has been concluded may differ significantly from the current market prices, which may result in the necessity for the Client to incur costs or be a source of income related to transaction settlement and may affect the final financial result achieved by the Client.

During the term of the transactions, market prices change and may depart significantly from the prices at which the transactions were concluded; this may result in a change in the valuation of transactions that may be unfavorable or favorable to the Client.

Any change in the valuation of transactions can occur rapidly and its scale can be significant.

In addition, transactions are exposed to the risk of **valuation volatility**, which means that potential gains or losses on transactions may increase or decrease as a result of changes in market factors affecting the instrument's valuation, including in particular:

- changes in spot and forward market interest rates and their mutual relations,
- changes in the level of market prices of debt securities,
- changes in yields of Bonds on foreign markets,
- changes in spot and forward market exchange rates and their mutual relations,
- changes in other market prices specific to the market and the type of transaction in question,
- changes in mutual relations of market prices,
- differences between reference rates adopted for a given transaction and market prices,
- occurrence of a difference between buy and sell prices for a given type of transaction on the financial market and changes in that difference.

Prices of financial instruments may also be affected by factors related to, among others, the political and economic situation (e.g. the condition of the state budget), changes in macroeconomic parameters (e.g. the economic cycle), inflation rate and the assessment of investment risk.

The volatility of prices in the economic cycle results from the fact that inflation tends to increase in periods of high economic growth, which entails the need to raise interest rates, causing in a decrease in the prices of fixed-interest bonds. In periods of slow economic growth, when inflation is low, market interest rates also decrease, which rises the prices of fixed interest bonds.

The condition of the state budget also affects volatility in such a way that when the budget records a surplus or small deficit, there is no surplus supply of Bonds from the State Treasury, which makes these securities become rare. Stable demand with a low supply causes a relative increase in the prices of the Bonds. In the situation of large budget deficits, the State Treasury ensures a large supply of Bonds, which results in a relative decline in their prices.

The yields of Bonds on foreign markets has a significant influence on the prices of Polish Bonds. Globalization enables the free movement of international capital. When risk aversion falls or increases on the American market or in Western Europe, investors should expect similar behaviors on the Polish market.

The Client should take into account the **risk of reduction or lack of liquidity** on the financial market,

which may result in a less favorable or unfavorable price for transaction on the debt securities market.

It is possible that the **availability of the market of debt securities** may be limited, which may affect the transaction price; these limitations may in particular prevent Bank Millennium from ensuring the possibility of concluding and executing transactions to purchase and sell a financial instrument at any moment chosen by the Client.

**3. Identification of the possibility that the Client might assume, as a result of transactions in that kind of financial instrument, financial commitments and other additional obligations, including contingent liabilities, additional to the cost of acquiring the financial instrument;**

In connection with transactions on the debt securities market there is a possibility that the Client may incur a financial liability resulting from the rights acquired by Bank Millennium as a result of the transaction in question.

Transactions in treasury Bonds involve the maintenance costs of the custody account and transaction settlement costs with the National Depository for Securities (the Central Register of Treasury Bills in the case of treasury Bills). There are no other financial liabilities in addition to the above.

**4. Description of margin requirements or similar obligations applicable when investing in financial instruments of that type.**

Not applicable.

**5. Information on impediments or restrictions for disinvestment, for example as may be the case for illiquid financial instruments or financial instruments with a fixed investment term, including an illustration of the possible exit methods and consequences of any exit, possible constraints and the estimated time frame for the sale of the financial instrument before recovering the initial costs of the transaction in that type of financial instruments.**

Despite the fact that treasury bonds and bills are quoted on a public trading market of debt instruments and on the interbank market, where market makers (banks with the status of treasury securities dealers) secure liquidity for individual issues, the investor should take into account the risk related to the limited liquidity of a given series of treasury bonds or bills. It means that the disposal of a bond/bill could be difficult because of the problems with finding an entity willing to invest in the issuer's bonds. In addition, if such an entity is found, the sale price set by the parties could be lower than the price that would guarantee that the investor earns the expected rate of return from its investment. The market price of bonds/bills may change under the influence of supply and demand, which may be affected among others by macroeconomic factors, the issuer's economic and financial standing and investors' behavior, which is difficult to predict. The restrictions in trading with bonds/bills may also result from the fact that some investors (such as investment funds and banks) have purchased the securities in order to hold them in their portfolios until maturity.

The suspension of trading in bonds/bills could lead to a significant decrease in the liquidity of trading and could make it difficult for an investor to sell bonds on the secondary market at a satisfactory price.

**6. Other risks**

When entering into transactions with Bank Millennium, the Client should also take into account the credit risk, settlement risk and operational risk of Bank Millennium as well as other risks of legal, accounting, fiscal and operational nature that are independent of Bank Millennium, including the risk related to the given benchmark unavailability and the possibility of determining an alternative benchmark, in accordance with applicable law, on the terms set out in the Regulations for concluding treasury transactions at Bank Millennium S.A..

One should note that the final result of investments may be affected by handling fees, and by the possible tax withheld on income from capital gains (including interest and discount). The Bank fulfils the obligations of a tax payer only if the obligation to withhold such tax is explicitly stated in the Polish law in this respect or from double taxation treaties binding on Poland. In order to

determine its own tax obligations, the Client should contact a tax advisor or a relevant tax authority.

**III.II MUNICIPAL BONDS**

**1. Identification of risks associated with that type of financial instrument including an explanation of leverage and its effects and the risk of losing the entire investment including the risks associated with insolvency of the issuer or related events, such as cancellation or conversion of debt.**

Municipal Bonds are debt securities with a maturity of at least one year issued by local government units (cities, municipalities). The Bonds are offered with a discount or pay a fixed or variable coupon.

The investment in municipal Bonds is subject to interest rate risk. In the case of variable rate Bonds, expectations or an increase in the interest rate determining the coupon amount (e.g. WIBOR 6M), results in an increase of the coupon amount and therefore also increases the attractiveness of these securities, which causes their prices to go up. Accordingly, expectations of a decrease or an actual decrease in the coupon interest rate contributes to a decrease in the prices of such Bonds. In the case of fixed rate Bonds, an increase in the interest rate corresponding to their maturity date results in a reduction of their prices. A decrease in the interest rate corresponding to the maturity date causes an increase in the prices of such Bonds.

In the case of coupon municipal Bonds, there is a **coupon reinvestment risk**, which may result in the inability to reinvest the coupon payments received at the originally assumed yield; as a result, the actual yield achieved on the debt securities held by the investor until maturity will differ from the yield assumed originally.

Additionally, investing in municipal Bonds is associated with the issuer's credit risk and financial liquidity risk. Therefore, in the event of the issuer's insolvency, the buyer of municipal Bonds may not receive the funds due to him under the Bonds or may receive them with a delay. The credit risk associated with a given municipal Bond is measured by the **issuer's or guarantor's credit rating** (if available) published by the relevant rating agencies (the lower the rating, the higher the credit risk of the municipal securities, which should be reflected in the higher yield of the instrument).

Since municipal Bonds are cash-based instruments, the leverage mechanism does not apply to investments in these instruments.

Investment in municipal Bonds is associated with the issuer's credit risk (in this case, the risk of the local government unit, i.e. a township, municipality and voivodship), which is the risk of losing the capacity to settle its liabilities on time. This risk may result in the issuer defaulting on coupon payments or on redemption of the bonds.

**2. Identification of the volatility of that type of financial instrument or limitations concerning the availability of the market for that type of financial instrument.**

The volatility of municipal bond prices depends on factors such as:

- the business cycle,
- condition of the issuer,
- yield of the Bonds on the domestic and foreign markets,
- liquidity and availability on the quotation market.

The volatility of prices in the economic cycle results from the fact that inflation tends to increase in periods of high economic growth, which entails the need to raise interest rates, causing in a decrease in the prices of fixed-coupon Bonds. In periods of slow economic growth, when inflation is low, market interest rates also decrease, which rises the prices of fixed interest bonds.

The yields of Bonds on the domestic and international markets have a significant effect on the prices of municipal Bonds. Globalization enables the free movement of international capital. When risk aversion falls or increases on the American market or in Western Europe, investors should expect similar behaviors on the Polish market.

Considering the availability of the municipal Bond market, it should be noted that the nominal value of a single Bond may constitute a restriction for some Clients.

Another restriction on availability is the liquidity of the Bonds market, i.e. the ease and speed with which transactions of the desired value can be executed.

The issues of municipal Bonds are usually smaller than treasury Bond issues. Accordingly, the liquidity of municipal securities is lower.

**3. Identification of the possibility that the Client may incur, as a result of transactions on that financial instrument, financial commitments with delivery of the underlying instrument, which are obligations additional to the costs of purchase of the financial instrument.**

Transactions in municipal Bonds involve the maintenance costs of the custody account and transaction settlement costs with the National Depository for Securities.

In the case of a public issue of municipal bonds, the settlement is performed by KDPW, while the settlements of privately-placed municipal bonds may be performed by KDPW or a bank or an external agent.

**4. Description of margin requirements or similar obligations applicable when investing in financial instruments of that type.**

Not applicable.

**5. Information on impediments or restrictions for disinvestment, for example as may be the case for illiquid financial instruments or financial instruments with a fixed investment term, including an illustration of the possible exit methods and consequences of any exit, possible constraints and the estimated time frame for the sale of the financial instrument before recovering the initial costs of the transaction in that type of financial instruments.**

For bonds not admitted to public trading, there is a high risk that the bonds held cannot be disposed quickly at any time because of the difficulties in finding an investor interested in purchasing them.

For bonds quoted on a public debt instruments trading market (a regulated market or a multilateral trading facility), the investor should also take into account the risk related to the reduced liquidity of the bonds. It means that the disposal of bonds could be difficult because of the problems with finding an entity willing to invest in the issuer's bonds. In addition, if such an entity is found, the sale price set by the parties could be lower than the price that would guarantee that the investor earns the expected rate of return from its investment. The market price of bonds may change under the influence of supply and demand, which may be affected among others by macroeconomic factors, the issuer's economic and financial standing, the NBP's monetary policy and investors' behavior, which is difficult to predict. The limitation of liquidity of the bonds may also result from the fact that some investors have purchased the bonds in order to hold them in their portfolios until maturity.

Bonds quoted on a public trading market are subject to the risk of suspension of trading and the risk of the bonds being excluded from trading.

The suspension or exclusion of trading in bonds could lead to a significant decrease in the liquidity of trading in the bonds and could make it difficult for an investor to sell bonds on the secondary market at a satisfactory price.

**6. Other risks.**

A Client concluding transactions on the debt securities market should consider the credit risk and settlement risk associated with the issuer of the debt securities, as well as other risks of a legal, accounting, tax and operational nature independent of Bank Millennium, including the risk related to the given benchmark unavailability and the possibility of determining an alternative benchmark, in accordance with applicable law, on the terms set out in the Regulations for concluding treasury transactions at Bank Millennium S.A..

One should note that the final result of investments may be affected by handling fees, and by the possible tax charges.

One should note that the final result of investments may be affected by handling fees, and by the possible tax withheld on income from capital gains (including interest and discount). The Bank fulfils the obligations of a tax payer only if the obligation to withhold such tax is explicitly stated in the Polish law in this respect or from double taxation treaties binding on Poland. In order to

determine its own tax obligations, the Client should contact a tax advisor or a relevant tax authority.

### III.III CORPORATE BONDS

#### 1. Identification of risks associated with that type of financial instrument including an explanation of leverage and its effects and the risk of losing the entire investment including the risks associated with insolvency of the issuer or related events, such as cancellation or conversion of debt.

Corporate bonds are financial instruments issued by various institutional issuers, excluding the State Treasury. In the case of variable rate Bonds, a new coupon value is determined in each interest period in accordance with the formula set forth in the terms and conditions of Bond issue/Bond issue letter (usually the coupon is based on WIBOR 6M or on the yield of treasury Bills). On the other hand, fixed rate Bonds have a predetermined coupon amount and the coupon is usually paid once a year.

Each of the two types of Bonds mentioned above bears interest rate risk. In the case of variable rate bonds, an increase in the interest rate determining the coupon amount, e.g. WIBOR 6M, results in an increase of the coupon amount and therefore also increases the attractiveness of these securities, which causes their prices to go up. Accordingly, a decrease in the coupon interest rate contributes to a decrease in the prices of such Bonds.

In the case of fixed rate Bonds, an increase in the interest rate corresponding to their maturity date results in a reduction of their prices. A decrease in the interest rate corresponding to the maturity date causes an increase in the prices of such Bonds.

Additionally, investing in the Bonds is associated with the issuer's credit risk and financial liquidity risk. Therefore, in the event of the issuer's insolvency, the buyer of corporate Bonds may not receive the funds due to him under the Bonds or may receive them with a delay. The credit risk associated with a given Bond is measured by the issuer's or guarantor's credit rating published by the relevant rating agencies (the lower the rating, the higher the credit risk of the corporate securities, which should be reflected in the higher yield of the instrument).

Since corporate Bonds are cash-based instruments, the leverage mechanism does not apply to investments in these instruments.

Investment in corporate Bonds is associated with the issuer's credit risk, i.e. the risk of losing the capacity to settle its liabilities on time, including the risk of the issuer's bankruptcy. This risk may result in a failure to pay coupon or redeem the issuer's bonds.

In the case of issuers who are banks or other credit institutions, there may exist a risk that the issuers' liabilities under the bonds may, where the conditions prescribed by law are satisfied, be subject to a debt cancellation or conversion measure according to the rules set forth in the BGF Act or other similar regulation.

#### 2. Identification of the volatility of that type of financial instrument or limitations concerning the availability of the market for that type of financial instrument.

The volatility of corporate bond prices depends on factors such as:

- the business cycle,
- condition of the issuer,
- yield of the Bonds on the domestic and foreign markets,
- liquidity and availability on the quotation market.

The volatility of prices in the economic cycle results from the fact that inflation tends to increase in periods of high economic growth, which entails the need to raise interest rates, causing in a decrease in the prices of Bonds. In periods of slow economic growth, when inflation is low, market interest rates also decrease, which rises the prices of Bonds.

The yields of Bonds on foreign markets has a significant influence on the prices of corporate Bonds. Globalization enables the free movement of international capital. When risk aversion falls or increases on the American market or in Western Europe, investors should expect similar behaviors on the Polish market.

Considering the availability of the Bond market, it should be noted that the nominal value of a single Bond may constitute a restriction for some Clients.

Another restriction on availability is the liquidity of the Bonds market, i.e. the ease and speed with which transactions of the desired value can be executed.

The issues of corporate Bonds are usually smaller than the issues of treasury Bonds and Bills. Accordingly, the liquidity of commercial papers is lower.

#### 3. Identification of the possibility that the Client may incur, as a result of transactions on that financial instrument, financial commitments with delivery of the underlying instrument, which are obligations additional to the costs of purchase of the financial instrument.

Transactions in corporate Bonds involve the maintenance costs of the custody account and transaction settlement costs with the National Depository for Securities.

In the case of a public issue of corporate bonds, the settlement is performed by KDPW through an entity keeping the securities account for the bondholder or a collective account, while the settlements of privately-placed corporate bonds may be performed by KDPW or a bank or an external agent.

#### 4. Description of margin requirements or similar obligations applicable when investing in financial instruments of that type.

Not applicable.

#### 5. Information on impediments or restrictions for disinvestment, for example as may be the case for illiquid financial instruments or financial instruments with a fixed investment term, including an illustration of the possible exit methods and consequences of any exit, possible constraints and the estimated time frame for the sale of the financial instrument before recovering the initial costs of the transaction in that type of financial instruments.

For bonds not admitted to public trading, there is a high risk that the bonds held cannot be disposed quickly at any time because of the difficulties in finding an investor interested in purchasing them.

For bonds quoted on a public debt instruments trading market (a regulated market or a multilateral trading facility), the investor should also take into account the risk related to the reduced liquidity of the bonds. It means that the disposal of bonds could be difficult because of the problems with finding an entity willing to invest in the issuer's bonds. In addition, if such an entity is found, the sale price set by the parties could be lower than the price that would guarantee that the investor earns the expected rate of return from its investment. The market price of bonds may change under the influence of supply and demand, which may be affected among others by macroeconomic factors, the issuer's economic and financial standing, the NBP's monetary policy and investors' behavior, which is difficult to predict. The limitation of liquidity of the bonds may also result from the fact that some investors have purchased the bonds in order to hold them in their portfolios until maturity.

Bonds quoted on a public trading market are subject to the risk of suspension of trading and the risk of the bonds being excluded from trading.

The suspension or exclusion of trading in bonds could lead to a significant decrease in the liquidity of trading in the bonds and could make it difficult for an investor to sell bonds on the secondary market at a satisfactory price.

#### 6. Other risks.

A Client concluding transactions on the debt securities market should consider the credit risk and settlement risk associated with the issuer of the debt securities, as well as other risks of a legal, accounting, tax and operational nature independent of Bank Millennium, including the risk related to the given benchmark unavailability and the possibility of determining an alternative benchmark, in accordance with applicable law, on the terms set out in the Regulations for concluding treasury transactions at Bank Millennium S.A..

One should note that the final result of investments may be affected by handling fees, and by the possible tax charges.

One should note that the final result of investments may be affected by handling fees, and by the possible tax withheld on income from capital gains (including interest and discount). The Bank fulfils the obligations of a tax payer only if the obligation to withhold such tax is explicitly stated in the Polish law in this respect or from double taxation treaties binding on Poland. In order to determine its own tax obligations, the Client should contact a tax advisor or a relevant tax authority.

With regard to debt instruments, the Bank provides the service of executing orders to purchase or sell financial instruments to the Client's account, in accordance with Article 69 sect. 2 pt. 2 of the Act on Trading in Financial Instruments.

#### IV. TYPES OF INVESTMENT SERVICES:

Execution of orders to purchase or sell financial instruments on the Client's account, in accordance with Article 69 sect. 2 pt. 2 of the Act on Trading in Financial Instruments – the service consists in executing orders to purchase or sell financial instruments to the account of the person giving the order. The Bank provides it by purchasing or selling financial instruments on its own account (i.e. in the manner described in Article 73 sect. 2 of the Act on Trading in Financial Instruments).