

Disclosure report on management principles and compliance with PFMI

Krajowa Izba Rozliczeniowa S.A.

Management principles at KIR and summary of compliance with PFMI

in accordance with the Rules for communication of information by financial market infrastructures

As of 1 February 2023

1. Introduction

This Disclosure report on management principles and compliance with PFMI ("Report") is prepared in order to disclose the principles of management of Krajowa Izba Rozliczeniowa S.A. [joint-stock company] (KIR) and sum up the KIR's compliance with the Principles for Financial Market Infrastructures (PFMI) developed by the Committee on Payment and Settlement Systems (CPSS) and Technical Committee of the International Organisation of Securities Commissions (IOSCO) and published by the Bank for International Settlements.

2. Summary of the key developments from the last Report

This is the first Report prepared by KIR.

3. General information about KIR

3.1. General description of KIR and range of provided services

KIR is a systemically important entity of the Polish payment system infrastructure which supports the development of safe digital processes in banking, economy and public sector.

KIR operations take place on the markets covering four strategic pillars: Pillar I: Comprehensive clearing services in PLN and EUR; Pillar II: Electronic identification services and trust services; Pillar III: Services in the area of combating abuses, AML, KYC and safe information exchange; Pillar IV: Services supporting modern payments and innovative services for the enhancement of economy digitisation.

The above-mentioned pillars are based on three strategic foundations: human resources, advanced technologies and mature processes, and research and development. The strategic foundations form the right conditions to pursue the business goals of KIR.

The scope of business activities of KIR is as follows:

- 1) exchange of payment orders between payment service providers and registration of reciprocal claims arising from orders;
- 2) operation of payment systems;
- 3) other activities related to clearing;
- 4) provision of payment services;
- 5) provision of services auxiliary to payment services, and particularly actions aimed at the popularisation of cashless payments;
- 6) maintenance of ICT system handling seizures of liabilities from the bank account;
- 7) maintenance of central information on accounts;
- 8) provision of services auxiliary to operational risk management for banks, credit unions and other providers of payment services, and particularly services auxiliary to countermeasures against the use of their operations in order to hide criminal activity or for the purposes related to offences, including tax offences or money laundering and financing terrorism;
- 9) provision of services handling and supporting actions performed on electronic information media and in the remote mode, including particularly within the scope of electronic data certification, handling of electronic invoices, archiving and making electronic documents available, as well as remote transfer of information and data;
- 10) provision of services of trust and electronic identification, and accompanying or auxiliary services;
- 11) provision of services within the scope of system security and cybersecurity;
- 12) counselling, particularly within the scope of clearing, payment, IT services, system security and cybersecurity;
- 13) sales of data transmission services, including network operation necessary to send data between devices using the same or different transmission protocols by the agency of public or dedicated data transmission network;
- 14) activities related to software, including development and sales of own IT solutions and licensing them;
- 15) data processing;
- 16) activities related to databases;
- 17) activities related to the management of IT devices;
- 18) rental or lease of office machines and devices, including computer hardware;
- 19) maintenance of archives upon order in paper and electronic form;
- 20) retail sales over the Internet;
- 21) educational and training activities, particularly within the scope of electronic trade, including its security, operation of clearing systems, certification and optical readout;
- 22) sales and promotion of products and services of other business entities;
- 23) publishing activities;
- 24) lease and operation of real property on its own account.

Basic data and statistics about services and operations, particularly basic data about the volume and value by the type of product, are available at the website, particularly at the following address:
<https://www.banki.kir.pl/uzyteczne-narzedzia-i-statystyki/dane-statystyczne/>.

3.2. General organisation of KIR

KIR is a joint-stock company with the following shareholders: Narodowy Bank Polski, Santander Bank S.A., Powszechna Kasa Oszczędności Bank Polski S.A., mBank S.A., ING Bank Śląski S.A., Bank Polska Kasa Opieki S.A., Bank Millennium S.A., Bank Handlowy w Warszawie S.A., BNP Paribas Bank Polska S.A., Bank Polskiej Spółdzielczości S.A., SGB-Bank S.A. and Związek Banków Polskich (Polish Bank Association).

Detailed information about KIR is available at the website, particularly at the following addresses: <https://www.kir.pl/o-nas/o-kir/>, <https://www.kir.pl/o-nas/wladze/>, <https://www.kir.pl/o-nas/akcjonariat/>, <https://www.kir.pl/o-nas/strategia-kir/>.

3.3. Legal and regulatory framework

Due to the operation of payment systems, KIR is under the supervision of the National Bank of Poland. The purpose of NBP supervision is to support the security and efficiency of the payment system infrastructure, and to ensure the organisation and operation of individual elements of the payment system in accordance with the provisions of the law in order to guarantee their uninterrupted operation and thus reduce the system risk related to their operation.

KIR has the status of national payment institution within the meaning of the Act of 19 August 2011 on Payment Services. The operation of national payment institution is subject to licence, which means that it requires obtaining prior permit from the Polish Financial Supervision Authority and entry to the register of payment service providers kept by the Polish Financial Supervision Authority.

KIR also operates on the basis of legal and regulatory framework arising particularly from:

- 1) Act of 15 September 2000 on the Code of Commercial Companies and Partnerships;
- 2) Act of 24 August 2001 on the Settlement Finality in Payment Systems and Securities Settlement Systems and the Principles of Supervision over such Systems;
- 3) Act of 5 September 2016 on Trust Services and Electronic Identification;
- 4) Act of 1 March 2018 on Combating Money Laundering and Financing Terrorism;
- 5) Regulation of the European Parliament and of the Council (EU) No. 910/2014 of 23 July 2014 on electronic identification and trust services for electronic transactions in the internal market and repealing Directive 1999/93/EC.

At the same time KIR fulfils its obligations imposed by the Act of 29 August 1997 on Tax Ordination and the Act of 29 August 1997 on the Banking Law.

3.4. System architecture and operations

Detailed information about the system architecture and operations is available at the KIR website, particularly:

<https://www.banki.kir.pl/elixir/system-elixir/>

<https://www.banki.kir.pl/express-elixir/>

<https://www.banki.kir.pl/euro-elixir/system-euroelixir/> and

<https://www.kir.pl/klienci-indywidualni/express-elixir/>

4. Descriptive information about compliance with individual principles for financial market infrastructure

This report is prepared with reference to the following PFMI principles:

Principle 1. Legal basis; Principle 2. Governance; Principle 3. Framework for the comprehensive management of risks; Principle 4. Credit risk; Principle 7. Liquidity risk; Principle 8. Settlement finality; Principle 9. Money settlements; Principle 13. Participant-default rules and procedures; Principle 15. General business risk; Principle 16. Custody and investment risks; Principle 17. Operational risk; Principle 18. Access and participation requirements; Principle 19. Tiered participation arrangements; Principle 21. Efficiency and effectiveness; Principle 23. Disclosure of rules, key procedures, and market data.

The remaining PFMI principles do not apply to KIR.

4.1. Summary of compliance with PFMI on a “principle by principle” basis:

Wording of the principle:	Summary of the principle application:
<p><i>The foundation of general principles for risk management in the financial market infrastructure (hereinafter “FMI”) includes its authority, structure, rights and responsibilities. The following principles provide guidelines on:</i></p> <ul style="list-style-type: none"> <i>a) legal basis for the FMI’s activities,</i> <i>b) the governance structure of the FMI, and</i> <i>c) the framework for the comprehensive management of risks, to help establish a strong foundation for the risk management of an FMI.</i> <p><i>An FMI should have a well-founded, clear, transparent and enforceable legal basis for each material aspect of its activities in all relevant jurisdictions.</i></p>	<p>All elements of operation of payment systems run by KIR require high degree of legal certainty, particularly with regard to compensation of mutual liabilities and participants’ membership in session systems, assurance of settlement finality and procedures related to non-performance of obligation by the participant/participants during a specific settlement session (Settlement Guarantee Mechanism).</p> <p>All elements of operation of payment systems are governed by the Polish law. All legal changes that might affect the operation of payment systems are analysed on an ongoing basis by relevant organisational units of KIR as part of advanced compliance control processes. In addition, the payment systems are subject to the supervision of NBP which, pursuant to the Act of 24 August 2001 on the Settlement Finality in Payment Systems and Securities Settlement Systems and the Principles of Supervision over such Systems, assesses, for example, whether the principles of operation of such systems comply with the provisions of the Polish law and, from time to time, grants permit for the introduction of changes in the principles of operation of a given system.</p>
<p><i>An FMI should have governance arrangements that are clear and transparent, promote the safety and efficiency of the FMI, and support the stability of the broader financial system, other relevant public interest considerations, and the objectives of relevant stakeholders.</i></p>	<p>KRS is a joint-stock company founded and operating, among other things, on the basis of the Act of 15 September 2000 on the Code of Commercial Companies and Partnerships, which guarantees legal responsibility towards owners that, in the case of KIR, are at the same time participants in payment systems run by KIR (with the exception of the Polish Bank Association). As the entity running the payment systems, KIR is responsible towards the participants for the observance of principles arising from the regulations of such systems within the scope of obligations of the system operator.</p> <p>Among other things, the KIR’s corporate governance is comprised of: Articles of Association of Krajowa Izba Rozliczeniowa Spółka Akcyjna, Regulations of the General Meeting of Krajowa Izba Rozliczeniowa Spółka Akcyjna, Regulations of the Supervisory Board of Krajowa Izba Rozliczeniowa S.A. and Regulations of Activities of the Management Board of Krajowa Izba Rozliczeniowa S.A.</p> <p>The principles of organisation of KIR, the scope of operation of its organisational units, the principles of their mutual cooperation and other matters related to internal organisation of KIR are set forth in the Organisational Regulations. These Regulations also set forth the principles of management of product (service) or group of products (services) by business lines.</p>

	<p>For example, within the scope of interbank clearing, the KIR Strategy for the years 2023-2025 defines the strategic goals concerning security and reliability of provided services and their comprehensiveness. The goals are assigned with meters with the set target value. The Management Board presents the Supervisory Board with periodical reports on the completion of the current KIR Strategy.</p> <p>The management of payment systems belongs to the Area of the President of the Management Board.</p> <p>The internal control system present at KIR covers closely related elements of administration and management of all areas of operation of KIR.</p>
<p><i>An FMI should have a sound risk-management framework for comprehensively managing legal, credit, liquidity, operational and other risks.</i></p>	<p>KIR has a documented risk management system (RMS) that is linked to the Information Security Management System (ISMS). The process of risk identification, analysis and assessment follows the formal rules. The process of risk analysis takes place periodically and on an ad-hoc basis if an event occurs which necessitates the performance of such analysis outside the predefined date. The process involves the analysis of strategic, operational risks, risks related to personal data protection, continuity of operation, information security, custody, investment, as well as credit and liquidity risks.</p>
<p><i>An FMI or its participants may face credit and liquidity risks arising from the payment, clearing and settlement processes. Credit risk is the risk that a counterparty will be unable to meet fully its financial obligations when due date or at any time in the future. These counterparties may include the FMI's participants (see Principle 4 on credit risk), settlement banks (see Principle 9 on money settlements) and custodians (see Principle 16 on custody and investment risks). Liquidity risk is the risk that a counterparty will have insufficient funds to meet its financial obligations when due, but may be able to do so at some time in the future. Although credit and liquidity risks are distinct concepts, there is often significant interaction between these risks. For example, a participant default in an FMI would likely result in the FMI facing both credit and liquidity risk, potentially requiring the FMI to draw on its liquidity resources to meet its immediate obligations. An FMI has a range of risk-management tools to mitigate and manage these risks.</i></p>	<p>KIR has established frameworks for the management of all aspects of risk that may comprehensively identify, assess, monitor and escalate the risk relevant for a given payment system.</p> <p>As part of procedures assuring the performance of settlement at the currency date for session systems, there is the Settlement Guarantee Mechanism (SGM) which, in the case of lack of funds to cover the liabilities of one or many participants, assures the performance of settlement with the funds available at a given session by the identification of orders that are not subject to settlement. NBP and KNF are notified about the fact of launching SGM.</p> <p>In the case of the Express Elixir system, the settlement takes place with the use of the deposit model based on the custodial account kept with the SORBNET2 system. KIR keeps ongoing records of funds gathered at the custodial account that belong to individual system participants.</p>
<p><i>An FMI should effectively measure, monitor and manage its liquidity risk. An FMI should maintain sufficient liquid resources in all relevant currencies to effect same-day and, where appropriate, intraday and multiday settlement of payment obligations with a high degree of confidence under a wide range of potential stress scenarios that should include, but not be limited to, the default of the participant and its affiliates that</i></p>	<p>KIR does not use own funds to settle or credit the participants at any time in the course of clearing of session payments systems and, therefore, it does not incur the liquidity risk related to securing the settlement of the cleared transactions.</p> <p>The settlement agent for the session payment systems is the National Bank of Poland. The liquidity risk or credit risk of KIR are supervised under the Risk Management System (RMS) organised at KIR.</p>

<p><i>would generate the largest aggregate liquidity obligation for the FMI in extreme but plausible market conditions.</i></p>	<p>In the case of the Express Elixir system, the settlement takes place with the use of the deposit model based on the custodial account kept with the SORBNET2 system. KIR keeps ongoing records of funds gathered at the custodial account that belong to individual system participants.</p>
<p><i>An FMI should provide clear and certain final settlement, at a minimum by the end of the date that is the deadline for the delivery of securities and monetary funds to the accounts. Where necessary or preferable, an FMI should provide final settlement intraday or in real time.</i></p>	<p>KIR makes relevant orders on time due to the set settlement sessions. The rules of transfer of payment orders to KIR by the participants and completion of clearing and settlement, including times of settlement sessions at NBP and times of making the resulting collections from interbank, interbranch and intrabranh settlements available to the participants, are set forth in participation agreements, relevant regulations and technical specification of session systems. The settlement in the Euro Elixir system becomes final when KIR conducts settlement in the TARGET2-NBP system for the specific settlement procedure (or in the TARGET-NBP system from 20 March 2023). The mechanism for order settlement in the Express Elixir system follows the deposit model and works on the basis of safe custodial account kept for this system by NBP in the SORBNET2 system.</p>
<p><i>An FMI should conduct its money settlements in central bank money where practical and available. If central bank money is not used, an FMI should minimise and strictly control the credit and liquidity risk arising from the use of commercial bank money.</i></p>	<p>The Elixir and Express Elixir systems are settled in central bank money with the use of current accounts of the participants and custodial account of KIR (for the Elixir system) or custodial account (for the Express Elixir system) in the SORBNET2 system. The Elixir and Express Elixir systems are used only for the clearing of transactions denominated in domestic currency (PLN). The Euro Elixir system is used for settlement in the ECB currency (EUR) in the trans-European TARGET2-NBP system (and TARGET system from 20 March 2023). KIR has implemented rigorous rules for risk analysis in this area.</p>
<p><i>An FMI should have appropriate policies and procedures to manage participant defaults. A participant default, if not properly managed, can have serious implications for the FMI, other participants, and broader financial markets. Further, a CCP¹ needs an appropriate segregation and portability regime to protect customer positions in the event of a participant default or insolvency. The following two principles provide guidance on:</i></p> <ul style="list-style-type: none"> <i>a) participant-default rules and procedures for all FMIs and</i> <i>b) segregation and portability issues for CCPs.</i> <p><i>An FMI should have effective and clearly defined rules and procedures to manage a participant default. These rules and procedures should be designed to ensure that the FMI can take timely action to contain losses and liquidity pressures and continue to meet its obligations.</i></p>	<p>The participant's/ participants' default on their financial obligations, that is the lack of appropriate funds for the Elixir system in the current accounts in the SORBNET2 system or in subaccounts or RTGS accounts of settlement banks at the time of the settlement session, leads to the application of the Settlement Guarantee Mechanism (SGM). Operational requirements that must be met by the participant are specified in the general rules and criteria of access to the KIR's payment systems, relevant regulations, participation agreement and technical specifications of the relevant system.</p> <p>In the Express Elixir system it is only possible to execute transactions that may be covered with funds gathered in the custodial account and entrusted to KIR by a given participant for the purposes of clearing of payment orders in the Express Elixir system (in the above-described deposit model).</p>

¹ CCP – Central counterparty

<p><i>In addition to the credit, liquidity, and other related risks that it faces from its payment, clearing, and settlement activities, an FMI also faces general business and operational risks. The inability of an FMI to continue as a going concern could have systemic risk implications for its participants and the broader financial markets. The following set of principles provides guidance on managing:</i></p> <ul style="list-style-type: none"> <i>a) general business risk;</i> <i>b) custody and investment risks; and</i> <i>c) operational risk.</i> <p><i>An FMI should identify, monitor, and manage its general business risk and hold sufficient liquid net assets funded by equity to cover potential general business losses so that it can continue operations and services as a going concern if those losses materialise. Further, liquid net assets should at all times be sufficient to ensure a recovery or orderly wind-down of critical operations and services.</i></p>	<p>KIR manages the following categories of risks: strategic, operational risks, risks related to personal data protection, continuity of operation, information security, custody, investment, as well as credit and liquidity risks. The implemented and formalised Risk Management System (RMS) covers the required aspects of identification of sources of risk, risk assessment, risk monitoring, risk management by way of proper response to incidents and unacceptable levels of risk. KIR assures the maintenance of liquid net assets funded by equity that allow for continuous operational activity and provision of services in the case of incurring losses related to general business risk.</p> <p>As part of RMS, KIR has developed and maintains the KIR's Recovery Plan, KIR's Orderly Wind-down Plan and KIR's Equity Increase Plan. The basic control mechanisms in this area are the adopted scenarios for the examination of exposure to risk in this area.</p>
<p><i>An FMI should safeguard its own and its participants' assets and minimise the risk of loss on and delay in access to these assets. An FMI's investments should be in instruments with minimal credit, market, and liquidity risks.</i></p>	<p>KIR keeps its liquid assets in the form of monetary funds gathered in bank accounts. When depositing monetary funds in bank accounts, KIR rigorously applies mechanisms to minimise the risk of loss on and delay in access to these assets. The instruments used by KIR are always characterised by minimal credit, market and liquidity risks.</p>
<p><i>An FMI should identify the plausible sources of operational risk, both internal and external, and mitigate their impact through the use of appropriate systems, policies, procedures, and control mechanisms. Systems should be designed to ensure a high degree of security and operational reliability, and should have adequate, scalable capacity. Business continuity management should aim for timely recovery of operations and fulfilment of the FMI's obligations, including in the event of a wide-scale or major disruption.</i></p>	<p>KIR has a documented Risk Management System (RMS) that is linked to the Information Security Management System (ISMS). The process of risk identification, analysis and assessment follows the best market practices and international standards (ISO 22301 and ISO 27001). The process of risk analysis takes place periodically at planned intervals and on an ad-hoc basis if an event occurs which necessitates the performance of such analysis outside the predefined date. The process involves the analysis of strategic, operational risks, risks related to personal data protection, continuity of operation, and information security. In the case of processes in which personal data are processed, the risk of non-execution of the rights of persons is identified and analysed.</p> <p>KIR introduced a number of security measures, both physical and organisational ones, to ensure high level of physical security and cyber-resilience.</p>

<p><i>Fair and open access to an FMI by direct participants, indirect participants, and other FMIs is important because of the critical role many FMIs play in the markets they serve. The following set of principles provides guidance on:</i></p> <ul style="list-style-type: none"> <i>a) access and participation requirements,</i> <i>b) the management of tiered participation arrangements, and</i> <i>c) the management of FMI operational links.</i> <p><i>An FMI should have objective, risk-based, and publicly disclosed criteria for participation which permit fair and open access.</i></p>	<p>The terms of participation in payment systems are defined in relevant regulations for these systems and participation agreements.</p> <p>All participants in a given payment system are subject to the same criteria of access to this system.</p>
<p><i>An FMI should identify, monitor, and manage the material risks to the FMI arising from tiered participation arrangements.</i></p>	<p>Participation in payment systems is subject to material limitations as to the entities that may be its participants.</p> <p>KIR does not have any legal relations with indirect participants, as they are submitted for clearing by the direct participant, and their clearing number is assigned to the clearing number of the submitting participant. KIR incurs no risk related to indirect participants, as the liability in that respect lies with the direct participant that manages the risk in this area. The Elixir and Euro Elixir session payment systems use contractual security mechanisms, including mechanism for the verification of the values of orders of indirect participants against the sum of values of orders of a given direct participant.</p>
<p><i>Efficiency and safety are important to an FMI in performing its payment, clearing, settlement, and recording functions. The following two principles provide guidance to FMIs on:</i></p> <ul style="list-style-type: none"> <i>a) efficiency and effectiveness, and</i> <i>b) communication procedures and standards, which is one traditional aspect of efficiency.</i> <p><i>An FMI should be efficient and effective in meeting the requirements of its participants and the markets it serves.</i></p>	<p>All of the KIR's shareholders (apart from the Polish Bank Association) are direct participants in the Elixir system that also have their representatives in the Supervisory Council. All changes in the regulations of the Elixir and Euro Elixir session payment systems that are the basic documents setting the principles of clearing and settlement completion are adopted by the Supervisory Board and, in the case of the Express Elixir system, by the Management Board, and then approved by the President of NBP by granting permit to introduce changes in the principles of operation of the payment system in the mode provided for in the Act of 24 August 2001 on the Settlement Finality in Payment Systems and Securities Settlement Systems and the Principles of Supervision over such Systems.</p>

<p><i>Transparency helps to ensure that relevant information is provided to an FMI's participants, authorities, and the public to ensure sound decision making and foster confidence. The following two principles provide guidance to:</i></p> <ul style="list-style-type: none"> <i>a) all FMIs on the disclosure of rules, key procedures, and market data to enable participants and other interested parties to have a clear understanding of the risks and controls on risks associated with an FMI, as well as fees and other costs incurred by participation in the FMI; and</i> <i>b) TRs² on the disclosure of market data to allow participants, authorities, and the public to make timely assessments of OTC derivatives markets and, if relevant, other markets served by the TR.</i> <p><i>An FMI should have clear and comprehensive rules and procedures and should provide sufficient information to enable participants to have an accurate understanding of the risks, fees, and other material costs they incur by participating in the FMI. All relevant rules and key procedures should be publicly disclosed.</i></p>	<p>Documents that define the principles of operation of the payment systems are the general rules and criteria of access to the KIR's payment systems, regulations of these systems, technical specifications and participation agreements. General rules and criteria of access to the KIR's payment systems, Regulations (without technical specifications) and model participation agreements for the Elixir and Euro Elixir session systems are available at the public website of KIR. The website also contains the regulations (without technical specifications) of instant payment systems, and general information and operating principles of this service.</p> <p>Information necessary for disclosure according to the PFMI requirements is made available, for example, in this Report.</p>
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² Transaction Repository