

## ALLFUNDS BANK S.A.U. INTERNAL CONTROL MECHANISMS

As a result of the material changes that have been gradually implemented in the banking sector in the last few years, new provisions and improvements in the internal organisation of credit institutions have been introduced. These changes and reforms in the banking system, along with the requirement of adequate internal control procedures, respond to the need to improve banks' corporate governance and introduce proper management of banking risks. The implementation and guarantee of a sound and prudent management at banks are therefore basic principles underpinning these new financial standards.

The internal governance of banks in the European Union is initially discussed in article 22 of Directive 2006/48/EC, which requires that *"every credit institution have robust governance arrangements, which include a clear organisational structure with well defined, transparent and consistent lines of responsibility, effective processes to identify, manage, monitor and report the risks it is or might be exposed to, and adequate internal control mechanisms, including sound administrative and accounting procedures"*. This Directive, along with others that historically regulated the activity of credit institutions, has been replaced by a series of European rules that are the result of adapting Basel III to the legal framework of the European Union. This has yielded a much more comprehensive and sophisticated regulation that focuses not only on the access to the activity of credit institutions but on a much broader and more robust prudential supervision.

In application of this regulation on banking supervision, the guidelines issued by the Bank of Spain (and other European supervisory bodies) establish a series of obligations for Spanish banks. Hence, in accordance with Rule 60 e) of Bank of Spain Circular 2/2016, dated 2 February, predicated on article 29.5 of Law 10/2014, dated 26 June, concerning the ordering, supervision and solvency of credit institutions, said institutions must publicly disseminate certain information specifying the manner in which they comply with corporate governance obligations.

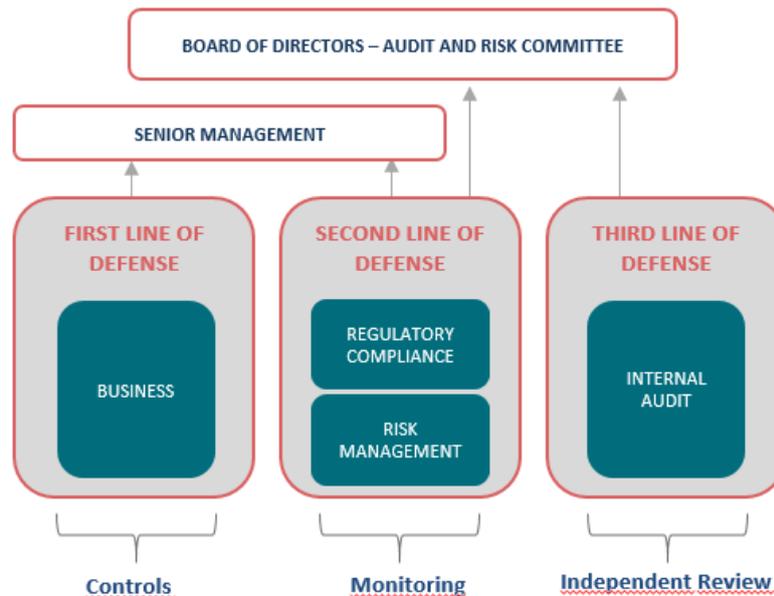
In this connection, in accordance with Rule 281. d) of Bank of Spain Circular 2/2016, dated 2 February, and with the provisions of article 29 of Law 10/2014 and article 43 of Royal Decree 84/2015, credit institutions must, among other requirements:

*d) Establish in writing policies for undertaking risks and adequate internal measurement procedures, stress tests, operating limits, review frequencies, bodies or persons responsible and other relevant aspects. In particular, and in line with their level of activity, they must have risk measurement and reporting systems that are appropriate for their management, monitoring and control. Furthermore, they must adequately document the functioning of the internal control systems in place.*

In accordance with these regulations, and pursuant to the requirement of publishing banks' internal control mechanisms, including administrative and accounting procedures, the control mechanisms at ALLFUNDS BANK S.A.U. (hereinafter "Allfunds Bank") are as follows:

## 1.- THREE LINES OF DEFENSE MODEL

Allfunds Bank has a control mechanism based in three lines of defense as represented in the following chart:



The first line of defense is formed by the different business and support departments of Allfunds Bank in charge of carrying out Allfunds Bank activities. This first line of defense manages risk indicators and/or the first level controls to detect possible risks and act effectively to mitigate them.

The second line of defense is formed by the Compliance and Risk Management teams, both acting autonomously and independently of each other and with respect to the first line of defense, which help to build and monitor the controls of the previous line of defense.

Finally, and as the third line of defense, Allfunds Bank has an Internal Audit function with the highest levels of independence and objectivity within the entity, which provides guarantees on the effectiveness of the control systems, carrying out an independent review of the two aforementioned lines and verifying the compliance with the model.

### Internal Audit

The Internal Audit Area (hereinafter “Allfunds Internal Audit or AIA”) is responsible for providing the Risk and Audit Committee and Senior Management with a reliable view of the effectiveness of the controls aimed to mitigate significant risks which affect the business, both current and foreseeable in the future. Its primary objective is to ensure independently, reliable and in a timely manner the proper functioning of corporate governance, risk management and the controls in place in order to mitigate current and emerging risks, considering the current and expected control environment in the future.

The Global Head of AIA, responsible for managing Allfunds Bank Group AIA as well as the rest of the members of AIA, is authorised to:

- Have access without any restriction to all of the Group information, departments, registries, properties and employees at any location, required to perform their functions.
- Have direct access to the Risk and Audit Committee, the Director General and the external auditors.
- Assign resources, determine the frequency of their reviews, select the departments and areas to be subject to such reviews, determine the scope of their work, value the need to perform audits and their scope and to use the necessary techniques to comply with the audit objectives.
- Obtain the necessary support from Allfunds employees, as well as any other specific services in or outside of Allfunds Bank.

### **Compliance and Anti-Money Laundering Unit**

The Compliance Area is divided into two units, Compliance Unit and Anti-Money Laundering Unit, which are independent of each other, and both managed by the Global Head of Compliance.

#### **Compliance Unit**

Allfunds Bank has an integrated Compliance Unit that ensures the proper and independent implementation of regulatory compliance, known and accepted by all the Group employees, ensuring the compliance risks and fostering a culture of compliance within the Group. For such purpose, it acts under the premises of independence, authority, objectivity, integrity, effectiveness and confidentiality:

- Periodically identifying and evaluating the indicators of compliance risk in the different business areas and establishing an annual program of supervision and control of the issues that are under its competence.
- Assessing the first line of defense in matters related to the compliance of the applicable regulations.
- Drawing up policies or preparing procedure manuals for the different business areas, as well as communications and training actions necessary for an adequate knowledge and awareness among employees.
- Advising and assisting both the Board of Directors and the Senior Management in relation to regulatory compliance matters, especially in the potential impact related to the developments in legislation.

Finally, the Compliance Unit reports to the Risk and Audit Committee through its quarterly reports and on an annual basis directly to the Board of Directors based on the results of the work performed and the associated risks, together with the proposals for mitigating measures that are considered adequate. Likewise, it will immediately inform the Board of Directors of any regulatory breach, incident or anomaly with special relevance.

### **Anti-Money-Laundering Unit**

Anti-Money Laundering (AML) and Countering the Financing of Terrorism (CFT) is an area of particular concern at Allfunds Bank. The commitment of Allfunds Bank on this is reflected in its Anti-Money Laundering and Countering the Financing of Terrorism programme (hereinafter, AML&CFT), and in the policies, procedures and controls developed in this programme.

The goal of Allfunds Bank in developing its AML&CFT programme is:

1. To protect the reputation of Allfunds Bank preventing it from being used for the illicit laundering of assets or movement of funds to support and/or finance terrorism; and
2. To help preserve the integrity of the financial system, as well as the supervision of the authorities in order to prevent money laundering, corruption and to combat the financing of terrorism.

In line with this goal, all entities belonging to Allfunds Bank regardless of their geographical location, must fully comply with applicable anti-money laundering and counter terrorism financing legislation.

Likewise the Anti-Money Laundering Unit reports to the Risk and Audit Committee and the Board of Directors, through its Regulatory Compliance reports.

The proper management of risks relating to money laundering and financing of terrorism requires the identification and analysis of risks relating to money laundering and the financing of terrorism to which Allfunds Bank is exposed, and the design and effective application of the policies and procedures that are proportionate to the risks identified. This risk analysis must take into account the type of customer, product and service offered, the distribution channels of the products and services, and the jurisdictions in which the customers of Allfunds Bank conduct their business.

The Board of Directors of Allfunds Bank approves and supervises the policies and procedures for managing AML&CFT and appoints the Head of AML&CFT, who is the Global Compliance Director, thereby ensuring sufficient independence and authority, and direct reporting to Senior Management and the Board of Directors. All this helps to ensure that the information is reported in a timely, comprehensive and accurate manner in regard to all questions linked to the efficient management of AML&CFT risks, in order to enable the Board and Management to take the necessary decisions.

Allfunds Bank has an updated AML&CFT Manual, which includes the policies and procedures relating to customers in the process of acceptance, as well as their monitoring and supervision in accordance with the AMLCFT program in place at Allfunds Bank. This Manual has been provided to all employees, and includes a clear description of their obligations, as well as guidelines on how to develop Allfunds Bank activities in compliance with applicable regulations. In this context, Allfunds Bank implements training plans adapted to the specific responsibilities and duties of each employee.

## **Risk Management**

The prudence applied by Allfunds Bank in risk management is a basic pillar in its activity and in the services provided to the customers. In turn, Allfunds Bank's organizational structure represents a system of clearly defined delegations for such risk management.

The general principles that guide the definition, monitoring and management of the risks are the following:

- The risks assumed must be compatible with the assets of Allfunds Bank Group and in accordance with the objective solvency level. In this regard, Allfunds Bank is committed to maintain a CET1 ratio of more than 17.50%.
- Willingness to maintain a "low" risk profile as a target through:
  - Maintaining the distribution activity, avoiding incorporating property positions into the balance sheet that generate risks that Allfunds Bank does not wish to assume.
  - The search for a high degree of diversification of structural risks, establishing limits to concentrations by customers, sectors, markets and/or geographies that may pose a threat to the solvency objectives, liquidity and recurrence of results.
  - Continuous attention to the tasks of identification and monitoring of risks, so that all areas are provided with adequate and dynamic systems that result in optimal management and control of the risks assumed.
- Existence of control and monitoring procedures for all the risks incurred by Allfunds Bank in the performance of its activity.
- Existence of solid management mechanisms and mitigation of operational and reputational risks.
- Independence of the risk function with respect to the business areas.
- Involvement of the organization in the philosophy of risk management.

The Board of Directors is responsible to establish Allfunds Bank's risk strategy. The Senior Management, with the support of the Risk Management Area, has delegated the following functions:

- Propose risk policies for Allfunds Bank and the level of risk assumed that Allfunds Bank considers acceptable.
- Authorize, where appropriate, the technical exceeded potentials that may occur within the assigned limits.
- Define the responsibility and functions of the people linked to risk management.
- Validate and, consequently, authorize internal and external reporting on risks.
- Supervise that the level of assumable risk is consistent with the strategic objectives set.
- Lead and lead the internal risk committee, which, among other functions, will review and approve the structure of limits that the Entity will establish for each risk factor.

Allfunds Bank Group's risk procedures are managed by the Risk Management Area, whose main mission is the control, monitoring and management of the risks arising during the Group's

activity. This mission is carried out on an ongoing basis taking into account the size, complexity and typology of Allfunds Bank's activity.

Allfunds Bank is currently reviewing its risk appetite framework and its risk appetite statement for each of the relevant risks to which it is exposed in the course of its activity. The main risks of Allfunds Bank and its management are reflected in the Prudential Relevance Report available on Allfunds Bank's public website.

## **2.- CONTROL ENVIRONMENT**

The Board of Directors of Allfunds Bank is the body in charge of the financial reporting and of ensuring there is an adequate internal control system in place, including administrative and accounting procedures. Additionally, the Board of Directors has an Risk and Audit Committee that meets on a quarterly basis and aims, among others, to advise the Board of Directors and to monitor the effectiveness of the control, audit and risk systems of Allfunds Bank.

However, the design of the control systems in connection with the financial reporting of the Allfunds Bank Group is supervised by the Allfunds Bank's Chief Executive. Furthermore, the effective implementation of control systems on financial reporting is the responsibility of Allfunds Bank's Finance and Management Control areas, in each of the Group's subsidiaries, as well as of the rest of areas involved or having an impact on the quality and reliability of the financial information used as a basis for preparing the Group's financial statements.

The finance area, the main area in charge of preparing the financial information, has its own functional organisational chart, which defines its lines of responsibility, duties and tasks. The organisational charts for these areas are updated whenever there are responsibility changes.

The General Code of Conduct of Allfunds Bank, approved by the Board of Directors in June 2016, is mandatory for all Group employees as well as for the Board of Directors, is well known and accepted by all of them. This General Code of Conduct establishes, among others, guidelines for conduct in relation to accounting obligations and financial information, requiring compliance with all internal control procedures established by the entity to ensure proper accounting of transactions and their proper reflection in the financial information published by the Group.

Additionally, the entity has a whistleblowing channel, which ensures the confidentiality of the same, as one of the processes established to guarantee the effective application of the applicable regulations, including financial and accounting irregularities. This channel provides a mean to encourage communication of breaches of the General Code of Conduct or specific codes and manuals or other irregularities, behavior, actions or events that may constitute an act allegedly illegal or professionally unethical that employees of the entity observed or those who have knowledge through customers, suppliers, partners and employees.

The finance area, and especially the employees in charge of the processes related to the preparation and review of Financial Information, receive constant training on accounting changes, changes in the regulations of the Bank of Spain and the Spanish Securities Commission. The training can be done internally, by attending specialized courses or by external consultants.

### **3.- RISKS ASSESSMENTS RELATED TO FINANCIAL REPORTING**

Allfunds Bank has established processes to identify the risks of errors in its financial reporting. The review of the scope of the different processes in order to identify such risks is carried out by using the financial information and other supplementary information as a basis.

When, during the year, there is evidence of, (i) previously unidentified circumstances that reveal potential errors in the financial information, or (ii) material changes in the Group's operations, the finance area assesses the existence of risks that should be added to the list of risks already identified.

Both the processes to identify financial reporting risks and the controls designed to monitor the relevant processes and activities, take into account all the goals of financial reporting based on materiality and on qualitative criteria, particularly focusing on the activities and processes most exposed to the risk of fraud and errors in estimates, and considering the principles of occurrence, integrity, detail and comparability. Specifically, the following objectives are set:

- Existence: All the assets (rights) and liabilities (obligations) recorded on the bank's balance sheet exist, and the transactions booked took place in the reference period,
- Totality: Not only do they exist, but all assets and liabilities are recorded at the closing of the balance sheet, along with the transactions that took place in the period.
- Valuation: The amounts at which the assets and liabilities have been booked, and the revenues and expenses recorded, were determined in accordance with generally accepted principles.
- Presentation: The information is sufficient, adequate and properly described and classified.

Within the finance area, the Group's Financial Reporting function is responsible for determining the Group's consolidation scope.

Subsidiaries are consolidated using the global integration method in the annual financial statements. As a result, all the balances and significant transactions between consolidated companies are removed during the consolidation process.

In that process the equity method will be applied for accounts belonging to jointly controlled entities, applying the exceptions provided in the applicable accounting regulations. This method will be also applied to associate entities.

As soon as the finance area is informed with regards to the acquisition of a investee, its inclusion in the consolidation scope is analysed and determined based on the foregoing considerations.

To determine the consolidation scope, Allfunds Bank takes into account, among others, the following types of risks: operating, technological, financial, strategic, market, legal, etc.

In preparing the risk assessment on financial information, a fundamental factor in assessing each process and its controls is the existence of valuation risk or the inclusion of estimates in their calculation.

The finance area is responsible for reviewing, at least once a year, whether or not there have been changes in the risks identified when the consolidated financial statements were prepared.

The main accounting policies including those relating to the identification of the Group's consolidation scope are described in detail in the annual report.

#### **4.- CONTROL ACTIVITIES**

The Internal Control processes for Financial Reporting at Allfunds Bank focus on ensuring the adequate record, valuation, presentation and breakdown of the transactions that are relatively important and, therefore, could affect the financial information. The accounts plan details the type of transaction covered, establishing the necessary procedures in order to keep them up to date.

Allfunds Bank has documented all the critical processes and activities which, due to their relevance, could impact on the financial information.

The accounting of Allfunds Bank and its subsidiaries is almost entirely automated and is automatically generated based on the record of the operation. Accordingly, particular attention is paid to manual accounting processes and the process of launching new services, activities or special operations.

Regarding manual accounting procedures, it is important to highlight that manual accounting entries are limited to users specialized in the area of operations and accounting. The entries are entirely traceable and always include the ID of the user making the entry together with its description. The Financial Area has developed a daily verification procedure to check that the manual entry is within the scope of the user with the aim to identify errors and/or fraud.

The appearance and launching of new services or the beginning of a new activity, special operations or any other event with an impact on the financial statements may be assessed from an accounting standpoint to ensure that the financial information generated is reliable and meets applicable accounting standards. Under this light, the Financial Area is informed by the areas implementing the various initiatives, in order to analyse and determine the applicable accounting policies, to provide, inventory definitions, required regulatory information and any other aspect with an impact on the financial statements.

In addition to the controls related to the procedures and activity, second level controls are implemented in order to detect material errors that might affect the financial information. Among these controls, we highlight the cross-checks between inventories and accounting databases, controls of inflows and outflows and miscellaneous, control of items pending application, cash accounts reconciliation, deviations from budgets, control of entries involving high amounts, etc.

Allfunds Bank's information systems relating to the preparation of financial information, either directly or indirectly, constantly guarantee that the financial information is properly compiled and published, through a specific internal control system.

Allfunds Bank has specific internal procedures that govern the management of access to the applications and systems in line with an array of profiles adapted to the different functions of each workstation.

Allfunds Bank has infrastructure in the data processing centers of Banco Santander, S.A. These processing centers comply with all the necessary safety and environmental measures. Furthermore, Prohuban, technological provider belonging to Santander's Group specialized in the design, setting up, maintenance and operation of the technological infrastructure, provides Allfunds Bank with user station and security/cybersecurity services. Periodically the service provision is monitored through committees established between Allfunds Bank and Prohuban. The controls defined by our supplier are reviewed on an annual basis in order to evaluate the level of compliance with the security measures established for the provision of the service.

The Technology Area has devised a Business Continuity Plan (BCP) for Allfunds Bank. In the event of a contingency, this enables data and information systems to be recovered in a timely manner, without a loss of content. At least once a year, the plan is partially tested to verify that it is properly working.

Allfunds Bank must also ensure in general terms that the delegation or outsourcing of functions or services (including those of an essential nature) is not carried out in a way that the quality of internal control and the ability of regulators to monitor the compliance of the obligations derived from the applicable laws and regulations may be materially impaired. To this end, the Board of Directors of Allfunds Bank has approved the Policy for Outsourcing Services. Allfunds Bank will adopt at all times the necessary measures in order to prevent that certain risks (image, regulatory and / or operational) will be materialized taking into account that outsourcing can be critical for the provision of satisfactory and continuous services to our customers and, therefore, to carry out their activities in a convenient way.

Therefore, when certain essential functions for Allfunds Bank are outsourced, the internal control capacity should not be lower than if it were carried out internally, and these third parties must also have control and safeguard mechanisms in their computer systems and contingency plans for damages or catastrophes that guarantee the continuity of the service provided.

Likewise, the entities of the Group provide to each other different services and mutual assistance among them.

## **5.- INFORMATION AND COMMUNICATION**

The finance area is responsible for the quality, transparency and adequacy of the individual and consolidated financial information, including it being based on suitable accounting methods.

To meet these basic goals regarding financial information, it is considered necessary to formally create a specific function in charge of defining and constantly updating Allfunds Bank's accounting policies, as well as to solve any queries or disputes arising from the interpretation of accounting standards.

This function is undertaken by the finance area, which resolves any conflict of interest that might arise between the different areas and directors within Allfunds Bank, regarding how to interpret or materialise the financial information in the different reports following the applicable guidelines and the accounting principles and policies that have been defined.

The accounting regulatory framework defines the policies applicable to the Group and allows the financial statements to show a true and fair view of the equity and financial situation, which

includes i) the Commercial Code and other commercial legislation, (ii) International Financial Reporting Standards adopted by the European Union, and (iii) Circular 4/2017 dated 27 November issued by the Bank of Spain.

The main IT systems and applications involved in generating the financial information used by Allfunds Bank are centralised and interconnected. There are procedures and controls that ensure the proper development and maintenance of these systems, as well as their correct operating, continuity and security.

Automatic accounting is parameterized and defined, subject to prior analysis and cross-checking, by the finance area so as to guarantee compliance with applicable regulations and the Group's accounting policies.

Consolidation of the Group's financial statements is a manual process underpinned by the use of Excel work sheets, a process considered sufficient based on the current consolidation scope.

## **6.- SUPERVISION OF THE INTERNAL CONTROL SYSTEM**

AIA is responsible for verifying that Allfunds Bank effectively complies with the different internal procedures established and that the different departments are operated and governed by them. To achieve this goal, AIA carries out the necessary controls and the results are escalated to the corresponding Risk and Audit Committee. The Risk and Audit Committee is responsible not only for the necessary follow-up to determine the effectiveness of the internal control systems, internal audit and risk management of the Company, but also verifies that the Board of Directors adopts, in due time, the necessary corrective measures to solve the deficiencies of internal control, non-compliance with laws, regulations and policies and other problems identified by the auditors.

In addition, the Risk and Audit Committee has as objectives to supervise the external auditor of the Company, propose the appointment, remuneration and dismissal of the external auditor, review and approve the scope and frequency of the audits and review the audit reports and monitor the establishment of accounting policies by the Company.

The above mentioned mechanisms have the aim of having the internal control system of Allfunds Bank working in the most accurate manner.

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