



PKO BANK POLSKI
SPÓŁKA AKCYJNA

DIRECTORS' REPORT
ON THE ACTIVITIES OF
POWSZECHNA KASA OSZCZĘDNOŚCI
BANK POLSKI SPÓŁKA AKCYJNA GROUP
IN 2005

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1. INTRODUCTION

Powszechna Kasa Oszczędności Bank Polski Spółka Akcyjna ("PKO BP SA", "the holding company", "the Bank") is the holding company of the Powszechna Kasa Oszczędności Bank Polski Spółka Akcyjna Capital Group ("the Group", "the Capital Group", "the PKO BP SA Group").

The PKO BP SA Capital Group reported in 2005 a positive net financial result of PLN 1,735 million, mainly due to the performance of PKO BP SA.

2. EXTERNAL FACTORS AND EVENTS WHICH ARE SIGNIFICANT TO THE GROUP'S PERFORMANCE

2.1 Macroeconomic factors

During the year 2005, the economic growth slowed down in comparison with the year 2004. According to preliminary estimations of GUS (Central Statistical Office), the growth of GDP in the most recent year amounted to 3.2%, compared to 5.3% in the year 2004. The main reason for the economic slow-down which took place in the first half of 2005 was the decline in internal demand due to the following factors: smaller growth of consumption (the effect of extinguishment of the consumption boom from the period of Poland's accession to EU), smaller growth of investments (the effect of greater than expected difficulties with acquiring financing from the EU aid funds, weaker domestic demand, appreciation of Polish zloty and increase in real interest rates) as well as a smaller increase in inventories compared to the period of Poland's accession to EU. However, in the second half of the year, the Polish economy saw certain signs of improvement: gradual increase of people's real income resulted in moderate revival in individual consumption, while the continued good financial performance of enterprises and decreased interest rates, combined with gradual restoration of domestic demand and the continued inflow of direct foreign investments contributed to moderate growth of investments. At the same time, throughout the whole period under analysis, the main driver of economic growth was the decrease in foreign trade deficit.

Despite the economic revival in the second half of 2005 and the overall improvement in companies' financial standing, in 2005 only a slight improvement was observed in the labour market. In December 2005, official unemployment rate decreased by 1.4 percentage points and amounted to 17.6%, with 2.8 million persons without regular employment.

After the period of a significant growth in the inflation rate (4.4% year-to-year at the end of 2004), the inflation rate in 2005 showed a declining trend. In the second half of the year, the inflation rate was slightly below the borderline for the inflation target of the National Bank of Poland (NBP) and oscillated around 1.5%, which was within the bottom range of fluctuations of the inflation rate around the NBP's target. The decrease of the inflation rate in the second half of the year 2005 was mainly the effect of the so called "high reference base", i.e. a considerable increase in prices in the corresponding period of the year 2004 resulting from Poland's accession to the European Union. Moderate salary increases and appreciation of the Polish zloty were also conducive to the decrease in the inflation rate. On the other hand, inflation was boosted by fuel prices, which were increasing over a prevailing part of the year due to increases in the prices of crude oil on the world markets. Eventually, the inflation rate as at the end of 2005 amounted to 0.7% on a year-to-year basis. In 2005, the average inflation rate was 2.1%, compared to 3.5% in 2004.

In 2005, household deposits increased by 3.6% due to a slow increase in the level of household income. However, the decreases in the NBP interest rates and the resulting decreases in the interest rates of bank deposits brought about a decrease in the share of bank deposits in the household savings' structure. At the same time, a growing proportion of household savings was kept in the form of trust fund units, shares or life insurance policies. The reluctance of enterprises to increase the size of investments, combined with good financial performance of enterprises, contributed to a considerable increase in the level of corporate deposits. As a result, the value of corporate deposits in December 2005 was almost 17% greater than in the corresponding period of 2004.

Household loans continued to grow during 2005, especially housing loans, which, among others, was due to the increasing level of household income and decreasing interest rates. In mid 2005, a small growth was noted in corporate loans, which, to a large extent, was due to low reference base, as



monthly increases only slightly exceeded or approximated those noted in the previous year. The decline in the growing trend was due to the reluctance of enterprises to launch new investment projects and the relatively small use of external financing.

At the same time, the Group's results were affected by the macroeconomic factors in Ukraine where the subsidiary of PKO BP SA – KREDOBANK SA operates. The main factors include:

- In 2005, the pace of the economic growth slowed down, due to the deterioration of price relations in foreign trade (decline in the prices of steel – the main export product of Ukraine and increase in the prices of crude oil – imported raw material) and little increase of investments (due to unstable political situation). According to preliminary estimates, the pace of this growth in 2005 amounted to 2.4%, compared to 12.1% in the whole year 2004.
- In 2005, on the labour market a decline was noted in the unemployment rate to 3.1% (in December 2005), compared with 3.5% in December 2004. According to the International Monetary Fund, the unemployment rate in real terms is at a much higher level of 8-12%.
- In 2005, the inflation rate dropped to the level of 10.3% y/y, compared to 12.3% in December 2004. The high level of inflation was supported by: increase in demand due to the rise in salaries in the public sector and pensions at the turn of 2004 and 2005 at the time of the election campaign; gradual rise in administrative prices that were held at an underestimated level at the end of 2004. The sharp rise in the prices of crude oil boosted the inflation rate in the first half of the year (up to 14.4%) and the subsequent stabilization of these prices resulted in inflation decrease in the last months of 2005.
- In 2005, the growth of the total value of deposits amounted to app. 60% y/y, compared to 35% y/y in December 2004. In 2005, there was a significant growth in the value of deposits held in domestic currency (over 65% y/y, compared to 31% at the end of 2004), and a smaller growth in the value of deposits held in foreign currency (about 50% compared to 53% in December 2004). The change of the current trends may have resulted from a slight increase in the interest rates on deposits held in domestic currency and a decrease in the interest rates of foreign currency deposits, as well as appreciation of the Ukrainian currency (hryvna - UAH).
- The value of granted loans increased by 61.9% y/y in December 2005, compared to 30.5% in December 2004. The growth in the value of granted currency loans was about 66.3% and was higher than the growth in domestic loans by app. 58.7%. Increase in the growth of domestic loans was due to the falling interest rates, while the sharp increase in the value of foreign currency loans could have been the effect of appreciation and favourable prospects for the rate of UAH. The biggest increase was noted in the category of long-term foreign currency loans (almost 100% y/y in December 2005).
- The monetary policy of the National Bank of Ukraine in 2005 was still focused on the exchange rate level. In the face of a continued very high inflation [and] aggressive fiscal policy, the National Bank of Ukraine undertook activities aiming at the tightening of the monetary policy. In April 2005, the Central Bank allowed a 3% appreciation of the Ukrainian currency, as a result of which the rate of UAH at the end of 2005 was 5.05 UAH/USD, compared to 5.30 at the end of 2004.
- As a result of frequent interventions of the NBU on the currency market, involving the purchase of US dollars (in order to avoid the more significant growth of the value of UAH), there was a significant increase in currency reserves. At the end of December, the value of reserves grew up to almost USD 19.5 billion.
- In August 2005, the Central Bank raised the main interest rate by 50 b.p. up to the level of 9.5%, due to the high level of inflation and the high money supply in the economy.

2.2 Monetary policy of the National Bank of Poland

Pursuant to the NBP's "Monetary Policy Assumptions for the Year 2005", maintaining the annualised inflation rate at 2.5%, with allowable fluctuations of +/-1 percentage point, was the main objective in 2005. The macroeconomic data published in the first half of 2005 (relating mainly to the growth of GDP and, in particular, domestic demand) proved to be worse than expected, which resulted in NBP decreasing its projections with regard to future GDP and inflation. As it became more probable that the inflation rate in 2005-2006 will be below the NBP's inflation objective, the Polish Monetary Policy Council decided to decrease interest rates in the period from March to August by 200 base points



altogether (by 225 base points in the case of the bills of exchange rediscount rate). As a result, at the end of 2005, the NBP reference rate amounted to 4.5%.

2.3 Financial market

During the year 2005, a significant decrease was recorded in the profitability of the State treasury debt securities, which varied from 190 b.p. in the case of short-term instruments to 80 b.p. in the case of long-term bonds. At the same time, in the fourth quarter of 2005 the profitability of Treasury securities increased, mainly due to increased uncertainty relating to the development of political situation after the September Parliamentary and October Presidential elections. Another factor which contributed to the decrease in the prices of Polish Treasury securities was related to the fact that investors no longer expected any further decreases in interest rates by the Monetary Policy Council.

In 2005, the Polish zloty appreciated by more than 5% in relation to euro and depreciated by 9% in relation to US dollar (data at the year-end). The depreciation of the Polish zloty in relation to the US dollar was due to a strong appreciation of the US dollar on the world markets in 2005. The appreciation of the effective PLN rate (weighted by the share of the particular currencies in the Polish exports) was due to the fact that the foundations of the Polish economy continued to be positive, as well as due to the positive influence of Poland's accession to the European Union and the high demand from investors for Central European currencies.

2.4 Regulatory environment

Major changes in the external regulatory environment which had an influence on the position of the PKO BP SA Group in 2005 related to the following:

- Amendments of 27 August 2004 (Journal of Laws No. 213 item 2155), which imposed an obligation on listed companies to prepare their consolidated financial statements in accordance with the International Accounting Standards, International Financial Reporting Standards, as well as amendments to executive regulations in the area of accounting, including the Decree of the Minister of Finance dated 10 December 2001 on the specific accounting principles for banks (Journal of Laws No. 149 item 1673 with subsequent amendments), which requires that banks measure specific financial assets and liabilities at amortised cost using the effective interest rate method,
- New rules regulating the functioning of the capital market, introduced as of 24 October 2005 by three acts comprising the new capital market law: the Act on Capital Market Supervision, the Act on Trading in Financial Instruments and the Act on Public Offering, Conditions Governing the Introduction of Financial Instruments to Organised Trading, and Public Companies; together with executive regulations, those acts created conditions for further liberalisation of the capital market and increase in competition by, among others, allowing brokers to carry out transactions in securities outside the stock exchange market, enabled better protection of investors' interests, introduced changes to the reporting requirements for issuers of securities listed on the stock exchange market and made it easier to undertake brokerage activities as well as resolved taxation issues in the umbrella-type funds, which should boost the growth of such funds;
- Changes in the definition of "own funds", modification of prudence regulations, including changes in calculation of capital adequacy, made on the basis of the Banking Law Act amended in 2004 (Journal of Laws No. 91 item 870) and the executive regulations issued for this Act (Resolution 4/2004 of the Banking Supervisory Commission and Resolution 6/2004 of 8 September 2004 – NBP Journal No. 15 items 25 and 27);
- Amendments to the VAT Act and the related executive regulations relating to, among others, tax reliefs for bad debts, definition of taxable income, new exemptions in the scope of taxable trading, list of deductible input VAT items;
- Increase in banks' costs due to increased protection of consumer rights (relates to the loss of copies of certain banking documents by the clients), resulting from the Banking Law amended in 2004 (Journal of Laws No. 91 item 870);
- Decrease in the banks' share in the EU Guarantee Fund (*Fundusz Poręczeń Unijnych*) in relation to the interest revenues from the obligatory reserve, according to the Law on the EU Guarantee Fund (Journal of Laws 2004, No. 121 item 1262);



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- Reduction of banks' costs relating to the bank deposits guarantee system, resulting from the decrease in the obligatory annual payment and the ratio determining the amount of the guaranteed funds;
 - New requirements for banks concerning banking secrecy, resulting from the amendments to the Act on Protection of Classified Information;
 - Modified requirements for reporting to the Securities and Exchange Commission (KPWiG) as well as the National Bank of Poland and the General Inspectorate for Banking Supervision (GINB) in respect of information required for defining monetary policy and assessing country's monetary situation, banks' financial standing and banking risk, as well as additional reporting requirements (effective from 30 June 2005) relating to taxation of interest on deposits held by non-residents and requirements relating to identification of such individuals;
 - Changes in the conditions that must be met while carrying out brokerage activities, including with respect to services provided, settlements processing, transaction recording, loan collaterals, issuing loans for the purchase of securities admitted to public trading by banks conducting brokerage activities, as introduced by the Decree of the Council of Ministers dated 19 April 2005 and the amended reporting requirements concerning brokerage and trust fund activities;
 - Changes in tax proceedings resulting from the amended Tax Ordinance Act, including in authorisation for taxpayers to issue guarantees and grant suretyships in order to secure tax liabilities;
 - New and amended supervisory legislative solutions binding for banks operating in Ukraine, including liquidity risk, currency risk, mandatory reserves and specific reserves,
 - Amended Act on the organization and functioning of pension funds,
 - New regulations concerning operating risk management, determined in Recommendation M of the Chief Inspector for Banking Supervision.

Most of the above changes in the regulatory environment resulted in additional financial and organisational expenditures incurred by the PKO BP SA Group. Conversion to IAS/IFRS and creation of new reporting requirements by the Central European Bank obliged the Bank and its subsidiaries to introduce new formats for the Bank's reporting to the Securities and Stock Exchange Commission, the National Bank of Poland and the Banking Supervisory Commission, which required adapting information systems and personnel training. Implementation of new accounting IAS/IFRS standards affected both the amount and the structure of the Bank's assets and liabilities, including the amount of the Group's equity, the amount and structure of its financial results (including net interest income, result on financial instruments, result on investments in securities, foreign exchange result, operating expenses) as well as the level of the capital adequacy ratio.

In addition, the Group's activities in the year 2005 were also affected by the preparation for the introduction of new capital adequacy regulations based on the New Capital Accord (Basel II Accord).

2.5 Competition in the banking sector

Banking sector

In 2005, majority of banks observed an increase in income from banking activities and a significant improvement in the efficiency of operations. As a result, the banking sector reported the highest ever financial result. The most important factors that affected the development of the banking sector were as follows:

- increasing competition on the banking services market, resulting, among others, in:
 - development of financial services offered by non-banking institutions,
 - extension and modernisation of banking products for individual and corporate customers, in particular products relating to housing loans, *bancassurance*, capital market products, products enabling assimilation of the EU aid funds; banks have diversified the prices of their services by promoting loyalty programs and packages;
 - e-banking development, including the development of credit card products and on-line services for individual and corporate customers;



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- extension of distribution channels for banking products; banks increased the number of outlets, concluded agreements for cooperation with financial intermediaries, agreements for mutual cash dispenser services and developed direct and Internet sales; the development of business activities was accompanied by an increase in the level of employment and the standard of customer service;
 - reducing operating expenses via *outsourcing* – more and more banks opted for *outsourcing* in certain areas of their activities; this related in particular to administrative functions, IT support, legal services, debt collection and card processing;
 - entrance of new foreign competitors to the Polish banking market – nearly 90 foreign banks, mainly from the European Union, expressed their interest in providing products and services in a cross-border form in the area of real estate financing, mortgage loans, asset management, servicing the most affluent clients, as well as the provision of financial services to local governments;
 - merger of European financial groups, UniCredito and HVB, resulting in the potential formal merger of two Polish banks – Pekao SA and BPH SA.

Changes in the non-banking competitive environment of the Group

Changes in the non-banking environment of the PKO BP SA Group related to both to the environment of the Bank and that of its subsidiaries.

- Among other sectors of the non-banking financial market, the investment funds market was growing most rapidly, which resulted in the growth of competition in relation to bank deposits. There was an increase in both the number of investment fund companies (TFIs) and the number of funds managed by these companies. Assets managed by investment fund companies rose by 62.5% compared to the balance as at the end of 2004 and amounted to PLN 61.3 billion at the end of 2005. This meant a significant increase in the share of investment funds in the absorption of household savings. Collaboration between investment fund companies and banks, including banks from the same capital group, became stronger. The investment fund companies selling participation units in bank outlets noted the biggest inflow of cash. The importance of electronic channels in the distribution of participation units was rising. The investment fund companies were introducing new product initiatives. They introduced the umbrella-type funds, the securitization funds (the first securitization fund on the Polish market was founded by TFI PKO/Credit Suisse) and expanded the scope of their activities to include asset management. Having noticed good conditions on the real estate market, they created funds investing on the real estate market. Together with banks, they also prepared structured products.
- The open pension funds market developed dynamically. During the year 2005, the assets managed by pension fund companies rose by approximately 37%, exceeding the level of PLN 86 billion. The number of pension fund customers increased. At the same time, competition on this market also increased, which resulted in the movements of customers between different funds. Treasury securities predominated in the structure of open pension fund deposits. The funds diversified their investments in listed companies.
- There was a significant increase in trading on the Stock Exchange – in 2005, turnover was 65% higher than in 2004. The revival on the Stock Exchange resulted in an increase in the prices of shares, which was reflected in the growth of the main stock exchange indices, WIG and WIG20.
- There was a revival on the life insurance market, which was a source of competition for bank deposits. More and more insurance companies started to operate in the area of bancassurance and used electronic distribution channels to sell their services.
- The process of equity changes initiating the consolidation process on the investment funds market, pension funds market and on the insurance market was carried out. It can be expected that the process will be continued in 2006.
- Foreign entities started to operate on the investment fund market and in the insurance sector, based on the uniform passport formula.
- The importance of financial intermediary entities on the market of housing loans, investment funds (including foreign funds) and insurance funds was increasing. The most dynamically growing



entities based their activities on collaboration with several banks, investment funds and insurance companies. The activities of intermediaries dealing on the country-wide domestic market have become stronger. New entities dealing on the domestic market started their activities.

- The lease services market grew rapidly, although it clearly slowed down compared to 2004. The slowdown was the effect of decrease in the value of financed vehicles, which continue to represent the largest segment of this market. To compensate the drop of interest in the leasing of cars, leasing companies financed more and more machines and equipment. The real estate lease market developed dynamically too. Leasing companies developed the so called "tailored services" – adjusted better and better to the needs and financial capability of the customer. Growing competition resulted in the decrease of margins and profits reported by leasing companies.
- A revival was observed in the private equity/venture capital sector. Similarly to the previous years, this sector operated mainly based on capital acquired abroad.
- There was a high but stable growth in the Ukrainian banking market. The retail market developed most dynamically. There was a continued deficit of capital. New banks have been registered, most of them with the participation of foreign capital. Decreases in interest rates resulted in the growth of market competition. Consolidation process could be noted on the market, mainly on the initiative of foreign investors.

3. THE PKO BP SA GROUP'S DEVELOPMENT STRATEGY FOR THE YEARS 2006-2008

In 2005, the development of the PKO BP SA Group was entirely subordinated to the implementation of the PKO BP SA Strategy for the years 2003-2005. The Bank's subsidiaries supplemented its business offer in order to support its position of the leader of the Polish banking market. In 2005, certain initiatives were undertaken for the growth of the Capital Group, including in the segment of pension funds, investment funds, development activities and activities conducted on the markets of Central and Eastern Europe.

On 8 December 2005, the Supervisory Board of the Bank approved the Strategy of PKO BP SA for the years 2006-2008. This is an Innovation Strategy which provides for the growth of an effective Capital Group, to be achieved by the development of activities on European markets, including expansion to the most attractive markets of the Central and Eastern Europe. New capital involvements will be focused on widening the possibilities of distribution of the Bank's products and services. The Bank, as the holding entity of the Group, will take part in the processes of consolidation of the Polish financial sector and will strengthen its position on foreign markets.

In the Bank's view, capital investments and other investment initiatives are possible to achieve and will be adequate to the resources held by the Group.



4. ORGANISATION OF THE PKO BP SA GROUP

As of 31 December 2005, the PKO BP SA Group consisted of PKO BP SA as the holding company and 16 direct or indirect subsidiaries of the Bank.

In 2005, there were no changes in the basic principles of Group management.

4.1 Entities included in the consolidated financial statements

These consolidated financial statements include the Bank – which is the holding company of the PKO BP SA Group, and the Bank's subsidiaries, as defined in IAS 27 "Consolidated and separate financial statements".

Table 1. Entities comprising the PKO BP SA Group

No.	Company	Value of involvement at acquisition price	Percentage of share capital	Consolidation method
		PLN thousand	%	
Holding company				
1	Powszechna Kasa Oszczędności Bank Polski Spółka Akcyjna			
Direct subsidiaries				
2	Powszechne Towarzystwo Emerytalne BANKOWY S.A.	205 786	100.00	Full
3	PKO Inwestycje Sp. z o.o.	153 403*	100.00	Full
4	Centrum Finansowe Puławska Sp. z o.o.	128 288	100.00	Full
5	KREDOBANK S.A. (former Kredyt Bank (Ukraina) S.A.)	111 970	69.018	Full
6	Inteligo Financial Services S.A.	59 602	100.00	Full
7	Centrum Elektronicznych Usług Płatniczych eService S.A.	55 500	100.00	Full
8	Bankowy Fundusz Leasingowy S.A.	30 000	100.00	Full
9	Bankowe Towarzystwo Kapitałowe S.A.	18 566	100.00	Full
Indirect subsidiaries				
Subsidiaries of PKO Inwestycje Sp. z o.o.				
10	Wilanów Investments Sp. z o.o.	82 981	100.00	Full
11	Fort Mokotów Sp. z o.o.	32 130	51.00	Full
12	POMERANKA Sp. z o.o.	19 000	100.00	Full
13	UKRPOLINWESTYCJE Sp. z o.o.	182	55.00	Full
Subsidiary of PTE BANKOWY S.A.				
14	Finanse Agent Transferowy Sp. z o.o.	1 861	100.00	Full

* including PLN 5.5 million of a specific extra payment.



Table 2. Other subordinated entities included in the consolidated financial statements

No.	Company	Value of involvement at acquisition price	Percentage of share capital	Consolidation method
		PLN thousand	%	
Jointly controlled entities				
1	Centrum Obsługi Biznesu Sp. z o.o.	17 498	41.44	Equity method
2	PKO/CREDIT SUISSE Towarzystwo Funduszy Inwestycyjnych S.A.	14 000	50.00	Equity method
3	WAWEL Hotel Development Sp. z o.	13 865	35.40	Equity method
Associates				
4	Bank Pocztowy S.A.	146 500	25.0001	Equity method
5	Kolej Gondolowa Jaworzyna Krynicka S.A.	15 531	37.83	Equity method
6	Ekogips S.A. – in liquidation	5 400	60.26	Equity method
7	Poznański Fundusz Poręczeń Kredytowych Sp. z o.o.	1 500	33.33	Equity method
8	Hotel Jan III Sobieski Sp. z o.o.	522	32.50	Equity method
9	Agencja Inwestycyjna CORP S.A.	29	22.31	Equity method
Associate of Bankowe Towarzystwo Kapitałowe SA				
10	FINDER Sp. z o.o.	5 555	42.31	Equity method

Due to immateriality of financial data, the following entities of the Group have never been included in consolidation:

- International Trade Center Sp. z o.o. in liquidation,
- Przedsiębiorstwo Informatyki Biznesowej "Elbank" Sp. z o.o. in liquidation,
- Sonet Hungary Kft in liquidation (a subsidiary of Inteligo Financial Services SA).

4.2 Changes in the organization of subsidiaries, associates and jointly controlled entities

In 2005, the following events had an impact on the structure of the PKO BP SA Group:

- Acquisition of shares in the increased share capital of Centrum Obsługi Biznesu Sp. z o.o.

On 25 January 2005, PKO BP SA acquired 34,992 shares, accounting for 41.44% of the company's share capital and votes at the shareholders' meeting. The acquisition cost amounted to PLN 17,498 thousand.

The Company is a joint venture of the Bank, the City of Poznań and Buildco Poznań S.A. with its registered office in Luxembourg. The main area of its business activities is the construction and operation of a hotel located in Poznań, which will be managed by an international hotel chain operator, Sheraton.

- Incorporation of POMERANKA Sp. z o.o.

On 31 March 2005, a deed of incorporation of POMERANKA Sp. z o.o. was signed. At the date of incorporation, the following subsidiaries of PKO BP SA were the shareholders of this Company:

- PKO Inwestycje Sp. z o.o., which acquired and paid for 498 shares with a total value of PLN 49,800,



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- Bankowe Towarzystwo Kapitałowe S.A. (former Dom Maklerski BROKER S.A.), which acquired and paid for 2 shares with a total value of PLN 200.

On 11 April 2005, the Company was registered with the National Court Register.

On 20 April 2005, PKO Inwestycje Sp. z o.o. purchased from Bankowe Towarzystwo Kapitałowe S.A. 2 shares in POMERANKA Sp. z o.o., and thus became the holder of 100% of shares in the company's share capital and obtained the right to exercise 100% of votes at its shareholders' meeting.

On 6 May 2005, PKO Inwestycje Sp. z o.o. took up new shares in the increased share capital of POMERANKA Sp. z o.o. with a value of PLN 3,950 thousand. Following this increase, the share capital of POMERANKA Sp. z o.o. amounts to PLN 4 million and consists of 40,000 shares with a nominal value of PLN 100 each.

The Company was set up in order to carry out development projects.

- Completion of the liquidation proceedings of the Bank's subsidiary – PKO Towarzystwo Finansowe Sp. z o.o.

On 22 February 2005, the Company was deleted from the National Court Register.

- Change of the name and the scope of activities of Bankowe Towarzystwo Kapitałowe S.A. – formerly Dom Maklerski BROKER S.A.

As part of implementation of the adopted strategy, the Company's activities relating to brokerage services were transferred to Bankowy Dom Maklerski PKO BP SA. This process was completed on 1 April 2005.

On 24 March 2005, the Company's Extraordinary General Shareholders' Meeting resolved to change the Company's Articles of Association, including changing its name to Bankowe Towarzystwo Kapitałowe S.A. and changing of the scope of its activities to venture capital activities.

These changes were registered with the National Court Register on 7 April 2005.

- Incorporation of UKRPOLINWESTYCJE Sp. z o.o. with its registered office in Kiev.

On 10 August 2005, UKRPOLINWESTYCJE Sp. z o.o. was registered with the Uniform National Register of Enterprises and Organisations of Ukraine. The company's share capital amounts to the hryvna equivalent of USD 100,000 and consists of 100 shares with a nominal value amounting to the hryvna equivalent of USD 1,000.

The Company's shareholders are:

- PKO Inwestycje Sp. z o.o. (a subsidiary of the Bank), which took up 55 shares accounting for 55% of the company's share capital,
- JEDYNKA S.A. (with registered office in Rzeszów), which took up 30 shares accounting for 30% of the share capital,
- ETALON INCEST (Ukrainian company), which took up 15 shares accounting for 15% of the share capital.

The main task of the Company is to undertake activities aimed at carrying out investment projects in Kiev or other Ukrainian cities.

- Registration of share capital increase of Kolej Gondolowa Jaworzyna Krynicka S.A.

On 29 September 2005, an increase in the Company's share capital was registered with the National Court Register, amounting to PLN 426,250. The shares in the increased share capital were taken up by the City of Krynica Górská. Following this increase, the Company's share capital amounts to PLN 41,053,150 and consists of 821,063 shares with a nominal value of PLN 50 each.

As a result of the increase in the Company's share capital, the Bank's share in its share capital decreased from 38.23% to 37.83%, and the Bank's share in votes at the Annual General Meeting decreased from 37.03% to 36.85%.

- Purchase of shares in KREDOBANK S.A. (the former Kredyt Bank (Ukraine) S.A.) from minority shareholders



PKO BP SA, acting through Przedsiębiorstwo „Rosan – Papiery Wartościowe” Sp. z o.o. with registered office in Lvov, submitted a proposal to the minority shareholders of KREDOBANK S.A. for the purchase of shares held by these shareholders. As a result, the Bank acquired 339,763,026 shares from the minority shareholders, accounting for about 2.367% of the Company's share capital. The price paid for the shares, including any additional fees and commission, amounted to PLN 2,439,350.

As a result of the above transaction, the Bank holds 69.018% of shares in the Company's share capital, which give right to 69.018% of votes at the Company's Annual General Meeting.

- Purchase of shares in Wilanów Investments Sp. z o.o.

On 3 November 2005, the Bank's subsidiary – PKO Inwestycje Sp. z o.o. acquired from Prokom Investments S.A., on the basis of a sale agreement, 1,960 shares in Wilanów Investments Sp. z o.o., of a total nominal value of PLN 1,960 thousand, accounting for 49% of the Company's share capital. The price paid for these shares, amounted to PLN 66.661 thousand, including additional fees.

As a result of the above transaction, PKO Inwestycje Sp. z o.o. holds 100% of shares in the Company's share capital, which give right to 100% of votes at the Company's Shareholders' Meeting.

- Purchase of shares from FINDER Sp. z o.o.

On 9 December 2005, the Bank's subsidiary - Bankowe Towarzystwo Kapitałowe S.A. acquired from a natural person, on the basis of sale agreement, 1,930 shares of FINDER Sp. z o.o. with a total nominal value of PLN 965 thousand. The price paid for the shares, including any additional fees, amounted to PLN 5,555 thousand.

As a result of the above transaction, Bankowe Towarzystwo Kapitałowe S.A. holds 42.31% of shares in the Company's share capital, which give right to 42.31% of votes at the Company's Shareholders' Meeting.

- Change of the name of KREDOBANK S.A. – former Kredyt Bank (Ukraina) S.A.

On 17 November 2005, the Extraordinary General Meeting of Kredyt Bank (Ukraina) S.A. resolved to change the Company's name to "KREDOBANK" S.A. and to change the Company's logo.

On 23 December 2005, the National Bank of Ukraine registered the amendment to the Company's Articles of Association introducing the new name of the Company.

- Activities aimed at increasing control over PKO/Credit Suisse Towarzystwo Funduszy Inwestycyjnych S.A.

On 22 December 2005, the Management Board of the Bank notified the Securities and Exchange Commission of its intention to purchase registered shares of PKO/Credit Suisse Towarzystwo Funduszy Inwestycyjnych S.A. accounting for 25% of votes at the Annual General Meeting. As a result of this transaction, the Bank will hold the Company's shares accounting for 75% of its share capital and votes at the Annual General Shareholders Meeting.

5. MAJOR EVENTS THAT HAD AN INFLUENCE ON THE ACTIVITIES AND RESULTS OF THE PKO BP SA GROUP

The main events which influenced the activities and results of the PKO BP SA Group in 2005 were connected with the business activities carried out by the Group companies and positive results achieved by the particular entities in the Group and have been described in the following sections of this Directors' Report.



6. PERFORMANCE OF THE PKO BP SA GROUP¹

6.1 PKO BP SA activity – the holding company of PKO BP SA Group

PKO BP SA is a universal bank that deals with individual persons and legal entities and other domestic and foreign entities. PKO BP SA may possess foreign currency as well as make foreign transactions and open and hold bank accounts in foreign banks and put funds into these accounts.

At the end of 2005:

- the Bank's gross interest-bearing assets amounted to PLN 84.5 billion and increased by PLN 6.7 billion (i.e. 8.6%) compared to 31 December 2004, of which gross loans of PKO BP SA amounted to PLN 48.7 billion and since the beginning of the year increased by PLN 7.6 billion (i.e. 18.5%). Loans accounted for 58% of the total amount of interest-bearing assets and, compared to the end of 2004, this share increased by 5 pp. due to the growth in the balance of loans which amounted to 118.5%.
- the Bank's interest-bearing liabilities amounted to PLN 78 billion and increased by PLN 4.8 billion (i.e. 6.5%) since the beginning of the year. Retail banking deposits accounted for 68.6% of the total amount of deposits and, compared to the balance at the end of 2004, this share decreased by 3.7 p.p., for the benefit of the other types of deposits. In relation to 2004, retail banking deposits increased by 1.1%, housing deposits increased by 20.6%, corporate deposits (including SMEs) increased by 12.8% and other deposits increased by 129.5%.
- the biggest part in the territorial structure of the deposit base had the following regions (total of retail and corporate): Mazowiecki (24.3%), Śląsko-Opolski (12.4%) and Wielkopolski (10.1%); their total part of all Bank's deposits amounted to 46.8% and in comparison to the year 2004 decreased by 2.2pp.,
- the number of savings-giro (ROR) accounts and Inteligo accounts increased by the total of 391 thousand and amounted to 5,903 thousand,
- the number of cards issued by PKO BP SA increased by 633 thousand and at the year end it amounted to 6,076 thousands, of which 200 thousand accounted for an increase in the number credit cards.

Retail banking

The Bank's activities in the area of retail banking focused on maintaining the volume of deposits and increasing the volume of loans by increasing the attractiveness of products offered by the Bank and improving service quality and sales effectiveness through the completion of the following tasks:

- with respect to new, non-standard deposit products,
- with respect to consumer loans (introduction of a new loan product - "Quick Credit Service" (*Szybki Serwis Kredytowy*)),
- with respect to investment banking, placing two new investment funds in the Bank's offer: PKO/Credit Suisse Akcji Nowa Europa [New Europe] and PKO/Credit Suisse Światowy Fundusz Walutowy [World Monetary Fund],
- with respect to development and intensification of distribution channels - launching 90 Mobile Points of Sales focusing on the sales of the Quick Credit Service and conducting an information campaign addressed to the holders of savings-giro (ROR) accounts concerning the PKO Inteligo e-banking services.

The Bank's activities in the area of Private Banking focused on increasing the number of customers covered by the Personal and Private Banking program, increasing the volume of loans while

¹ The financial data of the PKO BP SA Group companies has been presented according to these companies' IAS/IFRS financial statements.



maintaining high quality, increasing the number of issued high prestige cards and increasing the attractiveness of the Bank's offer by further tailoring it to the needs of its clients.

To the most important Bank activities for SMEs in 2005:

- improvement of Bank's offer competitiveness for SMEs and enlargement of availability of credits by implementing the new credit product "Quick Credit Service", modification of credit Hipoteka PARTNER, supporting entrepreneurs within the confines of European funds
- cooperation with European Bank for Reconstructing and Development – described in detail in point 12 of this Directors' Report

Corporate banking

In 2005, the Bank's activities in the area of corporate banking focused in particular on improving the efficiency of corporate customers service in order to strengthen business relations, improve market position and create the business image of the Bank as an active financial institution which is dynamically developing on the corporate market.

In order to improve competitiveness of PKO BP SA products designed for corporate customers, the Bank modified the existing products and introduced new products, such as: trust account, conditional settlements account, multi-purpose credit limit, the e-money instrument for entities making payments to retail customers. Moreover, cash pooling service has been implemented and the functionality of Virtual Supplier Accounts System and home-banking MultiCash system have been expanded.

Moreover, the Bank has implemented the service considering the issuance of securities, corporate bonds and bills of exchange PKO BP SA. Additionally, PKO BP SA cooperated with national financial institutions thus contributing to the increase of activity on the debt securities market.

Real estate financing

In the area of real estate financing, PKO BP SA has the following types of loans:

- housing loans,
- investment credits,
- credits supported by the state budget which have been granted until 31 March 1996 on the basis of other regulations

In terms of mortgage products in 2005 the main aim of PKO BP SA activity on the field of real estate financing was maintaining the dominant position on the market. As at 31 December 2005, the debt form mortgage products amounted to PLN 16.8 billion. In comparison to the year 2004 it increased by PLN 3.5 billion i.e. 26%.

The Bank maintains significant market share in sales of loans in PLN – on average it amounted to 40% in 2005.

The credit WŁASNY KĄT played the dominant importance in the portfolio.

To increase the attractiveness of the offer and its better adjustment to the client's needs:

- implementation of insurance in case of lost of job and hospitalization,
- modification of the Housing Custodial Account – three types of accounts have been separated adjusted to the transactions concluded on the real estate market,
- investors credits have been expanded – implemented the loan promesa,
- referential rates have been modified for individuals and investors credits.

Moreover, in order to attract new clients and expand the value of granted credits, the special offers for clients acquiring real estates realized by developers particularly investments semi financed by PKO BP SA have been prepared.

The total exposure of credits with state budget aid amounted to PLN 2,778.4 million at the end of 2005 and in comparison to the end of 2004 decreased by PLN 286.3 million (i.e. 9.3%).



The loans with transitional buyout of interest from state budget aid play dominant importance in the portfolio according to the normative and profitable rate. Their part in the portfolio amounted to 96.6%.

Money market activities

In 2005, the Bank's activity on the money market focused mainly on liquidity, interest rate and currency risk management, investment portfolio management and trade activities carried out on the inter-bank market and with the Bank's clients.

The most important activities focused on:

- Bank's debt securities portfolio management
- an increase of investments in securities denominated in foreign currencies
- assuring long-term financing in CHF
- the activity of Bank on the treasury securities market and interest rate derivatives
- development of transactions with non-banking clients

Financial results:

The relation of the total assets of PKO BP SA to the Group amounted to 98.6% in 2005 and the share of net profit PKO BP SA in the consolidated net result of the Group amounted to 96.7% in 2005. Because of that fact the Bank as a dominant entity has major impact on the balance sheet and the profit and loss account of the Group PKO BP SA. Thus, the presented consolidated financial results in point 8 reflect also results for PKO BP SA.

The activities of PKO BP SA – the Group's holding company, including its main products, services and areas of activity as well as financial performance for the year 2005 have been presented in the *Directors' Report on the activities of Powszechna Kasa Oszczędności Bank Polski Spółka Akcyjna in 2005*, which is an integral part of the annual report of PKO BP SA.

6.2 Activity of other entities of PKO BP SA Group

Bankowy Fundusz Leasingowy S.A.

The Company offers operating and finance lease services in respect of vehicles, machinery, equipment and real estate as well as other financial agency services. Special services of the Company include: BanCar Leasing, representing lease of passenger cars and trucks and Bankowy Wynajem – a long-term lease of automobiles.

- The value of the Company's equity at the end of 2005 amounted to PLN 22,010 thousand.
- The Company closed the year 2005 with a net profit of PLN 2,835 thousand.
- In 2005, the Company carried out lease agreements for a total amount of PLN 455.5 million. As regards the net value of the leased assets, the Company ranked 13th at the end of 2005 (according to data published by *Rzeczpospolita* on 11 January 2006).
- In 2005, the Company commenced the program of providing leasing services to small and medium-sized enterprises making use of the EU structural funds.
- In 2005, the Company introduced a new product to its offer - Ban Truck Leasing. This product is dedicated to Companies operating in the transport services industry and deals with the lease of heavy hauling equipment.
- The Company signed a loan agreement with the European Bank for Reconstruction and Development for an amount of PLN 60 million, for the financing of lease contracts concluded with small and medium-sized enterprises.

Centrum Elektronicznych Usług Płatniczych eService S.A.

The main activities of eService S.A. include: the acquisition (to the Bank's order) of retail points, the so-called acceptors, which execute transactions with the use of cards, the management of POS terminals' network, processing of data relating to card transactions performed at POS terminals, and



servicing of cash withdrawals at POS terminals installed, among other places, in PKO BP SA agencies and branches.

- The value of the Company's equity as at 31 December 2005 amounted to PLN 5,458 thousand.
- In 2005, the Company significantly improved its financial performance compared to the previous years. At the end of December 2005, the Company reported a net profit of PLN 8,739 thousand.
- The Company's share in the card acceptance market as regards the number of eService terminals reached the level of 30% at the end of 2005 and increased by 4.9% compared to the end of 2004. The number of eService terminals at the end of 2005 amounted to 29,557.
- In 2005, 49,348 thousand transactions for a total amount of PLN 8,056,806 thousand were conducted using the eService terminals. As regards the value of generated card transactions, the Company's share in the market at the end of 2005 was estimated at 25%.

Centrum Finansowe Puławska Sp. z o.o.

The Company manages the building „Centrum Finansowe Puławska”, located at 15 Puławska Street in Warsaw.

- The value of the Company's equity at the end of 2005 amounted to PLN 199,982 thousand.
- At the end of 2005, the Company reported a net profit of PLN 122 thousand.
The Company's financial results in 2005 were significantly affected by foreign exchange losses connected with an increase in the value of US dollar in relation to 2004, and the resulting increase in the costs of the long-term foreign currency loan taken by the Company for the construction of the Centrum Finansowe Puławska building. The currency risk related to the repayment of this loan is hedged by office space rental contracts denominated in USD. However, in accordance with the current accounting policies, the Company is not required to separate derivatives from these currency contracts, as they were concluded in a currency commonly used in such contracts.
- The rented office space and commercial area in the CFP building was subject to small fluctuations and amounted to 99% at the end of 2005.
- The Polish Building Employers Association (*Polski Związek Pracodawców Budownictwa*) prolonged the Developer's Certificate held by the Company until June 2007.

Inteligo Financial Services S.A.

The main area of the business activities of Inteligo Financial Services S.A. is the provision of e-banking services. The Company provides a platform for the development of electronic services of PKO BP SA in the field of keeping accounts and selling other banking products using interactive distribution channels.

- The value of the Company's equity at the end of 2005 amounted to PLN 43,153 thousand.
- The Company closed the year 2005 with a net profit of PLN 26,545 thousand. This profit is mainly the result of increase in income due to the extension of services provided by the Company to the Bank.
- The value of deposits held by PKO BP SA customers using the Inteligo accounts increased in 2005 by PLN 284 million in relation to the end of 2004, and amounted to PLN 1,523 million at the end of 2005.
- At the end of 2005, the Inteligo account with a 9% market share ranks 4th on the e-banking market in terms of the number of clients (estimates made by the Company on the basis of data provided by *Rzeczpospolita* for Quarters 1 to 3 of 2005 and information provided by mBank).
- In January 2005, the Company was awarded a certificate of compliance with the ISO 9001:2000 standard for designing software development, introducing changes to production environment, installation of changes and system maintenance.

Powszechne Towarzystwo Emerytalne BANKOWY S.A.

The main area of the activities of Powszechne Towarzystwo Emerytalne BANKOWY S.A. („PTE”) is the management of an open-end pension fund. Since 2003, the Bank holds 100% of PTE's shares.



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- The value of equity of the PTE BANKOWY S.A. Group (PTE BANKOWY S.A. and its subsidiary, Finanse Agent Transferowy Sp. z o.o.) amounted to PLN 73,829 thousand as at 31 December 2005.
 - The PTE BANKOWY S.A. Capital Group closed the year 2005 with a net profit of PLN 19,107 thousand.
 - In 2005, PTE reported a dynamic growth in the value of managed assets (collected in Bankowy Otwarty Fundusz Emerytalny – the open-end pension fund – “BOFE”). At the end of 2005, the value of BOFE assets amounted to PLN 2,749 million, and increased by 19% in relation to the end of 2004.
 - At the end of 2005, the number of accounts kept for BOFE members amounted to 455,941.
 - At the end of 2005, BOFE was ranked 8th on the market of pension funds, both as regards the value of assets and the number of accounts.
 - In the ranking of the rates of return published by the Insurance and Pension Funds Supervisory Commission (KNUiFE) in April 2005, BOFE was ranked 1st on the listing of rates of return with the result of 45.759%, while the weighted average was 41.480%. In September 2005, BOFE achieved a rate of return approximating the weighted average rate of return and was ranked 7th on the list.

PKO Inwestycje Sp. z o.o.

The Company's main activity is construction and development. PKO Inwestycje Sp. z o.o. specializes in the management of big development Project.

Development projects are carried out by the Company itself or by its subsidiaries, which are set up together with specialized developers.

- The value of equity of the PKO Inwestycje Sp. z o.o. Group (PKO Inwestycje Sp. z o.o. and its subsidiaries) amounted to PLN 174,410 thousand at the end of 2005.
- The PKO Inwestycje Sp. z o.o. Group closed the year 2005 with a net profit of PLN 20,833 thousand.

In 2005, the Company's activities focused on the following development projects:

- Project “Marina Mokotów”

The project is carried out by the Company's special purpose vehicle, Fort Mokotów Sp. z o.o., in which PKO Inwestycje Sp. z o.o. holds 51% of shares. The project includes construction and sale of private lodgings and business premises located in Warsaw, at 107 Raławicka Street.

The project is progressing according to the plan.

- Project “Nowy Wilanów”

The Project is carried out by a special purpose vehicle, Wilanów Investments Sp. z o.o., which was set up in March 2004 and in which PKO Inwestycje Sp. z o.o. holds 100% of shares. The project includes construction and sale of private lodgings and business premises located in the prestigious Warsaw district, Wilanów.

At the end of 2005, the project was completed in 78% as regards Phase I and 17% as regards Phase II.

- Project “Trzy Gracie”

The project includes construction and sale of a housing and commercial complex in Sopot, and it has been carried out directly by PKO Inwestycje Sp. z o.o. All private lodgings were sold until the end of 2005 in accordance with the plan. Business premises still remain to be sold.

- Project “Centrum Biznesu Fort Mokotów”

In 2005, the Company conducted research work with regard to the construction project “Centrum Biznesu Fort Mokotów”. As a result of the analyses performed by the Company, the Company withdrew from realization of this project. At the same time, the Company started to perform analyses connected with an alternative construction project.

- Project “Neptun Park”

In March 2005, a company was set up under the name of POMERANKA Sp. z o.o., in which PKO Inwestycje Sp. z o.o. holds 100% of shares, for the purpose of carrying out a housing construction



project. In accordance with the plan, in December 2005 the Company commenced work related to Phase I (construction of 5 buildings) in Gdańsk Jelitkowo.

Another company was set up under the name of UKRPOLINWESTYCJE Sp. z o.o., in which PKO Inwestycje Sp. z o.o. holds 55% of shares in the share capital, and whose purpose is to carry out development activities on the territory of Ukraine. Currently the Company conducts research on the Ukrainian development market.

Bankowe Towarzystwo Kapitałowe S.A.

In 2005, the Company carried out work relating to commencement of its activities in the field of venture capital.

- The value of the Company's equity at the end of 2005 amounted to PLN 18,393 thousand.
- The Company closed the year 2005 with a net loss of PLN 1,353 thousand.

KREDOBANK S.A. (the former Kredyt Bank (Ukraine) S.A.)

KREDOBANK S.A. in Lvov conducts banking activities in Ukraine.

- The value of equity of KREDOBANK S.A. as at 31 December 2005 amounted to UAH 134,208 thousand.
- KREDOBANK S.A. closed the year 2005 with a net profit of UAH 10,145.7 thousand.
- At the end of 2005, KREDOBANK S.A. achieved a 0.95% share in the Ukrainian banking services market as regards the value of net assets, and was ranked 22nd among Ukrainian banks.
- In 2005, KREDOBANK S.A. continued to be classified in Group II of the Ukrainian banks – “big banks”, i.e. with the value of assets exceeding UAH 1,300 million.
- The loan portfolio (gross) of KREDOBANK S.A. increased by UAH 584.1 million i.e. 56.7% in relation to the balance at the end of 2004 and amounted to UAH 1,613.6 at the end of December 2005.
- “A vista” deposits increased by UAH 213.5 million i.e. 88.0% in relation to the balance at the end of 2004, and amounted to UAH 456.1 million at the end of December 2005.
- Clients' term deposits increased by UAH 326.9 million i.e. 45.2% since the beginning of the year and amounted to UAH 1,050.1 million at the end of December 2005.
- In 2005, KREDOBANK S.A. concluded a loan agreement with PKO BP SA, under which KREDOBANK S.A. was granted a revolving working capital loan in the amount of USD million.
- In 2005, PKO BP SA extended two loans to KREDOBANK S.A. for an amount of USD 7 million and USD 7.5 million, each of them for the period of 8 years, which, following the consent of the National Bank of Ukraine, were included in own capital of KREDOBANK S.A.
- In cooperation with PKO BP SA, KREDOBANK S.A. developed a Strategy for expansive development of KREDOBANK S.A. in the years 2005 – 2008, which provides for a dynamic development of the Bank in the area of retail banking.

7. OTHER SIGNIFICANT SUBORDINATED ENTITIES

PKO/Credit Suisse Towarzystwo Funduszy Inwestycyjnych SA

The business activities of PKO/Credit Suisse Towarzystwo Funduszy Inwestycyjnych include setting up and management of investment funds.

- As at 31 December 2005, the value of the Company's equity amounted to PLN 55,209 thousand²,
- The Company closed the year 2005 with a net profit of PLN 30,692 thousand,
- The value of assets of the funds managed by the Company amounted to PLN 5,205 thousand at the end of 2005, which gave the Company an 8.5% share in the investment fund market and

² The financial data of PKO/Credit Suisse TFI SA is presented in accordance with the Company's PAR financial statements.



ranked it 4th among such companies (3rd at the end of 2004). The value of assets increased by 56% compared to the end of 2004.

- In 2005, the Company included the following products in its offer: Fundusz Rynku Pieniężnego (Money Market Fund), S-Collect (non-standardized securitization fund), Fundusz Akcji Nowa Europa (New Europe securities fund), Fundusz Obligacji Ekstra (bonds fund "Extra"), Światowy Fundusz Walutowy (International Monetary Fund), including: Papierów Dłużnych EUR (EUR debt securities), Papierów Dłużnych USD (USD debt securities), Papierów Dłużnych CHF (CHF debt securities), Papierów Dłużnych GBP (GBP debt securities) and Małych Japońskich Spółek (small Japanese companies). In addition, the Company introduced to its offer an Investment Deposit (Lokata Inwestycyjna), a product offered together with the Bank which combines the features of a deposit placement and an investment in a Balanced Fund (Fundusz Zrównoważony).
- In May 2005, the Company paid out to the shareholders a dividend from the profit for the year 2004 amounting in total to PLN 25.4 million (gross).

8. FINANCIAL PERFORMANCE OF THE PKO BP SA GROUP

Neither the Bank nor any other companies from the PKO BP SA Group published any forecasts relating to the financial results for the year 2005.

8.1 Balance sheet structure

The balance sheet of the holding company has the most significant influence on the balance sheet of Capital Group. It determines both the value and the structure of the Group's assets and liabilities. As at 31 December 2005, total assets of PKO BP SA accounted for 98.6% of total assets of the Group.

As at 31 December 2005, total assets of the Group amounted to PLN 91,613 thousand and increased by PLN 5,659, i.e. 6.6%, compared to the end of 2004.

8.1.1 Assets

Table 3. Major asset categories of the PKO BP SA Group (in PLN thousands)

Assets	As at		Change	
	31.12.2005	31.12.2004	PLN thousands	%
<i>1</i>	<i>2</i>	<i>3</i>	<i>4</i>	<i>5</i>
1. Cash and balances with the Central Bank	3 895 331	3 525 329	370 002	10.5%
2. Amounts due from banks	12 663 295	13 231 947	(568 652)	(4.,3)%
3. Financial assets	851 003	369 517	481 486	130.,3%
4. Derivative financial instruments	1 137 227	1 362 379	(225 152)	(16.,5)%
5. Other financial instruments valued at fair value through profit or loss	20 059 683	0	20 059 683	x
6. Loans and advances to customers	46 874 629	40 037 204	6 837 425	17.,1%
7. Investment securities	1 881 378	23 457 928	(21 576 550)	(92.,0)%
8. Property, plant and equipment	2 643 551	2 651 824	(8 273)	(0.,3)%
9. Other assets	1 607 084	1 318 237	288 847	21.,9%
Total assets	91 613 181	85 954 365	5 658 816	6.,6%

In comparison to the end of 2004, the most significant change in the assets' structure is the transfer of assets from "Investment securities" to "Other financial instruments valued at fair value through profit or loss" in connection with separation of the ALPL³ portfolio from the previous "available for sale" portfolio. This allowed the Bank to reflect the results from valuation of hedged items and hedging instruments within the same category of the profit and loss account, which increased the transparency of presented results from valuation of debt securities.

³ Assets and liabilities at fair value through profit and loss



As at 31 December 2005, the most significant item in the PKO BP SA Group's assets (51.2%) consists of loans and advances to customers.

Table 4. Loans and advances granted to the customers of the PKO BP SA Group (in PLN thousands)

Assets	As at		Change	
	31.12.2005	31.12.2004	PLN thousands	%
<i>1</i>	<i>2</i>	<i>3</i>	<i>4</i>	<i>5</i>
I. Loans granted to customers	46 283 983	39 555 713	6 728 270	17.0%
1. Gross loans and advances granted to customers, of which:	49 226 992	42 198 940	7 028 052	16.7%
- public sector	6 749 221	7 613 858	(864 637)	(11.4)%
- financial sector (except for banks)	332 727	279 916	52 811	18.9%
- non-financial sector	42 145 044	34 305 166	7 839 878	22.9%
2. Allowances for loans showing indicators of impairment	(2 943 009)	(2 643 227)	(299 782)	11.3%
II. Net receivables due to financial leasing	590 646	481 491	109 155	22.7%
Loans and advances to customers	46 874 629	40 037 204	6 837 425	17.1%

Receivables from customers with maturities over 1 year had a predominant role in the aging structure of gross loans and advances as at 31 December 2005 and 2004. Their total share in the Bank's loan portfolio increased from 62.0% at the end of 2004 to 64.2% at the end of 2005. In the aging structure of receivables, the greatest increase (by 2.9 pp.) was observed in the category of receivables due in more than 5 years, which was mainly due to the high dynamics of long-term housing loans.

Further information concerning the maturity terms of credits and loans given to clients of the Group is stated in the note 28 of Additional Information of Financial Statement.

8.1.2 Equity and Liabilities

Liabilities

Table 5. Major items of liabilities and equity of the PKO BP SA Group (in PLN thousands)

Item	As at		Change	
	31.12.2005	31.12.2004	PLN thousands	%
<i>1</i>	<i>2</i>	<i>3</i>	<i>4</i>	<i>5</i>
1. Liabilities, of which:	82 838 191	77 096 413	5 741 778	7.4%
- Amounts due to the Central Bank	766	144	622	431.9%
- Amounts due to other banks	2 083 346	998 718	1 084 628	108.6%
- Derivative financial instruments	1 257 384	793 739	463 645	58.4%
- Amounts due to customers	76 747 563	73 091 874	3 655 689	5.0%
- Other liabilities	2 749 132	2 211 938	537 194	24.3%
2. Total equity	8 774 990	8 857 952	(82 962)	(0.9)%
Total liabilities and equity	91 613 181	85 954 365	5 658 816	6.6%

The most significant item of the Group's liabilities and equity (83.8%) consists of amounts due to customers, which amounted to PLN 76,748 million as at 31 December 2005 and increased by 5.0% compared to the balance at the end of 2004. It was the main source of financing of the Group.

As at 31 December 2005, the main item in the Group's liabilities to customers (accounting for 82.8% of the total balance) consisted of amounts due to private customers, which amounted to PLN 63,540 million. The most significant item in this category consisted of term deposits, which amounted to PLN 42,814 million at the end of 2005 and decreased by 0.6% compared to the end of 2004.



The following changes took place in amounts due to customers compared to the end of 2004:

- amounts due to corporate entities increased by PLN 3,409 million, i.e. 51.5%, and this mainly related to term deposits, which increased almost twice,
- amounts due to private customers increased by PLN 2,430 million, i.e. 4.0% (of which current deposits increased by PLN 2,723 million, i.e. 15.1%),
- amounts due to public sector entities decreased by PLN 2,183 million (i.e. 40.7%) – the main reason for such a decrease was the withdrawal of funds by the Ministry of State Treasury in accordance with the Act on Bank Gospodarstwa Krajowego of 14 March 2003 and the Decree of the Minister of Finance dated 28 December 2004 on the rules for investing public funds.

In the amounts due to the customers of the Group by maturity, compared to the end of 2004, an increase was observed in amounts due to customers within up to 3 months (including current accounts and overnight deposits), which increased by 12.3% compared to the end of 2004, while the balance of deposits with maturities over 3 months decreased by 15.4%. This had an impact on the aging structure of amounts due to customers, in which the percentage of amounts due to customers within up to 3 months increased from 72.5% to 77.5%, with a corresponding decrease in the percentage of liabilities with longer maturity periods. The share of amounts due within one year amounted to 2% of the total amounts due to the customers.

8.2 Off-balance sheet items

Table 6. Off-balance sheet items (in PLN thousands)

Item	As at		Change	
	31.12.2005	31.12.2004	PLN thousands	%
<i>1</i>	<i>2</i>	<i>3</i>	<i>4</i>	<i>5</i>
I. Contingent liabilities	10 268 549	6 398 063	3 870 486	60.5%
1. Financial	8 792 299	5 659 586	3 132 713	55.4%
2. Guarantees	1 476 250	738 477	737 773	99.9%
II. Liabilities arising from purchase/sale transactions	279 032 415	170 084 929	108 947 486	64.1%
III. Other	14 571 039	14 120 739	450 300	3.2%
1. Irrevocable liabilities	8 519 942	9 504 826	(984 884)	(10.4)%
2. Collaterals received	6 051 097	4 615 913	1 435 184	31.1%
Total off-balance sheet items	303 872 003	190 603 731	113 268 272	59.4%

In comparison to the end of 2004, the total off-balance sheet items PKO BP SA increased by 59.4% mainly due to increase in liabilities related to purchase/sale transactions, which increased by 64.1%. This item mainly consisted of derivative transactions and forward exchange transactions which were concluded by PKO BP SA in order to manage the Bank's foreign currency liquidity as well as for speculation and arbitrage purposes.

Additionally, the description of the total off-balance sheet transactions is stated in the Note 45 of the Additional Notes to consolidated financial statements.



8.3 Profit and loss account

Table 7. Main items of the profit and loss account of the PKO BP SA Group (in PLN thousands)

Item	2005	2004	Dynamics
1	2	3	4
1. Net interest income	3 544 475	3 512 733	100.9%
2. Net fees and commission income	1 217 882	1 583 012	76.9%
3. Dividend income	16 112	3 396	474.4%
4. Result from financial instruments at fair value	31 706	(45 675)	x
5. Result from investment securities	276 856	(20 651)	x
6. Foreign exchange result	612 101	473 436	129.3%
7. Net other operating income	766 523	452 236	169.5%
8. Total income items (1-7)	6 465 655	5 958 487	108.5%
9. Impairment losses	(161 090)	(169 030)	95.3%
10. General administrative expenses	(4 161 051)	(3 941 767)	105.6%
11. Share in the profits (losses) of associates	23 531	21 925	107.3%
12. Profit before taxation	2 167 045	1 869 615	115.9%
13. Income tax expense	(411 424)	(361 523)	113.8%
14. Profits (losses) of minority shareholders	20 801	1 587	1310.7%
15. Net profit	1 734 820	1 506 505	115.2%

8.3.1 Income items

In the Group's profit and loss account for the year 2005, the total of income items amounted to PLN 6,466 million and was PLN 507 million (i.e. 8.5%) higher than in 2004. The main items comprising this amount were net interest income and net fees and commission income.

Net interest income

Table 8. Interest income and expense of the PKO BP SA Group

Item	2005	2004	Dynamics
1	2	3	4
1. Interest income, of which:	5 662 012	5 310 475	106.6%
- from loans and advances granted to customers	3 573 404	3 067 934	116.5%
- from securities at fair value through profit or loss	1 256 445	1 398 947	89.8%
- from placements with other banks	601 248	423 171	142.1%
- from investment securities	139 506	326 073	42.8%
- other	91 409	94 350	96.9%
2. Total interest expense, of which:	(2 117 537)	(1 797 742)	117.8%
- relating to amounts due to customers	(1 924 327)	(1 616 676)	119.0%
- relating to deposits from other banks	(71 969)	(53 905)	133.5%
- other	(121 241)	(127 161)	95.3%
Net interest income	3 544 475	3 512 733	100.9%

The net interest income consists of interest income of PLN 5,662 million and interest expense of PLN 2,118 million, which increased, respectively, by 6.6% and 17.8% in comparison to 2004. Higher dynamics of expenses was connected to an increase in the volume of deposits and better competitive position of the Group with respect to deposit interest rates.

The most significant item in the Group's interest income in 2005 was income from loans and advances granted to customers, which accounted for 63.1% of total interest income (5.3 pp. increase in relation to 2004), and then income from securities at fair value through profit or loss, which accounted for



22.2% of total interest income (4.1 pp. decrease in relation to 2004). These securities mainly included bonds and Treasury and money bills.

In the structure of interest expense in 2005, the most significant item was the expense related to amounts due to customers, which accounted for 90.9% of total interest expense and increased by 1.0 pp. in relation to 2004.

In 2005, the average interest rate of PKO BP SA loans was 7.7%⁴, while the average interest rate of deposits was 2.6%⁵. Compared to 2004, these rates sustained at the same level in the case of loans, and increased by 0.3 pp. in the case of deposits.

Net fees and commission income

Table 9. Fees and commission income and expense of the PKO BP SA Group (in PLN thousands)

Item	2005	2004	Dynamics
1	2	3	4
1. Fees and commission income, of which:	1 537 579	1 861 390	82.6%
- from loans and advances granted by the Group	72 983	478 374	15.3%
- other	1 464 596	1 383 016	105.9%
2. Fees and commission expense	(319 697)	(278 378)	114.8%
Net fees and commission income	1 217 882	1 583 012	76.9%

In 2005 net fees and commission income decreased by 23.1% in relation to 2004. This amount consists of fees and commission income amounting to PLN 1,538 million (i.e. 17.4% decrease in relation to 2004) and fees and commission expense of PLN 320 million (i.e. 14.8% increase in relation to previous year).

The decrease in fees and commission income mainly relates to income from loans and advances, which decreased by 84.7% due to the fact that, starting from 2005, such income is deferred and accounted at amortized cost using the effective interest rate, which discounts the expected cash flow to net carrying amount over the period to maturity of the loan. Fees and commissions are included in the calculation of the effective interest rate because they are an integral part of the effective return on the loan or advance and adjust their carrying amount.

In terms comparable with 2004, i.e. including all fees and commissions recognised on a cash basis in 2005, the dynamics of fees and commission income would amount to approximately 113%.

As of 1 January 2006, the Bank introduced a new "Table of Banking Fees and Commission Rates". This change resulted from market conditions and new products and services offered by the Bank.

Other income items

The total of other income items (other than net interest income and net fees and commission income) amounted to PLN 1,703 million and increased by 97.4% in comparison to 2004. This was due to the following:

- The result from financial instruments at fair value amounted to PLN 32 million and was PLN 77 million higher than corresponding balance in the previous year;
- The result from investment securities amounted to PLN 277 million (an increase of PLN 298 million compared to 2004) – the increase was a result of an increased activity of the holding company on the Stock Exchange, especially in the third quarter of 2005, due to the boom on the stock exchange market during this period;

⁴ The average interest rate for loans was calculated as the relation of interest income from loans to the average balance of loans in the reporting period.

⁵ The average interest rate for deposits was calculated as the relation of interest expense relating to deposits to the average balance of deposits in the reporting period.



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- Foreign exchange result amounted to PLN 612 million and increased by 29.3% in relation to 2004, mainly due to better result on FX SWAP and CIRS transactions (the result on these transactions is of an interest type); these transactions are used in order to hedge currency liquidity, including that related to housing loans;
 - Net other operating income amounted to PLN 767 million (an increase of 169.5%) and consisted of other operating income of PLN 876 million and other operating expense of PLN 109 million; the increase in this item was due to the growth of income of the consolidated company Fort Mokotów Sp. z o.o., which is part of the PKO Inwestycje Group, due to the development of its activity, and consolidation of Wilanów Investment Sp. z o.o. in 2005 (also from the PKO Inwestycje Group);
 - Dividend income amounted to PLN 16.1 million (more than four times higher compared to 2004).

8.3.2 Impairment losses

The result from impairment losses amounted to PLN (-) 161 million in 2005 and improved by PLN 8 million compared to 2004. This was due to better quality of the loan portfolio as well as the finalisation in the fourth quarter of 2005 of the sale of a portfolio of non-performing retail loans.

8.3.3 General administrative expenses

In 2005, the Group's general administrative expenses amounted to PLN 4,161 million and increased by 5.6% in relation to 2004. In the same period, general administrative expenses of PKO BP SA as a holding company decreased by 0.4%. The increase in general administrative expenses was due to the previously mentioned consolidation of Wilanów Investments Sp. z o.o. and an increase in the costs of Fort Mokotów Sp. z o.o. due to the development of its activities. The increase in the administrative expenses of the above-mentioned Group companies has been compensated by the growth of their income, recorded under "Other operating income".

The individual expense items were as follows:

- Employee costs – personnel costs incurred by the Group in 2005 amounted to PLN 2,053 million and increased by PLN 110 million, i.e. 5.7%, comparing to 2004. The main reason for the increase was a change in the salaries level in PKO BP SA; the increase in the costs of salaries was the result of the Bank's strategy aimed at adjusting the salaries level in the Bank to the average salaries level in the banking sector in Poland and the planned restructuring of employment;
- Non-personnel costs amounted to PLN 1,576 million in 2005 and increased by 11.4% compared to 2004;
- Depreciation of tangible fixed assets and amortization of intangible assets amounted to PLN 467 million in 2005 and decreased by PLN 51 million, i.e. 9.8%, compared to 2004;
- Other administrative expenses in 2005 amounted to PLN 74.9 million, which was slightly less than in 2004. The main items are: taxes and charges, which amounted to PLN 66.9 million in 2005 and increased by 5.2% compared to 2004, and contribution to the Banking Guarantee Fund, calculated as a specific percentage of assets weighted by risk (determined separately for each year), which in 2005 contribution to the Banking Guarantee Fund amounted to PLN 8 million and decreased by PLN 3.7 million, i.e. 31.8%, compared to 2004.



8.3.4 Key financial ratios

The financial results of the PKO BP SA Group for 2005 resulted in the following levels of the key financial ratios:

Ratio	2005	2004
1	2	3
1. Profit (loss) before taxation / average assets (ROA ⁶ _{gross})	2.44%	data not available ⁷
2. Net profit (loss) / average assets (ROA _{net})	1.95%	data not available
3. Profit (loss) before taxation / average equity (ROE ⁸ _{gross})	24.58%	data not available
4. Net profit (loss) / average equity (ROE _{net})	19.68%	data not available
5. General administrative expenses / total income items (C/I)	64.36%	66.15%

8.4 Equity and Capital Adequacy Ratio

Table 10. Equity of the PKO BP SA Group (PLN thousands)

Item	As at:		Change by:
	31.12.2005	31.12.2004	
1	2	3	4
1. Share capital	1 000 000	1 000 000	0.0%
2. Other capital items	5 850 063	6 027 024	(2.9)%
3. Currency translation adjustments	(4 082)	(11 472)	(64.4)%
4. Retained earnings	150 405	270 046	(44.3)%
5. Net profit for the period	1 734 820	1 506 505	15.2%
Equity attributable to the shareholders of the holding company	8 731 206	8 792 103	(0.7)%
Minority interest	43 784	65 849	(33.5)%
Total equity	8 774 990	8 857 952	(0.9)%
Capital adequacy ratio	13.90%	18.44%	4.54 pp.

In comparison to 2004, the Group's equity decreased by 0.9%. A decrease in the Group's equity comparing to 31 December 2004 in spite of the relatively high net profit for the period was the effect of a number of factors, among which the most significant were: the appropriation of PLN 1 billion from the net profit for 2004 to shareholder dividends, adjustments made in respect of IAS 39 and reduction of the revaluation reserve.

The Group's capital adequacy ratio as at 31 December 2005 was 13.90% and decreased by 4.54 percentage points in relation to 2004.

The following reasons contributed to the decrease of the capital adequacy ratio:

⁶ The ROA gross and ROA net ratios are calculated as the relation of, respectively, gross profit (loss) and net profit (loss) to the arithmetical mean of the balances of assets at the beginning and end of the reporting period.

⁷ ROA and ROE for the year 2004 cannot be calculated on a basis comparable to 2005 due to the lack of information on the opening balances of assets and equity according to IFRS, i.e. as at 31 December 2003.

⁸ The ROE gross and ROE net ratios are calculated as the relation of, respectively, gross profit (loss) and net profit (loss) to the arithmetical mean of the balances of shareholders' equity (including accumulated profits from previous years and net profit for the period) at the beginning and end of the reporting period.



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- decrease of the Shareholders' funds used in the calculation of the ratio - mainly as a result of reduction of the revaluation reserve (due to revaluation gains realised on the sale of available for sale financial assets and transferred from the revaluation reserve to the result on financial operations in the profit and loss account) and an increase in the PKO BP SA loan portfolio which decreases the amount of the Group's funds used in calculation of the capital adequacy ratio,
 - increase of the total capital requirement - mainly due to the increase of assets with a risk weighting of 100% as a result of growth of the loan portfolio and the application of the amended rules for calculating capital requirements which came into force on 1 January 2005.

9. RISK MANAGEMENT POLICY

Risk management is one of the most important internal processes of the PKO BP SA and the other entities of the Group – particularly in KREDOBANK SA and in Bankowy Fundusz Leasingowy SA (BFL SA). The aim of this process is to ensure an appropriate level of security and profitability of lending activities in a changing legal and economic environment. Risk management covers both credit risk management and market risk and operating risk management.

9.1 Credit risk

Development of an effective credit risk management system aims at increasing the security and profitability of the services offered by the Group. In credit risk management, the Bank and the Group entities follow the following rules:

- each loan transaction is subject to comprehensive credit risk assessment, which is reflected in an internal rating or credit scoring,
- credit risk relating to potential and concluded loan transactions is measured on a regular basis taking into consideration changing external conditions and changes in the financial standing of the borrowers,
- credit risk assessment is additionally verified by independent units responsible for credit risk assessment,
- credit risk is diversified by geographic regions, industry, products and clients,
- credit decisions may only be taken by authorised persons,
- the Bank and the Group entities hedge against credit risk by creating allowances (specific provisions) for the impairment of loan exposures.

In 2005, KREDOBANK SA amended its internal regulations relating to credit policy, authorisations to take credit decisions, activities of credit committees and recognition of specific provisions.

9.2 Financial risk

The structure of the balance sheet and off-balance sheet liabilities of the PKO BP SA Group do not expose the Group to the risk of loss of liquidity understood as the ability to meet current and future obligations. Because of the Group's structure, the risk is generated mainly by PKO BP SA - the holding company of the Group.

The Bank has a consistent and well-developed liquidity risk management system, a stable deposit base and a portfolio of liquid securities which ensure high financial liquidity of the Bank.

In 2005, market risk management principles and methods were introduced in BFL SA and were modified in KREDOBANK SA.

The description of assets and liabilities at the point of liquidity of the Group PKO BP SA was stated in the Note 3 of the Additional Notes to the consolidated financial statements.

9.3 Operational risk

Operational risk is understood as the risk of a loss arising from non-compliance or weakness of internal processes, people and systems or from external events. The objective of operational risk management is to optimise operational efficiency by reducing operating losses and costs and



increasing the speed and adequacy of Group companies' response to events which are beyond their control.

In the field of operational risk management, PKO BP SA follows the following rules:

- operational risk management principles and procedures cover the full scope of the Bank's activities,
- the Bank defined specific responsibilities and reporting lines in the area of operational risk management at different decision-taking levels,
- the Bank's internal regulations define the process of identification and assessment of operational risks for all major areas of the Bank's activity,
- the Bank regularly monitors operational events exceeding PLN 40,000 and communicates them to the Bank's Management Board,
- operational risk management is performed at the level of comprehensive system solutions and day-to-day risk management activities,
- comprehensive operational risk management is delegated to selected head office units and specialized organisational units, which are responsible for setting detailed targets,
- the process of operational risk management is coordinated by the Bank's Credit and Operational Risk Department.

In 2005, KREDOBANK SA issued – in agreement with the Bank – internal regulations for operational risk management, which became effective on 1 January 2006. The operational risk management objectives and instruments in the company are consistent with the objectives and instruments used in the Bank. The organisation of the operational risk management process has been adjusted to the specific nature of this entity.

BFL SA is in the process of organizing its operational risk management system. The company appointed a task force for the purpose of coordinating the process of developing internal regulations for the functioning of the individual organisational units of this entity.

10. MAJOR EQUITY INVESTMENTS

Powszechna Kasa Oszczędności Bank Polski SA

The Bank acquired shares in Centrum Obsługi Biznesu Sp. z o. o. accounting for 41.44% of the Company's share capital and votes at the shareholders' meeting.

The Bank purchased from minority shareholders the shares of KREDOBANK S.A. accounting for 2.367% of the Company's share capital and votes at the Annual General Meeting.

The Bank sold 5 shares of Łódzka Agencja Rozwoju Regionalnego S.A. (ŁARR S.A.) to the Łódzkie Voivodship. The value of the transaction amounted to PLN 50 thousand. The shares subject to the transaction accounted for 2.42% votes at the Annual General Shareholders' Meeting of ŁARR S.A.

The Bank sold 50,312,200 shares in Wschodni Bank Cukrownictwa S.A. (WBC S.A.) to Getin Holding S.A. The value of the transaction amounted to PLN 52,827,810. The shares subject to the transaction accounted for 25.1321% of the share capital and 25.1441% of votes at the Annual General Shareholders' Meeting of WBC S.A. The Bank acquired the shares in WBC S.A. in 2003 as a result of realisation of the restructuring program of WBC S.A.

The Bank made an additional payment to PKO Inwestycje Sp. z o.o. in the total amount of PLN 87,500 thousand for realization of investment projects.

In 2005 PKO BP SA made equity investments on the regulated market by making transactions within the portfolios controlled by the Equity Investment Department and BDM. The total value of the portfolios at acquisition cost as at 31 December 2005 was PLN 15.6 million and decreased by PLN 339.4 million in comparison to 31 December 2004.

PKO Inwestycje Sp. z o.o.

The Company acquired and took up shares in a newly created company, POMERANKA Sp. z o.o., accounting for 100% of shares in the Company's share capital and votes at the shareholders' meeting, for a total amount of PLN 4 million, and made an additional payment to the company at an amount of PLN 15 million.



The company acquired, from Prokom Investments S.A., shares in Wilanów Investments Sp. z o.o. accounting for 49% of the company's share capital, for a total amount of PLN 66,661 thousand, and made an additional payment to the Company for a total amount of PLN 2,350 thousand. As a result of this transaction, PKO Inwestycje Sp. z o.o. holds 100% of shares in the company's share capital, which give right to 100% of votes at its shareholders' meeting.

The company took up shares in a newly created company, UKRPOLINWESTYCJE Sp. z o.o., accounting for 55% of shares in the company's share capital and votes at its shareholders' meeting, for a total amount of PLN 182 thousand.

Bankowe Towarzystwo Kapitałowe S.A.

As part of its venture capital activities, the company acquired, from a natural person, shares in FINDER Sp. z o.o., accounting for 42.31% of shares in the company's share capital and votes at its shareholders' meeting, for a total amount of PLN 5,555 thousand.

11. RELATED PARTY TRANSACTIONS

In 2005, PKO BP SA provided the following services to related (affiliated) entities:

- keeping bank accounts,
- accepting deposits,
- granting loans and advances,
- issuing debt securities,
- granting bank guarantees and conducting foreign exchange operations.

In addition:

- Under the cooperation agreement with Inteligo Financial Services S.A., in 2005 the Bank made payments to the company for a total amount of PLN 106.9 million; these payments were mainly related to remuneration for services arising from the company's day-to-day operating activities and the re-invoicing of the costs of Centrum Bankowości Elektronicznej Inteligo and the Call Center in Lublin;
- Under the lease agreement with Centrum Finansowe Puławska Sp. z o.o., in 2005 the Bank made payments to the company for a total amount of PLN 59.7 million; these payments were mainly related to rent and operating fees.

The significant transactions between PKO BP SA and its subsidiaries, including credits exposure of these entities as at 31 December 2005, were presented in Additional Information for the Financial Statement for 2005.

Granted off-balance sheet liabilities

Off-balance sheet liabilities of a financial and guarantee nature granted to related entities as at the end of 2005 amounted to PLN 453.3 million, and decreased by PLN 259.0 million in comparison to the end of 2004.

Out of the total amount of these liabilities, PLN 328.3 million relates to liabilities granted to Bankowy Fundusz Leasingowy S.A., mainly in respect of open credit lines and issued guarantees, while PLN 81 million represents financial liabilities and open credit lines granted to Centrum Obsługi Biznesu Sp. z o.o.

All transactions with related entities were made on an arm's length basis. Maturity dates range from 1 month to 10 years.

12. INTERNATIONAL COOPERATION

European Bank for Reconstruction and Development

PKO BP SA participates in the "Loan Window" programme being a part of the "UE/EBRD SME Finance Facility" (on the basis of the Loan Agreement of 21 February 2003 concluded by PKO BP SA and the



European Bank for Reconstruction and Development for the financing of small and medium-sized enterprises).

As at 31 December 2005, the Bank has signed 1,775 loan agreements for a total amount of EUR 32.7 million. Apart from granting loans from the funds provided by EBRD, PKO BP SA also participated in improving the lending process and identifying the needs of small and medium-sized enterprises in their relations with banks.

As regards the other companies from the PKO BP SA Group:

- In September 2005, Bankowy Fundusz Leasingowy S.A. signed a loan agreement with EBRD for a total amount of PLN 60 million. The funds received under the „*The EU/EBRD SME Finance Facility*” programme, which are provided, among others, by the European Commission, are allocated for the development of small and medium-sized enterprises.
- In December 2005, KREDOBANK S.A. signed a loan agreement with EBRD for a total amount of USD 10 million. These funds are to be used for issuing medium- and long-term loans to private individuals secured by a mortgage.

Co-operation with other foreign institutions

PKO BP SA signed five ISDA agreements with foreign banks and one annex to a previously signed framework agreement as well as one note agreement with a foreign bank.

Three *nostro* accounts have been closed. At 31 December 2005, the Bank has 28 *nostro* accounts at correspondent banks, denominated in 12 currencies, and keeps 31 *loro* accounts denominated in three currencies for foreign banks.

The Bank signed two additional agreements to the Global Loan Agreement with the European Investment Bank:

- Amendment No. 1 dated 31 October 2005 – which postpones all deadlines in the agreement by one year,
- Amendment No. 2 dated 28 November 2005 – which supplements the agreement with the rules for using the Municipal Finance Facility and the Municipal Infrastructure Facility (credit lines available under the Global Loan and sponsored by the European Commission).

The Bank cannot use the Global Loan facility due to the fact that EIB did not agree the procedures for establishing pledges on Treasury securities in the National Depository for Securities (*Krajowy Depozyt Papierów Wartościowych - KDPIW*).

KREDOBANK S.A. processes settlements in 17 currencies. It holds 43 *nostro* accounts and keeps 75 *loro* accounts. Thanks to co-operation with its shareholders, i.e. PKO BP SA and EBRD as well as the main correspondent banks, it provides its clients with a wide range of services in the area of international transactions.

Since September 2005, KREDOBANK S.A. has received several loans from CARGILL FINANCIAL SERVICES INTERNATIONAL INC. (USA), an international financial organisation, for a total amount of USD 11,754 thousand.

In September 2005, an agreement was signed in Prague between KREDOBANK S.A. and HVB Bank Czech Republic a.s. for an inter-bank loan to be used for financing delivery of machinery and equipment from Czech Republic to Ukraine.

Cooperation with rating agencies

Rating scores are currently assigned to PKO BP SA by four rating agencies: Moody's, Standard & Poor's, Capital Intelligence and Fitch Ratings. These ratings are granted free of charge on the basis of generally available information, in particular interim and annual reports, and on the basis of information provided by the Bank directly to the above agencies.

In 2005, the following rating agencies changed the ratings of PKO BP SA:

- Moody's – increased its financial strength rating twice: on 13 January from D+ to C- and on 28 November from C- to C,



- Capital Intelligence – on 1 February, the Bank received a report from this agency on PKO BP SA, dated December 2004, in which the support rating was decreased from 1 to 2.

Increases in the Bank's ratings are constrained by Poland's country ceiling, i.e. the level of ratings assigned by the agencies to the Polish economy.

Table 11. PKO BP SA ratings as at 31 December 2005

FITCH RATINGS	
Support rating	2
STANDARD AND POOR'S	
Long-term domestic currency liabilities rating	BBBpi
MOODY'S INVESTORS SERVICE LTD.	
Long-term deposit rating	A2 stable outlook
Short-term deposit rating	Prime-1 stable outlook
Financial strength	C stable outlook
CAPITAL INTELLIGENCE	
Long-term foreign currency liabilities rating	BBB+
Short-term foreign currency liabilities rating	A2
Domestic strength	BB+
Support rating	2
Outlook	stable

13. INVESTOR RELATIONSHIPS

13.1 Shareholders' holdings, directly or indirectly through subsidiaries, at least 5% of total votes at the Annual General Meeting

According to the Bank's knowledge, the State Treasury is a shareholder which holds, directly or indirectly through subsidiaries, at least 5% of total votes at the Bank's Annual General Meeting.

According to the Bank's knowledge, the State Treasury had the following number of PKO BP SA shares as at 31 December 2005:

Table 12. Shares held by the State Treasury as at 31 December 2005

Shareholder	Number of shares held	Percentage of Bank's share capital	Number of votes at AGM resulting from shares held	Percentage of votes held at AGM
State Treasury	515 711 446	51.57%	515 711 446	51.57%

13.2 Changes in Articles of Association

During the year, the Bank's Articles of Association were changed by two resolutions of the Ordinary Annual Meeting of PKO BP SA adopted on 19 May 2005:

- Resolution No. 29/2005 regarding amendments to the Articles of Association of PKO BP SA – the contents of § 6 of the Articles were changed; the previous registered "B" and "C" series shares were converted to bearer shares, and sections 3 and 4 were deleted from § 6 of the Articles,
- Resolution No. 30/2005 regarding amendments to the Articles of Association of PKO BP SA – the contents of § 11 section 1 were changed; in accordance with the new wording of § 11 section 1 of the Articles, Supervisory Board is appointed for a common term; other contents of § 11 section 1 did not change.



The consolidated text of the Bank's Articles of Association is included on the website of PKO BP SA.

13.3 Securities' issues

The Bank did not issue any securities in the period covered by this report.

13.4 Re-acquisition of own shares

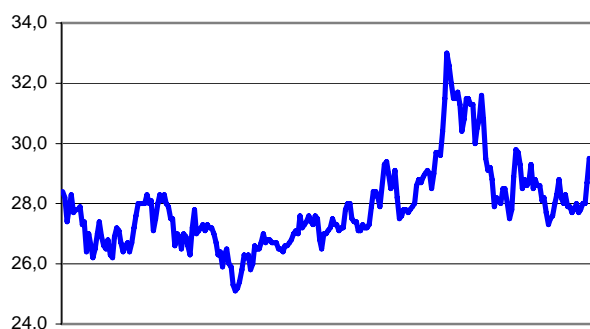
During the period covered by this report, the Bank did not re-acquire its shares on its own account.

13.5 Listed price of the Bank's shares

The price of the Bank's shares as at 31 December 2005 amounted to PLN 29.00 and increased by PLN 1.20 i.e. 4.3% compared to the price as at 31 December 2004.

During the year 2005, the price of the PKO BP SA shares fluctuated from PLN 25.10 as at 28 April 2005 to PLN 33.00 as at 19 September 2005. The following factors had impact on the level of the prices of the Bank's shares: trends prevailing on the Stock Exchange and the Bank's financial results.

PKO BP shares price (period 03.01.2005-31.12.2005) (PLN)



13.6 Compliance with corporate governance rules

PKO BP SA complies with all corporate governance rules enacted by resolution no. 44/1062/2004 of the Stock Exchange Board dated 15 December 2004 on adopting corporate governance rules for joint stock companies being the issuers of shares, convertible bonds or bonds with priority right admitted to trading on the official market, except for the following rules: Rule 5 (relating to the requirement to document the participation of a shareholder's representative at AGM), Rule 24 (relating to the details of personal, factual or organisational relations between members of the Supervisory Board and the given shareholder), Rule 28 (relating to the activities of the Supervisory Board, including appointment of Audit and Remuneration Committees), Rule 38 (relating to the salaries of Management Board members), Rule 43 (relating to selection of the auditors), with which the Bank complies only partially, and Rule 20 (relating to independent members of Supervisory Board), which the Bank does not comply with at all.

13.7 Employee shares

Acting at the request of the State Treasury Minister under the Act of 30 August 1996 on commercialisation and privatisation (Journal of Laws 2002 No. 171, item 1397 with subsequent amendments) and § 14 section 1 of the decree of the State Treasury Minister dated 29 January 2003 on detailed principles for dividing entitled employees into groups, determining the number of shares falling to each of those groups and the procedure for acquiring shares by entitled employees (Journal of Laws No. 35, item 303), the Bank, on 4 April 2005, notified the public of commencing the process of free-of-charge transfer of 105,000,000 "B" series PKO BP SA shares to entitled employees. As at 31 December 2005, the number of shares assigned to employees amounted to 103,763,142.

The process of a free-of-charge transfer of shares to entitled persons, including the signing of agreements for a free-of-charge transfer of shares and the issuing of deposit certificates confirming



the transfer of ownership to the entitled person, was carried out starting from 6 April 2005 at locations and dates which were determined separately for the employees entitled to acquire PKO BP SA shares free of charge and the successors of the entitled employees.

In accordance with Art. 38.3 of the Act on Commercialisation and Privatisation, in correspondence with Art. 48 of the Banking Law, employee shares which were acquired free of charge by entitled employees may not be disposed of within 2 years of the date on which the first shares were sold by the State Treasury, and the employee shares acquired by members of Management Board – within 3 years of the date on which the first shares were sold by the State Treasury.

13.8 Holders of any type of securities giving special control rights with respect to the issuer

PKO BP SA does not issue any securities which give special control rights with regard to the Bank. However, the State Treasury holds a package of 515,711,446 shares which give right to 51.57% of votes at the Annual General Meeting.

13.9 Restrictions for the transfer of ownership of securities and exercising voting rights

In accordance with the provisions of the Bank's Articles of Association, the transfer of "A" series shares requires consent of the Council of Ministers in the form of resolution. The transfer of "A" series shares after acquiring such consent results in the expiry of the above restrictions.

14. SERVICE PROMOTION AND IMAGE BUILDING

- Promotional activities of the Bank in 2005 concentrated mainly upon the following:
 - building up the image of the Bank as a modern leader in the area of banking, providing a multi-channel access to products and services,
 - strengthening positive and consistent image of the Bank as a patron of Polish national culture and sponsor of Polish Olympic organisations,
 - maintaining the leading position of the Bank on the retail market,
 - strengthening the Bank's position in the corporate market by creating an image of the Bank as professional advisor in the market of financial services.

Promotional activities on the retail market were carrying out mainly as promotional campaigns for the Bank's products and services, including: a new cash loan facility called QUICK CREDIT SERVICE, the AUTO PARTNER loan, mortgage loan WŁASNY KĄT ("Own flat"), subscribed deposits, credit cards, including in particular the MasterCard UEFA Champions League, QUICK CREDIT LIMIT FOR BUSINESSES – a new offer for small and medium-sized enterprises. In Autumn 2005, the Bank carried out an image and product campaign "E-banking leader", which finalised the 2005 campaign supporting the sales of the PKO-Inteligo e-banking services. The aim of this campaign was to strengthen the positive features of the Bank's image as a reliable and safe financial institution and, at the same time, emphasize the changes connected with innovation and improvement of the efficiency of PKO BP SA operations. The projects used during this campaign were of innovative nature and definitely differed from those carried out so far.

Promotional activities aimed at supporting private and personal banking – essential for enhancing the prestige of the PKO BP SA brand – were carried out in the form of an annual program involving PR and advertising activities.

The Bank carried out intense promotional activities in the area of corporate banking by making an effective use of selected business events (seminars, conferences, meetings, business competitions), especially of a local nature, as well as promoting individual financial services addressed to various client segments. In doing this, the Bank referred to successful sale of its products, such as syndicated loans, municipal bonds or the European Program.

As part of implementation of the Bank's marketing strategy for T-bonds, the Bank carried out a multimedia campaign for T-bonds based on a new graphic layout of advertisements.



- Promotional activities of other members of the PKO BP SA Group in 2005 focused mainly upon the following:
 - ensuring advertising support for the sale of products, especially new products and services, and creating positive image of the company (KREDOBANK S.A.),
 - promoting housing estates in the course of construction: “Neptun Park” in Gdańsk, “Trzy Gracje” in Sopot and “Marina Mokotów” and “Nowy Wilanów” in Warsaw (PKO Inwestycje Sp. z o.o. and its subsidiaries),
 - sponsorship of socially significant cultural events (including events held in Centrum Finansowe Puławska), sports events, educational events and other healthcare and charity projects, especially for children in need (Centrum Finansowe Puławska Sp. z o.o.),
 - activities supporting the image of Bankowy Fundusz Leasingowy S.A., including sponsorship of the ranking of the most dynamically developing companies “Gazete Biznesu 2005” and carrying out advertising campaigns in selected newspapers,
 - promotional campaigns and competitions addressed to customers of Inteligo Financial Services S.A., e.g. “Płacę z Inteligo” (“I pay by Inteligo”),
 - promotion of the financial results of Bankowy OFE and services provided to members of the fund, among others through the development of the www service and advertising campaign on professional web portals.

The Bank's sponsorship and charity activities were aimed at supporting culture, life-saving and health care. The Bank has supported almost 2,000 undertakings. In 2005, the Bank continued the long-term program “PKO Bank Polski Kulturze Narodowej” (PKO BP for National Culture), under which the Bank acted as the patron of: renovation of a replica of Michelangelo's fresco “The Last Judgment” and the ceremony of making this work available to the public, which was held at the National Museum in Cracow, ceremonial concert “V Wielki Recital” (Fifth Great Recital) held to commemorate the 85th anniversary of foundation of the Adam Mickiewicz University in Poznań, exhibition of manuscripts accompanying the Ninth Easter Ludwig van Beethoven Festival and anniversary concerts of Wanda Warska and Hanna Banaszak. The Bank continued to cooperate with the National Philharmonic, National Library and the National Museum in Warsaw (exhibition of sculptures by W. Hasior). The Bank was the general sponsor of another edition of the Polish Radio Music Festival, which commemorated the 80th anniversary of the Polish Radio, the Andrzej Drawicz Prize, the “Rawa Blues” Festival at Rawa Mazowiecka and the 48th International Festival of Contemporary Music “Warszawska Jesień” (Warsaw Autumn).

As part of the “PKO Bank Polski Blisko Ciebie” (PKO BP Close to You) program, the Bank sponsored, among others, the Stage-play Song Competition (Przegląd Piosenki Aktorskiej) in Wrocław and an international cross-country skiing event “Bieg Piastów”, and subsidized the continuation and promotion of two social programs: “Cała Polska czyta dzieciom” (Whole Poland Reads to Children) and educational program “Zostańcie z nami” (Stay with Us), organised by the Foundation of the Weekly Polityka (Fundacja Tygodnika Polityka). The Bank sponsored also a few Students' Days (Juwenalia)

As part of the “PKO Bank Polski Reprezentacji Olimpijskiej” (PKO BP for the Olympic Representation) program, in 2005 the Bank continued its cooperation with the Polish Olympic Foundation (Polska Fundacja Olimpijska). The Bank was a sponsor of the Polish women's foil team and the title sponsor of the Word Cup in women's foil “Dwór Artusa PKO BP” and the sponsor of “For Wołodyjowski's Sabre Competition (Turniej o Szablę Wołodyjowskiego).

In the area of health care and health promotion, the Bank provided financing for, among others, Fundacja Rozwoju Kardiochirurgii (Foundation for Cardiosurgery Development) – to support the Polish artificial heart program, Fundacja na rzecz Przeszczepów Wątroby i Wspierania Postępu w Chirurgii Przewodu Pokarmowego (Liver Transplant Foundation), Fundacja Służby Zdrowia Samodzielnego Publicznego Wojewódzkiego Szpitala Zespołowego w Szczecinie (the Szczecin Public Hospital Foundation), Śląska Akademia Medyczna (The Silesian Medical Academy) – for the purchase of special apparatus for laparoscopic surgery, Szpital Uniwersytecki w Krakowie (The University Hospital in Cracow), Szpital Zachodni im. Jana Pawła II w Grodzisku Mazowieckim (a hospital in Grodzisk Mazowiecki), Caritas Polska and PCK Zarząd Główny (Polish Red Cross Central Management Board) – assistance for the victims of natural disasters in Asia. Additionally, the Bank made a donation for the “Różowa Konwalia” (Pink Lily of the Valley) program carried out by Polskie Towarzystwo Ginekologii



Onkologicznej (Polish Oncologic Gynaecology Association), provided financing for the purchase of specialist medical equipment for Fundacja "Spełnionych Marzeń" (Dreams Fulfilled Foundation) and Stowarzyszenie Pomocy Dzieciom z Chorobami Serca i Nerek (Association for Children with Heart and Kidney Diseases).

KREDOBANK S.A., apart from its activities on the financial market, supports cultural and artistic projects, and assists in solving current social problems. The main directions of its activity in this area include providing assistance to children-orphans and supporting arts, culture and sports. To recognise the charity activities of KREDOBANK S.A., in June 2005 the Regional Charity Fund honoured the President of the Bank's Management Board with the King Dynała Order of 3rd degree.

Awards and Distinctions

In 2005, PKO BP SA together with other members of the PKO BP Group, received a number of awards and distinctions. The most important are listed below:

- "Debut of the Year 2004" (Debiut 2004 Roku) on the Warsaw Stock Exchange - an award granted by the Stock Exchange Newspaper PARKIET for the last-year privatisation of PKO BP SA – the biggest one in the history of the Warsaw Stock Exchange (February 2005);
- "Superbrands Polska 2004" - title granted to the Bank in recognition of the leading Polish brand in the financial sector (February 2005);
- "Employer of the Year" (Pracodawca Roku) – title awarded by a students' organisation, AIESEC (April 2005),
- "European Medal" – an award granted to the Bank in the "services" category for the "European Program" and to the Bank's subsidiary „eService" for "Authorisation of transactions carried out using cards" in the 10th edition of the competition organised by BCC and the European Integration Committee (April 2005);
- Europroduct – Promotional title granted Bank's products and services in the 8th Competition Edition organised by Polish Trade Association, in "service" category – for The European Program and in "product" category – for the Consolidation Loan, "Nasz Remont" loan, STUDENT credit card, and for current account SUPERKONTO with INTELIGO package (June 2005).
- "Benefactor of the Year 2004" (Dobroczyńca Roku 2004) – two titles granted to PKO BP SA in annual competition organised by the Academy for the Development of Philanthropy in Poland (Akademia Rozwoju Filantropii w Polsce); in the "culture and arts" category – for supporting culture and arts institutions, including the National Philharmonic in Warsaw, and in the "health care and health promotion" category – together with Inteligo Financial Services – for providing financial assistance for the Polish Artificial Heart Program (April 2005);
- Golden Rock 2004 – prize awarded by MasterCard Europe for issuing the PKO Euro Biznes card – the first in Poland MasterCard credit card for small and medium-sized enterprises (April 2005);
- Rock Awards 2004 – an award granted to the Bank's subsidiary, „eService", for the greatest achievement in developing the network of points of sale accepting MasterCard cards (April 2005);
- European Medal awarded to „eService" for "Authorization of transactions carried out using cards" by the Office of the European Integration Committee and Business Centre Club;
- Golden Jubilee Award – granted to the President of PKO BP SA by MasterCard Europe for a continued support of MasterCard Europe in Poland, and in particular for acting as chairman of Europay Forum Polska (April 2005);
- "Brand Worth of European Trust" (Marka Godna Europejskiego Zaufania) – title granted to the Bank by "Reader's Digest" in the current year edition of the European market research among its readers (April 2005);
- First place in Newsweek's ranking of "the most valuable company" (April 2005);
- "The Philharmonic's Sponsor of the Year" (Sponsor Roku Filharmonii) – title granted to the Bank for its last-year cooperation with the National Philharmonic (June 2005);
- Diamond to the Golden Statue of the Polish Business Leader awarded by the Business Centre Club to companies that were previously awarded the Polish Business Leader statue. PKO BP SA received the Diamond award for the third time (June 2005);



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- A distinction granted to PKO BP SA in Students' Employers' Ranking KOMPAS, in the "financial institution" category (June 2005);
 - First place in FORBES's ranking (September issue) granted to PKO BP SA in the category of "quick loans" for one of the cheapest revolving loan facilities and reasonable credit card interest rates;
 - Arts & Business Awards 2005 of the Commitment to Europe arts & business Foundation; PKO BP SA received an award in the "Sponsor art & business" category; in addition, the Bank received a distinction in the category of "Partnership of the Year" for its long-term cooperation with Willa Decjusza in Cracow, which may serve as an example of a long-term and mutually beneficial cooperation of a commercial firm with a cultural institution (November 2005);
 - "Laureate" title in the "Bank Dostępny" (Accessible Bank) competition organised by the Foundation "Otwarte Drzwi" (Open Door) and the National Bank of Poland, in two categories: Clients Award – granted to PKO BP SA for the Inteligo account, and in the "Duży Bank" (Big Bank) category – granted to the First Branch of PKO BP SA in Lwówek Śląski (December 2005);
 - awards and distinctions granted to KREDOBANK S.A.:
 - Ranked 4th among financial institutions in the 4th national Ukrainian competition for the best periodic report for the year 2004 provided by joint-stock companies and enterprises - issuers of bonds, as part of the program "Your share – your capital", organised by the Securities and Exchange Commission of Ukraine;
 - Diploma of the Supreme Council of Ukraine granted to the President of KREDOBANK S.A. for the bank's contribution in the development of banking system in Ukraine (June 2005);
 - Certificate granted to KREDOBANK S.A. by the economic weekly "Inwestgazeta" as a confirmation of the Bank's entering in the ranking of "TOP 100. The best companies of the financial sector" (July 2005);
 - First place in the "Banking, insurance and financial services" category in the national Ukrainian competition for "The best national product of the year". (November 2005).

15. SIGNIFICANT CONTRACTS AND IMPORTANT AGREEMENTS WITH THE CENTRAL BANK OR SUPERVISORY BODIES

During the year 2005, the Bank signed the following significant contracts:

- On 1 June 2005, the Bank signed a contract with a consulting firm for the provision of consulting services relating to preparation and implementation of a plan for optimisation of selected costs of the Bank.
- On 29 July 2005, PKO BP SA signed a Letter of Intent with Poczta Polska (Polish Mail) regarding an extension of cooperation between these two companies.
- On 28 August 2005, the Bank concluded property and civil liability insurance contracts (in total, four insurance policies). Insurance coverage was provided to the Bank by a co-insurance pool comprising: TU Allianz Polska SA (60% share in risk) and PZU SA (40% share in risk).
- On 7 October 2005, the Bank signed a contract for the sale of a portfolio of retail non-performing loans classified as "loss" (balance sheet and off-balance sheet items). The amount due under this transaction was received by the Bank into its bank account on 20 October 2005.
- During the year 2005, the Bank signed 12 significant loan agreements with one borrower, for a total amount of PLN 3,760 million.
- On 22 December 2005, the Bank signed a syndicated loan agreement with a significant borrower from the fuel industry, which consists of tranche A of EUR 250 million and tranche B of EUR 750 million (the share of the Bank amounted respectively to: EUR 22.7 million and EUR 68.2 million). The total value of services arising from long-term agreements with that borrower meets the criteria referred to in § 2 section 2 of the Decree of the Minister of Finance of 19 October 2005 on current and periodic information provided by the issuers of securities.
- The Bank concluded a syndicated loan agreement with a customer from the gas fuel production and distribution industry, which consists of tranche A of EUR 600 million and tranche B of EUR 300 million, and which can be used in either EUR, USD or PLN. The share of PKO BP SA in these tranches amounts to EUR 100 million and EUR 50 million, respectively.



In 2005, the Bank did not enter into any important agreements with either the Central Bank or the supervisory bodies.

As at the date of this Report, the Bank is not aware of any agreements which might result in changes to the proportion of shares held by its current shareholders besides the contract joining PKO BP SA and the Ministry of Treasury concerning the Bank's shares to be available to authorized personnel according to the law as at 30 August 1996 of commercialisation and privatisation.

In 2005, the other companies from the PKO BP Group did not conclude any significant contracts or enter into any important agreements with either the Central Bank or the supervisory bodies.

16. LOANS TAKEN, AND LOAN, GUARANTEE AND SURETYSHIP AGREEMENTS

During the year 2005, PKO BP SA did not take out any loans or advances or receive any guarantees or suretyships that were not related to its operating activity.

During the year 2005, KREDOBANK S.A. did not take out any loans or advances or receive any guarantees or suretyships that were not related to its operating activity.

17. UNDERWRITING AGREEMENTS AND GUARANTEES GRANTED TO SUBSIDIARIES

In 2005, PKO BP SA did not sign any underwriting agreements with Group companies.

The guarantee granted by PKO BP SA to its subsidiary - Bankowe Towarzystwo Kapitałowe S.A. (formerly Dom Maklerski BROKER S.A.) for an amount of PLN 105 million expired on 31 January 2005. This guarantee was issued as a security for the company's payments to the Stock Exchange Transaction Settlement Guarantee Fund (*Fundusz Gwarantowania Rozliczeń Transakcji Giełdowych*).

On 6 October 2005, PKO BP SA issued a guarantee to its subsidiary – Bankowy Fundusz Leasingowy S.A. for an amount up to PLN 22 million. The guarantee provides a security for the company's repayment of the first tranche of the loan granted by the European Bank for Reconstruction and Development of London.

On 7 November 2005, PKO BP SA issued a guarantee to its subsidiary - Centrum Elektronicznych Usług Płatniczych eService S.A. for an amount up to PLN 100 thousand. The guarantee provides a security for a contract concluded with POLKOMTEL S.A. for the sale of prepaid phone card units.

As at 31 December 2005, the value of guarantee arising from the Agreement for Organisation, Conducting and Servicing of a Bonds Issuance Program, concluded between PKO BP SA and its subsidiary - Bankowy Fundusz Leasingowy S.A., amounted to PLN 25 million. This guarantee relates to the closing of an issue of bonds.

18. ENFORCEABLE TITLES ISSUED BY THE GROUP

During the year 2005, PKO BP SA issued 30,284 banking enforceable titles for a total amount of PLN 324,204,403.

As regards KREDOBANK S.A., the law of Ukraine does not provide for issuing banking enforceable titles by banks in the meaning defined in the Polish Banking Law.

19. MANAGEMENT AND SUPERVISORY BOARDS OF PKO BP SA IN THE REPORTING PERIOD

Members of Management Board in the reporting period

Starting from 19 May 2005, members of the Bank's Management Board are appointed for a common term of three years.



Table 13. Members of Management Board in the reporting period

No.	Name and surname	Function	Date of appointment
1.	Andrzej Podsiadło	President of Management Board	20.06.2002; 19.05.2005 re-appointed to another term
2.	Kazimierz Małecki	First Deputy President	04.07.2002; 19.05.2005 re-appointed to another term
3.	Jacek Obłąkowski	Member	20.06.2002; 19.05.2005 re-appointed to another term
4.	Danuta Demianiuk	Deputy President	02.01.2003; 16.09.2005 re-appointed to another term
5.	Sławomir Skrzypek	Deputy President	20.12.2005
6.	Piotr Kamiński	Member	10.03.2003; 16.09.2005 re-appointed to another term
7.	Krystyna Szewczyk	Member	14.05.2004; 16.09.2005 re-appointed to another term

Other functions performed by Board members during the reporting period

Table 14. Other functions performed by Board members during the reporting period

No.	Name and surname	Assets and Capital & Liabilities Management Committee	Credit Committee	Steering Committee for the Integrated Information System	Steering Committee for Implementation of Branch Modernisation Program (set up on 15.03.2005)
1.	Kazimierz Małecki	Chairman		Chairman	
2.	Danuta Demianiuk	Vice-chairman	Chairman	Member	Vice-chairman until 19.12.2005
3.	Sławomir Skrzypek				Vice-chairman since 20.12.2005
4.	Piotr Kamiński		Vice-chairman		
5.	Jacek Obłąkowski			Vice-chairman	Chairman
6.	Krystyna Szewczyk	Member		Vice-chairman	Member



Members of Supervisory Board

Table 15. Supervisory Board in the reporting period

No.	Name and surname	Function	Date of appointment
1.	Bazył Samojlik	Chairman Member Chairman	25.08.2003 19.05.2005 20.05.2005
2.	Urszula Pałaszek	Member Vice-chairman	19.05.2005 20.05.2005
3.	Krzysztof Zdanowski	Member Secretary	19.05.2005 23.06.2005
4.	Andrzej Giryn	Member Member	25.03.2002 19.05.2005
5.	Stanisław Kasiewicz	Member Member	25.08.2003 19.05.2005
6.	Ryszard Kokoszczyński	Vice-chairman Member	06.06.2002 19.05.2005
7.	Jerzy Osiatyński	Member Member	25.03.2002 19.05.2005
8.	Czesława Siwek	Member	19.05.2005
9.	Władysław Szymański	Member Member	25.03.2002 19.05.2005
10.	Arkadiusz Kamiński*	Secretary	25.04.2002

* The appointment of Mr Arkadiusz Kamiński expired on 29 April 2005 due to submitted resignation.

Holders of commercial powers of attorney, Board meetings and implementation of resolutions of General Meetings and recommendations of the State Treasury Minister

As at 31 December 2004, there were 17 holders of commercial powers of attorney in PKO BP SA. During the year 2005, the Management Board of the Bank appointed 4 and dismissed 3 holders of commercial powers of attorney. As at 31 December 2005, there were 18 holders of commercial powers of attorney.

During the year 2005, the Management Board held 51 minuted meetings and took 364 resolutions.

The most important activities and decisions taken by the Management Board, which had an influence on the economic and financial position and activity of the Bank, have been presented in the relevant parts of this Directors' Report.

The Annual General Meeting of PKO BP SA was held on 19 May 2005.

The resolutions passed during the Annual General Meeting were implemented by PKO BP SA.

Rules for appointing and dismissing members of Management Board

In accordance with § 19 of the Bank's Articles of Association, Management Board members are appointed by the Supervisory Board for a common three-year term. Board members may only be dismissed for important reasons.

Authorisations granted to members Management Board

In accordance with § 20 of the Bank's Articles of Association, the scope of Management Board responsibilities includes all matters related to the conducting of Bank's affairs that have not been reserved by law or Articles of Association for the General Meeting or Supervisory Board, including purchase and disposal of property, property interests or perpetual usufruct, which do not require



consent of the General Meeting in accordance with § 9 section 1 point 5 of the Bank's Articles of Association.

Contracts concluded between the issuer and persons performing management functions

In accordance with the definition contained in § 1 section 2.1 point 35 letter a) of the Decree of the Minister of Finance of 19 October 2005 on current and periodic information provided by the issuers of securities (Journal of Laws No. 209 item 1744), members of Management Board are the persons who manage the Bank.

With each member of Management Board, the Bank concluded two contracts binding in 2005, which provide for compensation in the event of resignation or dismissal without an important reason:

- employment contract, which provides for a severance payment amounting to a 3-month basic salary recently received by the Board member,
- anti-competition contract, which provides compensation for complying with competition ban over a 6-month period after termination of the employment contract. This compensation amounts to 100% of the monthly basic salary received by the Board member prior to termination of the employment contract and is to be paid in arrears over the period of the ban.

The monthly basic salary is the equivalent of six times average remuneration determined in the Act of 3 March 2000 on the remuneration of persons managing certain legal entities (Journal of Laws No. 26, item 306 with subsequent changes).

Emoluments and other benefits provided to members of management and supervisory boards

Full information on emoluments and other benefits provided to members of the Bank's Management and Supervisory Boards in the reporting period has been presented in the Note 46 of the PKO BP SA Financial Statement for 2005.



Bank's shares held by members of Management and Supervisory Boards

Bank's shares held by members of the Bank's Management and Supervisory Boards as at 31 December 2005. The nominal value is PLN 1 per share.

Table 16. Shares held by Members of the Bank's Management and Supervisory Boards

No.	Name and surname	Number of shares held at the date of submitting this report
I. Management Board		
1.	Andrzej Podsiadło	450
2.	Kazimierz Małecki	2627
3.	Sławomir Skrzypek	-----
4.	Danuta Demianiuk	-----
5.	Piotr Kamiński	-----
6.	Jacek Obłąkowski	512
7.	Krystyna Szewczyk	-----
II. Supervisory Board		
1.	Bazył Samojlik	-----
2.	Urszula Pałaszek	-----
3.	Krzysztof Zdanowski	-----
4.	Andrzej Giryn	-----
5.	Stanisław Kasiewicz	106
6.	Ryszard Kokoszcyński	-----
7.	Jerzy Osiatyński	-----
8.	Czesława Siwek	4000
9.	Władysław Szymański	-----

Members of the Bank's Management and Supervisory Boards as at 31 December 2005 have no shares in subordinate entities.

20. SIGNIFICANT POST BALANCE SHEET EVENTS

- On 1 January 2006, PKO BP SA introduced a new Table of Banking Fees and Commission Rates. The changes result from market conditions and the significantly extended scope of the Bank's operations.
- On 24 January 2006, PKO BP SA concluded with Credit Suisse Asset Management Holding Europe (Luxembourg) S.A. a conditional agreement for the sale of 45,000 registered preference shares of PKO/Credit Suisse Towarzystwo Funduszy Inwestycyjnych S.A. The Bank will acquire these shares once it fulfils all the conditions specified in the agreement. The expected transfer of the shares will take place by the end of the first quarter 2006. The shares acquired by the Bank account for 25% of votes at the company's Annual General Meeting. As a result of this acquisition, PKO BP SA will hold 75% of shares in the company's share capital and votes at the Annual General Meeting. The price for the shares acquired by the Bank amounts to PLN 55 million.
- On 25 January 2006, PKO BP SA concluded an agreement with its customer for issuing banking guarantee. Under this agreement, the Bank is required to issue, at the request of the customer, a guarantee to the Customs Office in respect of an excise security amounting to 309 million. The agreement for issuing banking guarantee binds from 1 February 2006 to 31 January 2007, plus a 90-day liability period. As at the date of this agreement, the total value of all agreements signed by the Bank with that customer amounted to PLN 1,104.9 million.
- On 27 January 2006, PKO BP SA concluded a Partners' Agreement with the City of Sopot and NDI S.A., with the participation of Centrum Haffnera Sp. z o.o., for an investment project relating to re-vitalisation of Sopot's tourist centre.



The Bank's will engage through take up app. 49.4% of shares in Centrum Haffnera Sp. z o.o.) and loan exposure.

The Bank will participate in the above project upon the fulfilment of the conditions specified in the Agreement.

- On 14 February 2006, the Bank received a report from the rating agency Capital Intelligence in which the rating for the financial strength of PKO BP SA was increased from BB+ to BBB- with a stable outlook. This change was made owing to the improving quality of the Bank's loan portfolio and increasing effectiveness of its operations.
- On 8 March 2006 the Bank's Supervisory Board made a resolution accepting Mr Piotr Kamiński membership resignation in the PKO BP SA Supervisory Board starting from 9 March 2006 that is at the date of Mr Piotr Kaminski election at the position of Vice President at Bank Pocztowy SA
- On 16 March 2006 PKO BP SA received the approval of the Chairmen of Office of Competition and Customer Protection for concentration resulting from the overtake the control through PKO BP SA over PKO/Credit Suisse Towarzystwo Funduszy Inwestycyjnych SA

Significant post-balance sheet events in other PKO BP SA Group companies:

- On 9 January 2006, Bankowe Towarzystwo Kapitałowe S.A. – PKO BP SA subsidiary – took up 351 shares in the increased share capital of FINDER Sp. z o.o. The acquisition price amounted to PLN 1 million. As a result of the above transaction, the share of Bankowe Towarzystwo Kapitałowe S.A. in the share capital and votes at the Shareholders' Meeting of FINDER Sp. z o.o. increased from 42.31% to 46.43%. The increase in the share capital was registered with the National Court Register.
- On 9 March 2006 the Extraordinary General Shareholders Meeting of KREDOBANK SA – of the Bank's subsidiary made a resolution to increase the share capital by UAH 75,750 thousands. The subscription period will be last from 26 April to 26 October 2006.

21. CONTRACT WITH THE ENTITY AUTHORISED TO AUDIT FINANCIAL STATEMENTS

On 8 August 2005, the Bank entered into a contract with Ernst & Young Audit Sp. z o.o., an entity authorised to audit financial statements, for an audit of stand-alone financial statements and consolidated financial statements for the years ending 31 December 2005, 2006 and 2007 and a review of stand-alone financial statements and consolidated financial statements for 6-month periods ending 30 June 2005, 2006 and 2007.

Total fees under the contracts concluded by Ernst & Young Audit Sp. z o.o. and Group entities related to reviews and audits of standalone and consolidated financial statements amounted to PLN 2,247.0 thousand (net of VAT) for the year 2005 and PLN 1,568.2 thousand (net of VAT) for the year 2004.

The total amount of fees arising from contracts concluded with Ernst & Young Audit Sp. z o.o. for remaining services other than reviews and audits of financial statements was as follows: PLN 2,319.4 thousand (net of VAT) for the year 2005 and PLN 2,889.0 thousand (net of VAT) for the year 2004.

The significant part of remuneration arising from contracts other than reviews and audits of financial statements concluded between the Bank and Ernst & Young Audit Sp. z o.o. was associated with the assistance in IFRS implementation in 2005 and activities concerning the privatisation of the Bank in 2004.



22. MANAGEMENT BOARD REPRESENTATIONS

The Management Board of PKO BP SA hereby represents that, according to its best knowledge:

- the annual financial statements and comparative data were prepared in accordance with the accounting principles in force and give a true and fair view of the Group's financial position and results;
- the annual Directors' Report on the activities of the PKO BP SA Group gives a true view of the Group's development, achievements and standing, including a description of the main risks.

The Management Board of PKO BP SA hereby represents that the entity authorised to audit financial statements which performed an audit of the annual financial statements of PKO BP SA was selected in accordance with law, and that both this entity and the certified auditors who performed this audit met the conditions required to issue an impartial and independent audit opinion, in accordance with the relevant national laws.

This *Directors' Report on the activities of the PKO BP SA Group in 2005* consists of 43 consecutively numbered pages.

President of Management Board
Andrzej Podsiadło

First Deputy President
Kazimierz Małecki

Deputy President
Danuta Demianiuk

Deputy President
Sławomir Skrzypek

Member
Jacek Obłąkowski

Member
Krystyna Szewczyk