



PZU SA  
PZU Życie SA  
PTE PZU SA, TFI PZU SA

in the right way

2006

annual report of the PZU Group



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## 1. Basic information on the **PZU SA Group**

annual report

# 2006

**Headed by Powszechny Zakład Ubezpieczeń SA (PZU), the PZU Group** is one of Poland's largest financial institutions and one of the leading insurance groups in Central and Eastern Europe. The Group's main advantages include its strong competitive position, high level of equity and operating efficiency.

At the PZU Group we are committed to sustained growth, systematic improvement of the quality of services and to meeting the needs of our customers. The Group's key companies are valued for their experience, traditions, strong financial condition and excellent access to agents and branches.

The PZU Group's strong competitiveness stems mainly from our leading position on the Polish insurance market, both in the life and property and casualty segments, due to our very strong sales capability and high brand awareness in Poland. Additionally, the PZU Group has been able to keep its costs low in comparison to its direct competitors in recent years. All of these factors have contributed directly to the Group's excellent operating performance.

The PZU Group offers the widest range of products available on the Polish market, while systematically expanding its range of services. Our customers can choose from nearly 200 insurance products, including property and casualty insurance, as well as life insurance. Other business operations include management of an open pension fund, investment funds and savings programmes.

The PZU Group's leadership on the Polish insurance and financial markets has been recognized in a number of independent rankings, as well as titles and awards. The PZU Group took second place in the ranking of the Top 100 Most Valuable Polish Companies carried out by A.T. Kearney consultants for the Polish edition of Newsweek (the PZU Group was estimated to be worth PLN 41,912 million in 2006). In 2006, just as in each of the previous five years, Poles chose PZU as Reader's Digest's 'Most Trusted Brand' in the largest European consumer survey. In Poland, the PZU brand came third in a ranking by Rzeczpospolita daily and Ernst & Young. The PZU brand is estimated to be worth PLN 1.9 billion, which is more than any other domestic brand and not just in the insurance market, but also across the financial sector as a whole.

An important part of the PZU Group's activity is played by initiatives in the area of *Corporate Social Responsibility* (CSR). These initiatives help to further build our position within Polish society, in the business environment and vis-à-vis various stakeholders, including customers, employees, shareholders, business partners, public opinion, institutions, organizations and the media.



## 2. Financial highlights of the PZU Group in 2006 r.

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annual report

### The PZU Group's financial highlights

Source: The PZU Group, financial statements

Item	PZU Group	PZU SA	PZU Życie SA
Gross premium written ('000 PLN)	15,454,108	7,677,355	7,589,821
Premium earned net of reinsurers' share ('000 PLN)	15,098,464	7,383,274	7,579,467
Gross claims paid ('000 PLN)	8,775,362	4,368,448	4,276,050
Claims paid net of reinsurers' share ('000 PLN)	8,483,071	4,102,413	4,276,050
Loss ratio (%)	57,2	57,1	56,7
Costs of insurance activities ('000 PLN)	2,952,924	1,974,327	919,076
Acquisition expenses ('000 PLN)	1,413,406	1,004,348	370,759
Administrative expenses ('000 PLN)	1,643,197	1,066,050	550,863
Reinsurance commission and share in reinsurers' profits ('000 PLN)	103,679	96,071	2,546
Combined Ratio (%)	x	83,8	x
Underwriting result ('000 PLN)	3,577,236	1,362,082	2,265,454
Investment income ('000 PLN)	3,923,911	2,925,492	2,466,297
Gross profit ('000 PLN)	4,617,237	3,737,300	2,367,146
Net profit ('000 PLN)	3,706,456	3,280,883	1,936,329
Assets ('000 PLN)	49,445,091	26,204,195	27,685,532
Equity ('000 PLN)	13,330,887	13,448,705	4,517,269
Investments ('000 PLN)	46,614,710	24,050,156	27,051,278
Gross technical reserves ('000 PLN)	33,602,247	11,955,358	21,458,005
Technical reserves coverage ratio (%)	138.7	169.0	121.4
Solvency margin coverage ratio (%)	x	1,004.1	297.1
ROE (w %)	30.6	26.9	45.5
ROA (w %)	8.0	13.3	7.5



Dear Ladies and Gentlemen,

2006 was an excellent year for the PZU Group. We continued to improve our financial performance and all of the Group's companies increased revenues and incomes. This was largely the result of the good economic situation we have been enjoying in Poland recently.

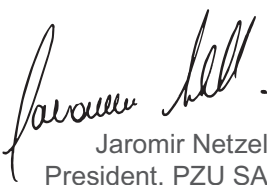
The record PLN 3.7 billion in profits generated by the Group put us at the top of the ranking of the most profitable institutions in Central Europe. Even more importantly, this was not just the outcome of a strong business environment, including improving macroeconomics and strong growth on the Warsaw Stock Exchange, but was above all the effect of the enormous commitment of our staff across all the Group's companies. I have always recognized the efforts put into developing the Group's value and will always continue to do so. This time, at the end of the year, all employees have received special bonuses in recognition of the excellent results. A similar decision was also taken by the management boards of the Group's companies after the 1st quarter results.

We have improved our relationships with employee representatives. An agreement put an end to the collective dispute that had lasted for more than a year. We quickly worked out sound principles for remuneration increases. The Management Board of PZU SA, which I have the pleasure of heading, is deeply committed to the principle that the greatest asset of any financial institution is its employees. Without them, management's objectives cannot be met.

At the PZU Group, we are facing ambitious challenges for this and the coming years. Two years ago, the Group adopted a mid-term strategy, including a range of useful propositions, and now, having modified them, it is time to implement them.

This will involve a thorough upgrade of our branch network to better meet the needs of our customers and accommodate the size of the Group and its need for fast growth. We need to be investing in developing our sales network and training, but also in modern distribution channels for our products to meet the growing demands of our customers. The decision to retain all of the Group's profits from last year will definitely contribute to our plans to upgrade operations. Much of this money will go on capital projects. We must remember that in order to retain our leading position in this part of Europe we must also be mindful of access to new customers. Indeed, the PZU Group is planning to enter the banking sector, and PZU Życie SA intends to acquire a private medical service provider. We also need more investment in our Ukrainian business and will have to further diversify our investment portfolio by activating our operations on the property market. We are also considering acting through private equity funds.

All of these measures, if correctly executed, should provide a strong stimulus for growth across the entire PZU Group for years to come. In 2007, once again the PZU Group will generate record profits, set at up to PLN five billion. We need to fully exploit this time, in all fields. We need to remember that prosperity will not last forever. Strong economic growth should help the PZU Group to strengthen its equity and organization, so as to secure our future and confidently face off stiffening competition from international players, both in Poland and throughout Central Europe.

  
Jaromir Netzel  
President, PZU SA



## 4. Factors and events influencing PZU Group operations in 2006

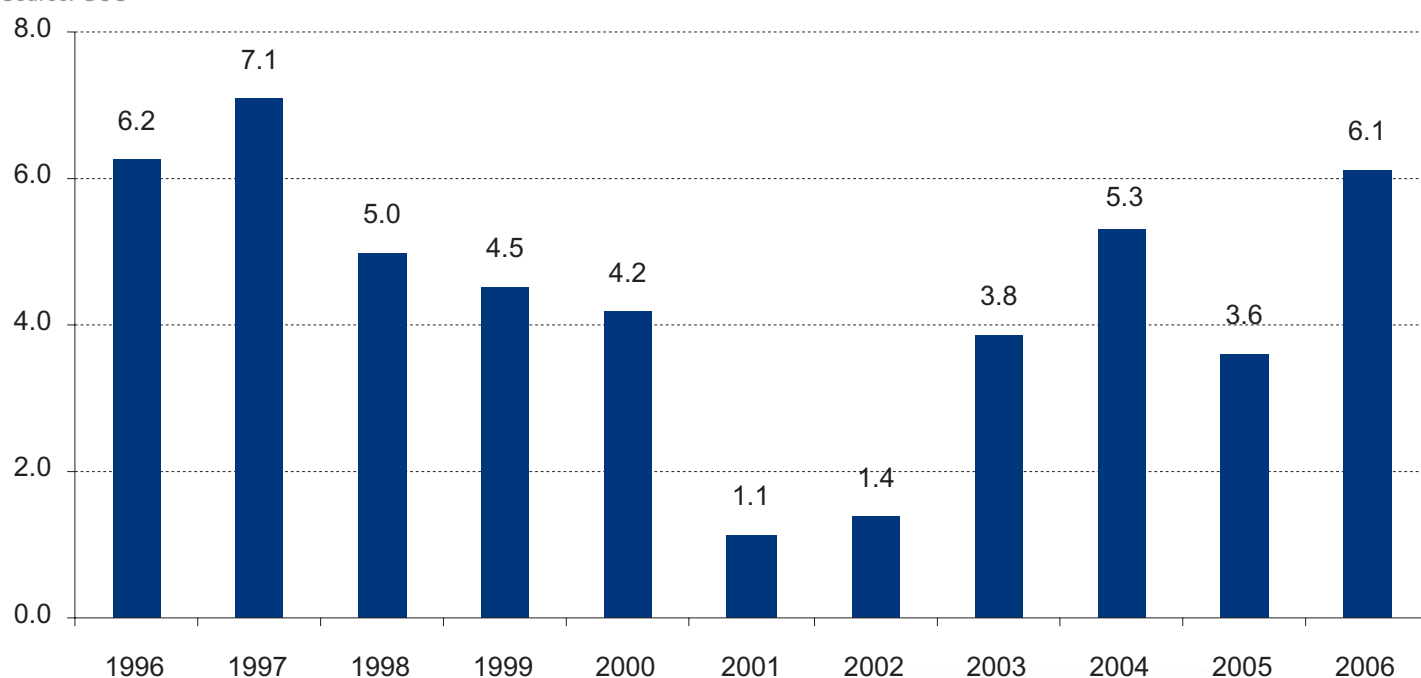
### 4.1. Poland's economic situation in 2006

#### 4.1.1 Economic growth

According to the estimates of the Polish Central Statistical Office (GUS) for 2006, the economy grew at 6.1% (the highest rate since 1998). The main drivers of growth included household consumption and capital investment. Investments rose by 16.5% and were generated mainly by the enterprise sector and the public sector following an increased rate of absorption of EU funds (mainly on infrastructure). Household consumption rose by 5.2%, which was helped by a high increase of disposable income (by more than 6% in real terms), including a gradual increase in employment and real incomes. While exports grew dynamically (a 21% increase in goods and services, according to the balance of payments in Euro terms), strong domestic demand also drove imports (up 22% in Euro terms), boosting the overall current trade deficit to 2.3% of GDP (from -1.7% of GDP in 2005). However, some other new European Union Member States, notably the Baltic States, Cyprus, Slovakia and Slovenia, have showed higher growth rates than Poland.

Gross Domestic Product growth in Poland, 1996 – 2006 (real terms, %)

Source: GUS



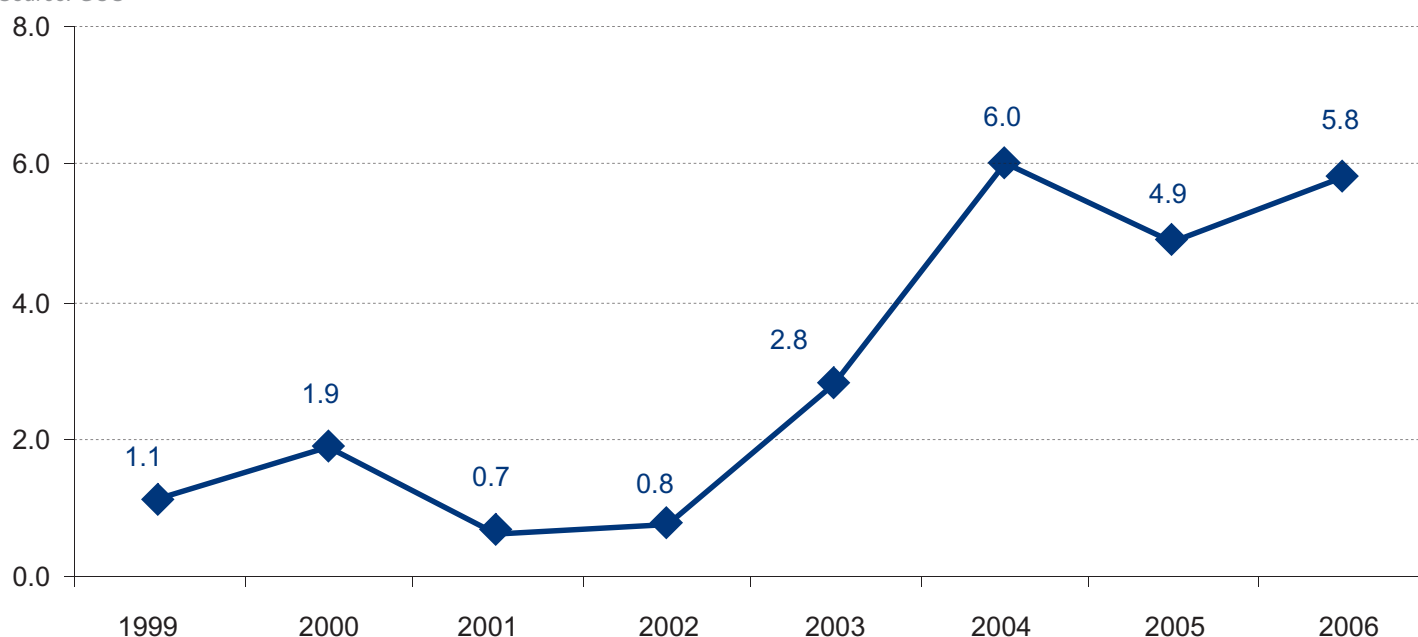


#### 4.1.2 Companies' financial performance

The excellent economic environment in 2006 translated into higher rates of return. The cost level indicator stood at 94.2% (compared to 95.1% the year before), the rate of return on sales of products, goods and materials at 5.5% (from 5.3%), the return on sales ratio at 5.8% (from 4.9%) and the net profitability ratio at 4.7% (from 3.9%). The liquidity ratio was at 35.1% (vs. 31.9%). In 2006, 50.4% of all enterprises reported export sales (compared to 48.2% in 2005). Export sales accounted for 20.2% of total sales of products, goods and materials (from 18.7%) and 81.6% of all exporters turned a profit (compared to 78.4% in 2005). In comparison to 2005, net revenues from the sales of products, goods and materials rose in all sectors, but especially in the construction sector (by 21.9%), the hotel and restaurant sector (by 16.6%), trade and maintenance (by 16.2%) and industrial processing (by 15%). Only two of 39 groups reported by the Polish Classification of Activity (PKD) reported lower incomes, i.e. in manufacturing of office machines and computers (by 3.5%) and coal mining (by 3.7%).

Return on sales ratio in Poland, 1999–2006 (%)

Source: GUS





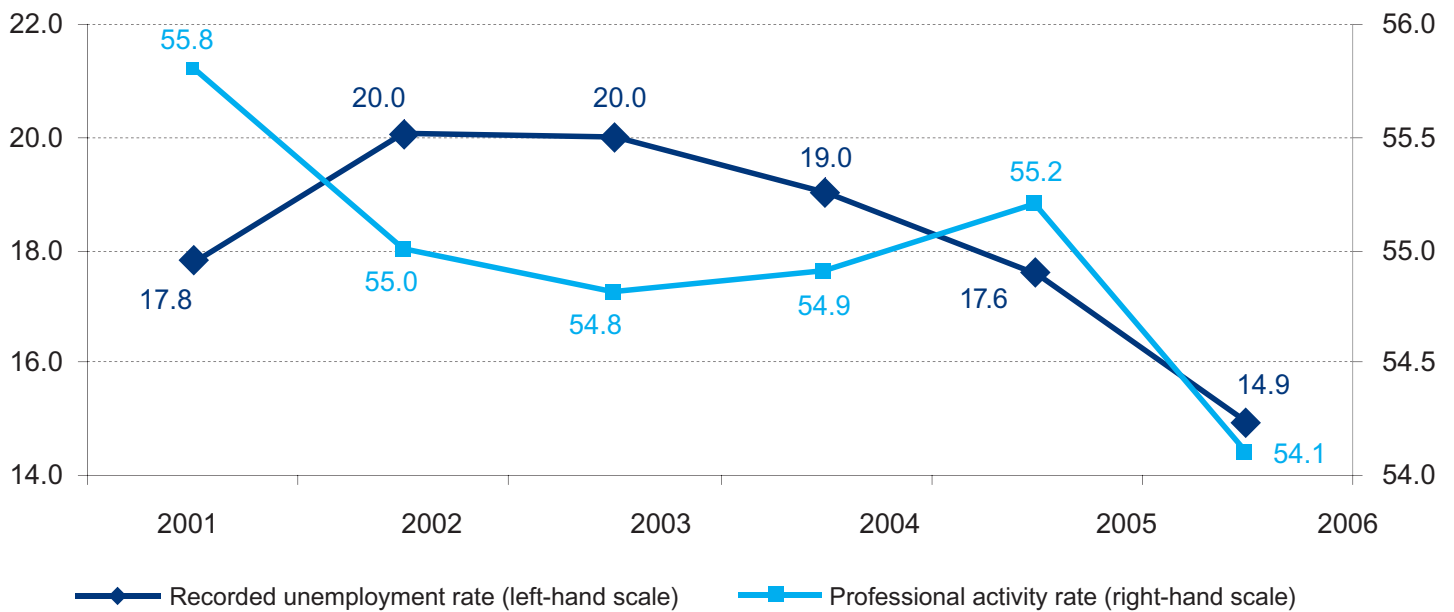
## 4.1.3 Labour market

In 2006, the labour market reported positive developments. The number of unemployed dropped by nearly 0.5 million (to 2,309,000) and the end-of-year registered unemployment rate stood at 14.9% (compared to 17.6% at the end of 2005). This improvement is partly due to an increase in a number of employed and partly to retirements from the labour market, including economic emigration. As a result, the economic activity of the population dropped to 54.1% (compared to 55.2% in 2005).

A wave of economic emigration and productivity gains increased the pressure on salaries. In 2006, the average salary across the economy increased by 4% in real terms and reached PLN 2,663 in the 4th quarter (including PLN 2,823 in the enterprise sector).

Unemployment rate and economic activity ratio in Poland, 2001-2006 (%)

Source: GUS



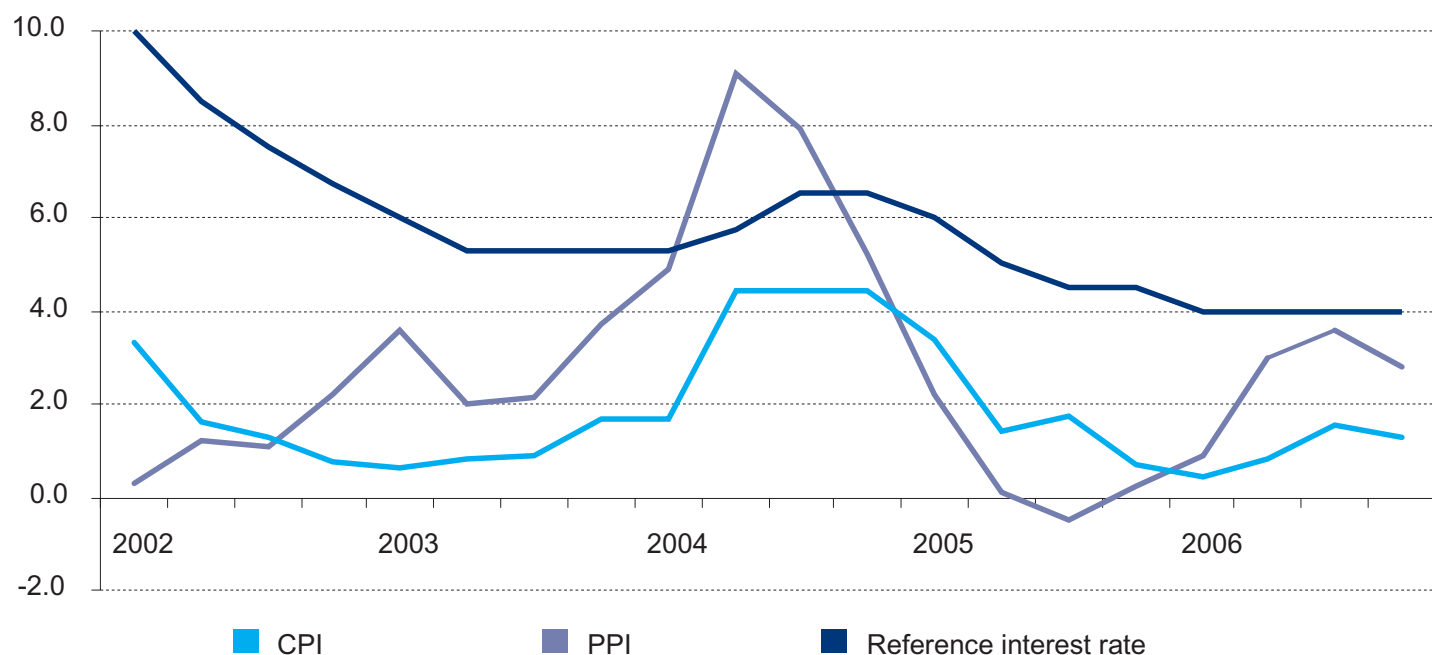
## 4.1.4 Prices

The Consumer Price Index (CPI) rose in 2006 by 1% on average (or 1.4% annually). Despite the drought, food prices only increased by 0.6%. The growing strength of the zloty dampened fuel cost increases to 1.5%. The low level of the inflation rate was sustained throughout the year, despite a gradual increase in domestic demand. This was helped by: globalization (deflation of goods imported from India and China), expansion of large-area retailers and by bans on Polish food imports imposed by Russia and Ukraine.

At the end of the year, the Producer Price Index (PPI) flattened out at 2.6% (a 2.3% yearly average). This was largely the effect of rising costs of metallic ore extraction and the production of electricity, water and gas. Within manufacturing industry, prices remained stable (at 0.7% growth) but as the construction market boomed, so did construction service prices, reaching 4.3%.

CPI and PPI inflation and reference interest rate in Poland, 2002–2006 (%)

Source: GUS



## 4.2 Centralization of financial supervision in Poland

In 2006, Poland saw an important change in the supervision over financial institutions. The Polish Financial Supervision Authority (PFSA) was established on 19 September, pursuant to the Act on supervision of financial market of 21 July 2006 (Journal of Laws, No. 157, item 1119). The new regulator pooled the responsibilities of the former Polish Securities and Exchange Commission and the Insurance and Pension Funds Supervisory Commission and is set to absorb the

responsibilities of the Commission for Banking Supervision as of 1 January 2008. In this way, the Polish Financial Supervision Authority supervises the capital market, insurers and pension funds and provides supplementary supervision over financial conglomerates that own the supervised entities. The Polish Financial Supervision Authority (PFSA) itself reports to the Prime Minister.

## 4.3 The Polish financial market in 2006

### 4.3.1 The currency market

In 2006, the zloty gained both against the US Dollar (11%) and the Euro (0.7%). The appreciation versus the US Dollar occurred during the second half of the year and was driven by the US currency's weakening against the Euro on the international markets and, on the domestic market by an improving economic performance (higher than forecast) and budgetary spending (lower than forecast). The zloty's real effective exchange rate remained unchanged throughout the year, boosting the competitiveness of Polish exports. The zloty/US Dollar and the zloty/Euro exchange rates displayed less variability than in previous years, stabilizing the Polish currency on a horizontal trend.

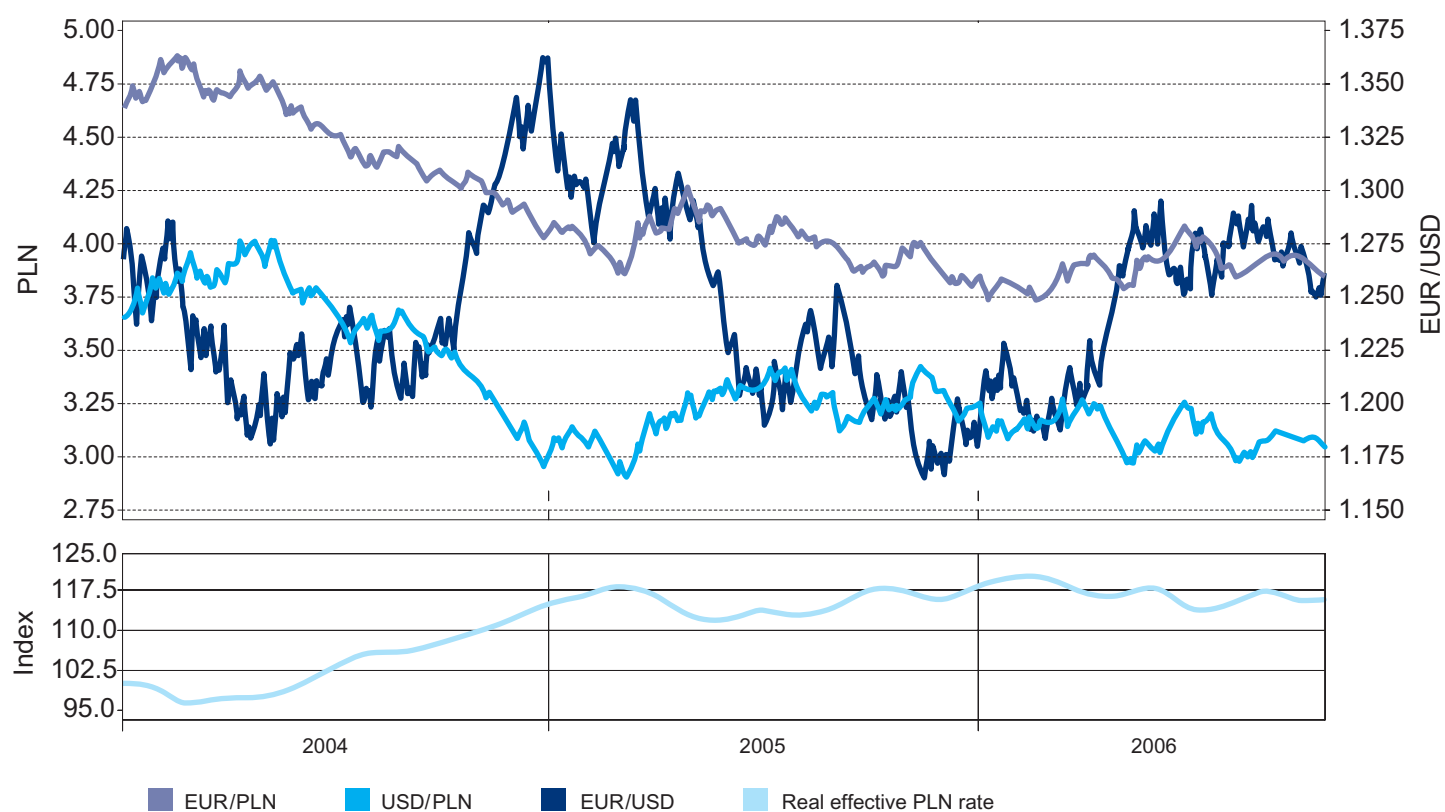
Due to the floating exchange rate regime, the zloty was influenced by developments in the balance of payments: the higher current-account deficit was compensated by financial inflows, especially from direct foreign investments, transfers from the EU and by the foreign borrowing of the domestic private sector. Short-term capital reduced its involvement in Polish treasury papers and corporate equities.



# 06

The spot PLN/US Dollar and PLN/Euro exchange rates, Euro/US Dollar rate and the effective PLN rate, 2004-2006

Source: Reuters EcoWin



## 4.3.2 The money market and treasury bond market

Central bank interest rates were cut twice, both during the first quarter of 2006. As a result, the reference interest rate (seven-day open market operations) was reduced by 50 bps to 4% (compared to a 200 bps reduction in 2005). The Monetary Policy Council took these decisions when the inflation rate reached a record-low of 0.6-0.4%, between January and March 2006. Despite the very good prospects of the inflation rate staying safely within the NBP's inflation target range (2.5% +/- 1 points) the market behaved as if it were expecting higher interest rates in the following year. This was manifested in higher yields on bonds and higher interest rates offered on household deposits, especially during the first half of 2006. As a result, the yield on two-year bonds dropped by 0.5 points, on three-year bonds by 0.07 points and the interest rate on zloty-denominated household deposits by 0.12 points. Four-year bonds saw yield improvement of 0.04 and ten-year bonds of 0.09 points.

Wholesale bonds sold for PLN 70.8 billion, up by PLN 5.7 billion (8.7%) from 2005. The government bond debt rose to PLN 308 billion at the end of the year (up 14.8% compared to the end of 2005). The financial sector debt amounted to PLN 504.9 billion, or 47.7% GDP.

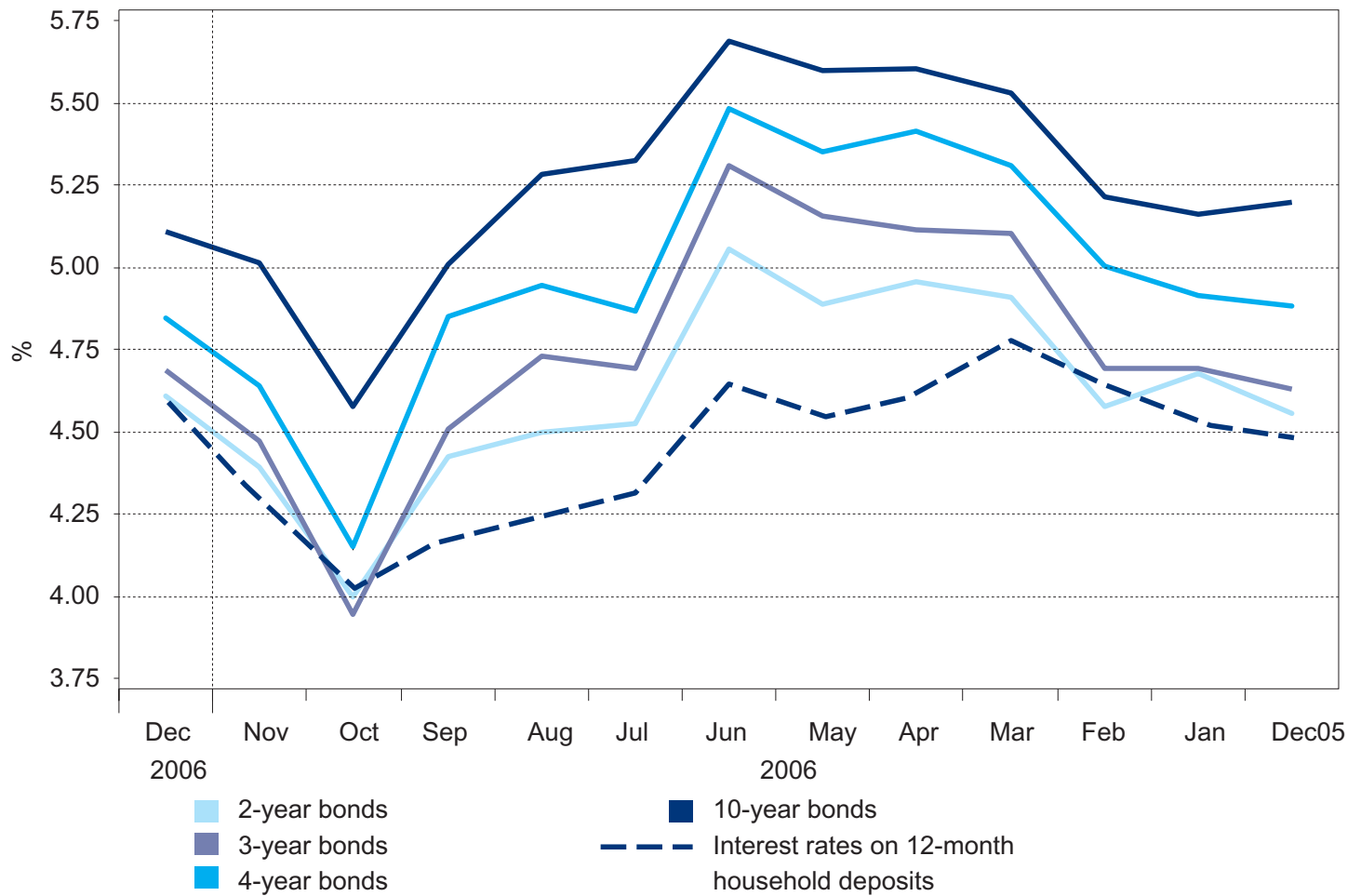
Zloty-denominated deposits from individuals and companies rose to PLN 366 billion (up 13.8% on 2005). In 2006, the rate of growth in household deposits was high at 8.4%, but far lower in comparison to the record-breaking 25.8% growth in corporate deposits. Most of the corporate investment programmes were financed from retained earnings. Just as in 2005, growth was concentrated on current deposits, from both households and companies, even though a growing portion of savings was shifting into investment funds.



# 06

Yields on treasury bonds and household deposit interest rate, 2006 (%)

Source: Reuters EcoWin



#### 4.3.3 The capital market

A fifth year of growth brought the Warsaw Stock Exchange its fastest rate of asset growth, caused mainly by increases in share prices. The market-wide WIG Index rose by 41.6% vs. 2005 in the highest upturn since 1993 (when it gained 44.9%). The end-of-year capitalization of the Warsaw Stock Exchange amounted to PLN 438 billion (up 42% on 2005), equivalent to 41.4% of GDP, compared to 31.4% of GDP in 2005.

The improving financial condition of companies, resulting from the rapid pace of economic growth and sustained high demand for listed companies from institutional investors (mainly domestic investment funds and open pension funds) and individual investors (with an awakening of international involvement) caused record double-digit increases in all of the important indices. In comparison to 2005, the blue-chip WIG20 rose by 23.8%, while the mid-cap and small enterprise indices, MIDWIG and WIRR rose by 69.1% and 132.4%, respectively.

IPOs also provided a high rate of return, with 38 companies, including six international ones, offering their stock in 2006 (10% more than in 2005). Dividends were another significant source of returns and the PLN 12.8 billion paid out by companies set an absolute record in the history of the Warsaw Stock Exchange. The dividend rate rose to 2.6%. A confirmation of this increased stock-exchange activity came in the form of record trading levels in shares (more than PLN 343 billion, including a day average of PLN 320.3 billion in a staggering 83% increase on 2005) and in derivatives (deal numbers up 20% and trading volume up by more than 50% vs. 2005).

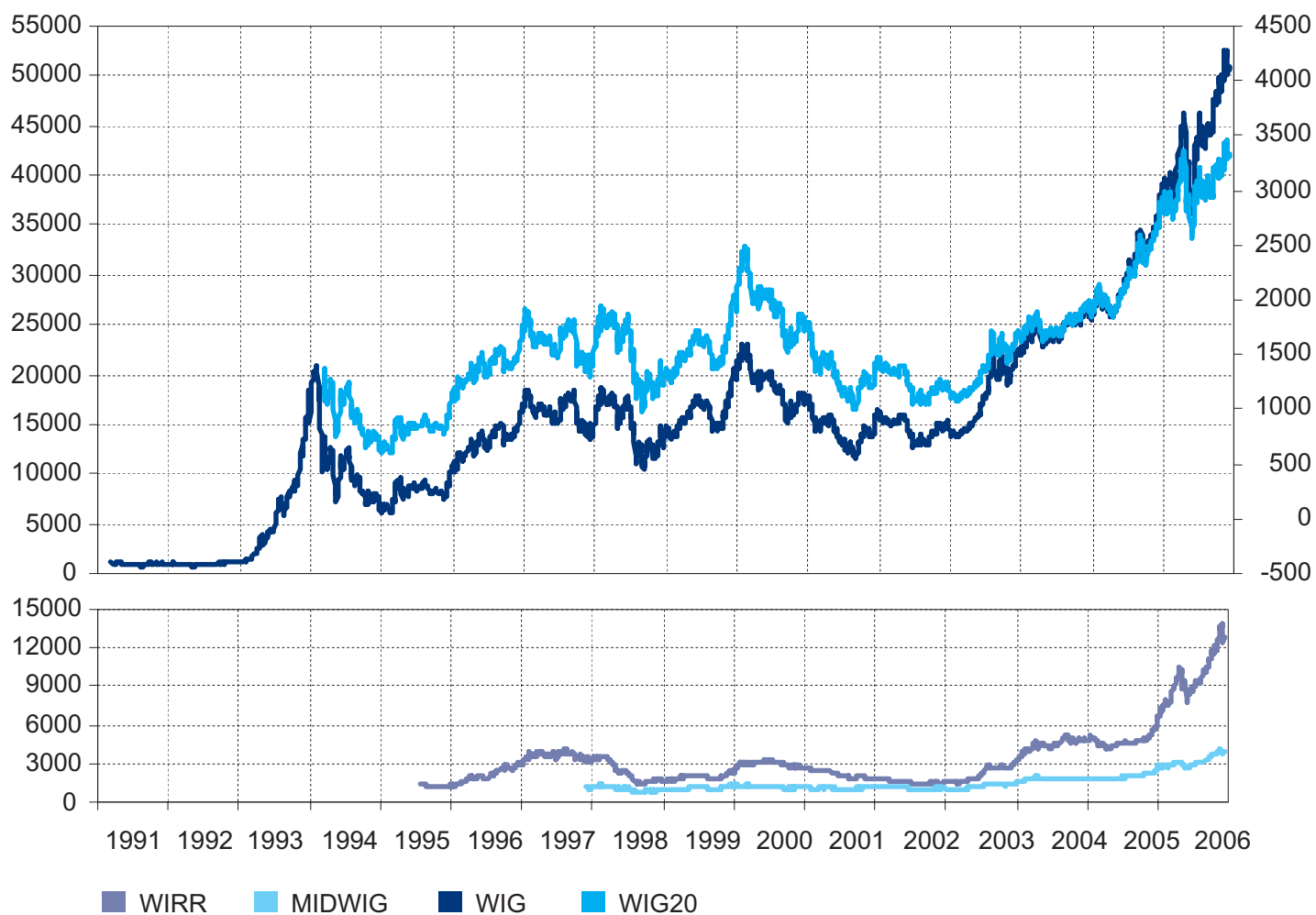




# 06

The Warsaw Stock Exchange indices: WIG20, WIG, MIDWIG and WIRR, 1991–2006

Source: Reuters EcoWin



## 4.4 The Polish insurance market and pension and investment funds in 2006

### 4.4.1 The insurance market

#### Insurance companies

At the end of 2006, there were 75 companies, of which 65 were domestic and 10 international, holding licenses for insurance operations in Poland. This number included 33 life-insurers (Segment 1) and 42 non-life insurers (Segment 2).

#### Insurance companies based in Poland and Polish branches of international insurers in 2006

Source: The PFSA

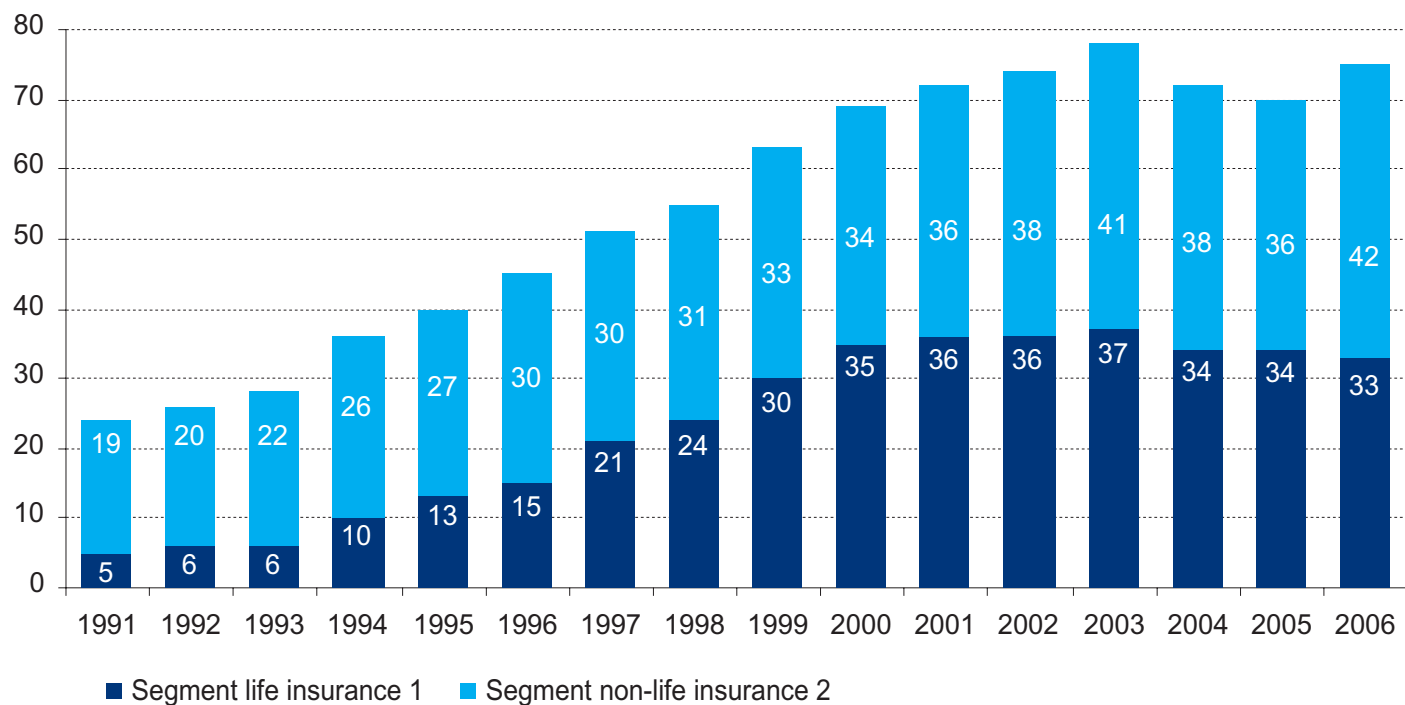
Segment	Insurance companies based in Poland				Polish branches			Total Polish and international
	Public listed	Mutual	Reinsurers	Total	EU/EFTA based	Other countries	Total	
Life	30	2	0	32	1	0	1	33
Property and casualty	25	7	1	33	8	1	9	42
Total	55	9	1	65	9	1	10	75



The number of notified insurance companies from European Union Member States and EFTA countries rose significantly, with over 350 companies expressing their intention to exercise the freedom to provide services in Poland. At the same time, 18 Polish companies notified their intention to start selling insurance in other European Union Member States.

## Licensed insurance companies in Poland, 1991-2006

Source: The PFSA



## Market shares

During the year, 13 life insurers (Segment 1) and 27 non-life insurers (Segment 2) increased their market shares. The PZU Group remained the main player, with a 36% share of the market in Segment 1 and a 47% share in Segment 2.

In 2006, just as in the previous years, both segments of the insurance market were highly concentrated, with the top-five insurers representing 71% of the gross premiums written in life insurance and 76% in property and casualty insurance.

## Sector performance

The Polish insurance sector generated ca. PLN 37.5 billion in total gross premiums written. This represented a 21% increase compared to 2005.

In life insurance, gross premiums written rose 38% to more than PLN 21 billion. Smaller companies grew faster than the top five players, as had also been the case in previous years. The internal structure of Sector I premiums was slightly modified, with 48% of premiums from group insurance and the remaining 52% from individual insurance. Regular premiums accounted for 56% of the total and single premiums for 44%.

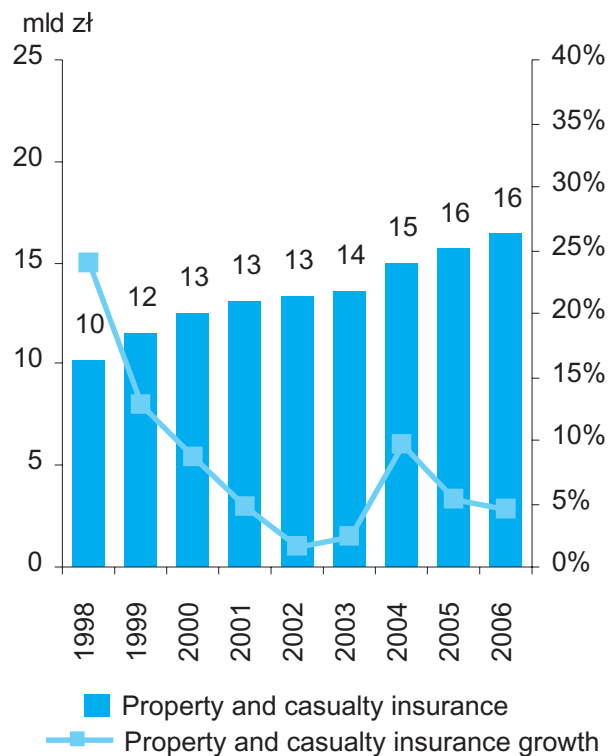
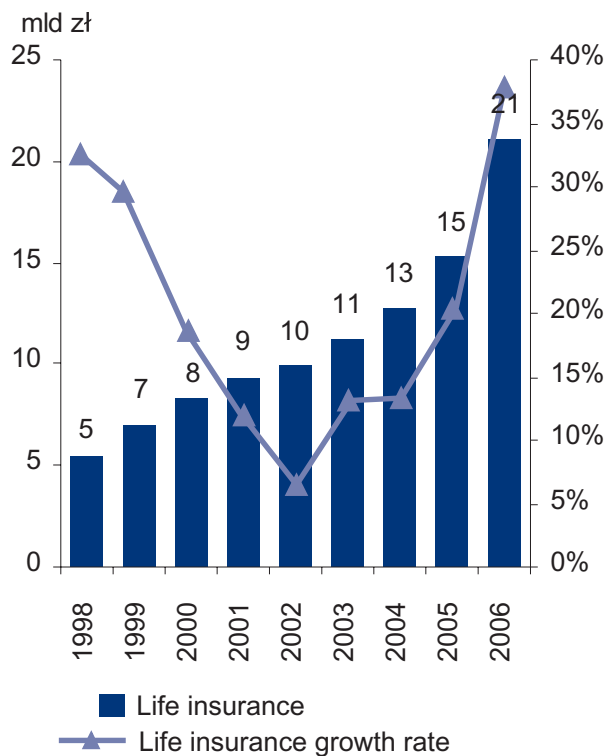
Property and casualty gross premiums written rose to PLN 16 billion, or up 5% on the 2005 figure. Just as with life insurance, this segment also saw smaller companies, outside the top five, post the highest growth rates.



# 06

The Polish insurance market growth measured by gross premiums written, 1998–2006

Source: The PFSA



In the structure of the total gross premiums written, 2006 was the first year when life premiums (at 56%) were higher than property and casualty premiums (at 44%).

Insurance companies paid out ca. PLN 16.8 billion in gross claims and benefits, or ca. 6% more than in 2005. This was split between PLN 8.5 billion in life insurance, up 12%, and PLN 8.4 billion in property and casualty insurance, or ca. 1% more than in 2005.

The technical result of the insurance sector amounted to PLN 4.8 billion in 2006 and was up by 42% compared to 2005.

The technical results of the life insurance segment reported PLN 3.2 billion and the property and casualty segment PLN 1.6 billion.

The aggregate financial result amounted to PLN 6.8 billion on a 29% growth above the 2005 figure.

In 2006, the total assets of all insurance companies registered by the PFSA amounted to PLN 108.3 billion, of which 67% were investments. The total technical reserves of the sector amounted to PLN 77.7 billion.



## 4.4.2 The pension funds market

### Players on the open pension funds market

There were 15 general pension fund companies (PTEs) on the Polish market at the end of 2006.

The open pension fund (OFE) market in Poland, 2000–2006

Source: The PFSA

OFE	2000	2001	2002	2003	2004	2005	2006
Number of OFE	21	17	17	16	15	15	15
OFE members (millions)	10.4	10.6	11.0	11.5	12.0	11.7	12.4
Net assets (PLN billions)	9.6	19.4	31.6	44.8	62.6	86.1	116.6

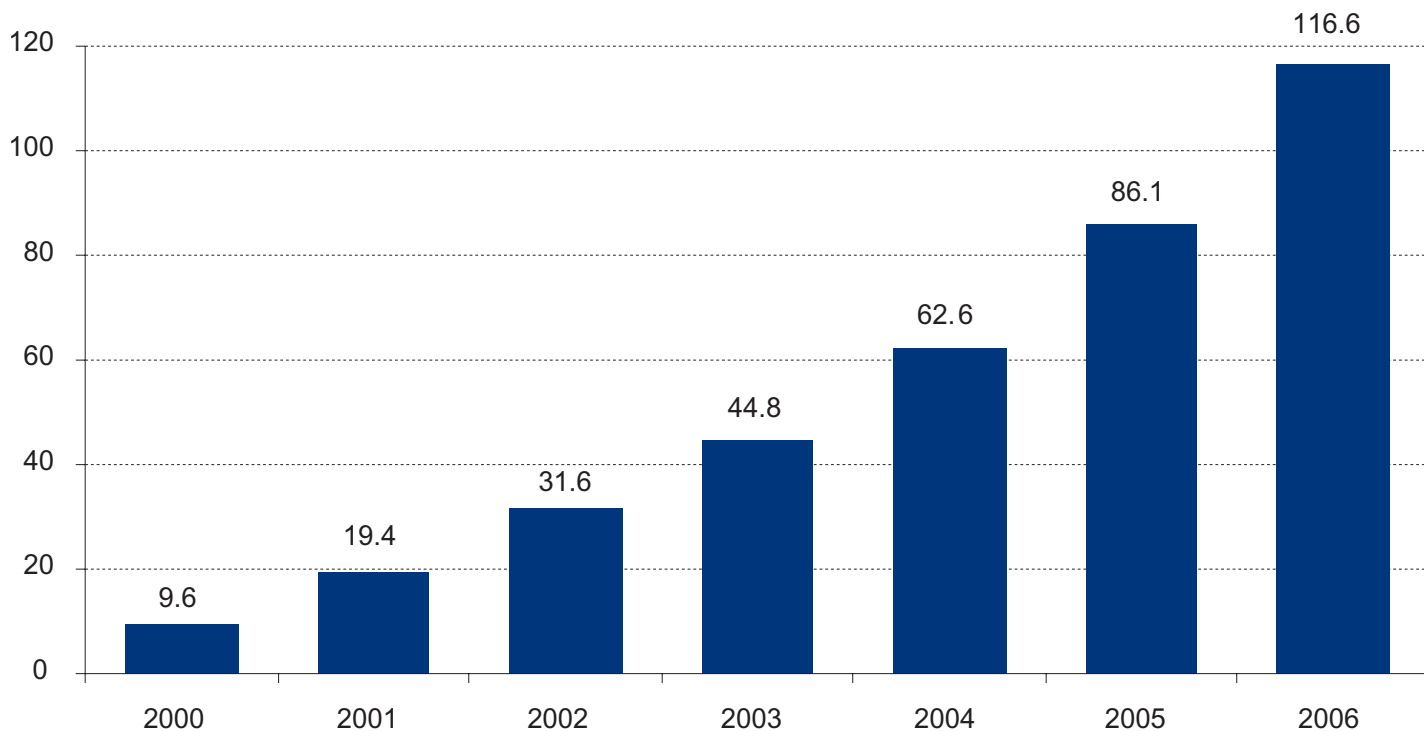
### Net assets

At the end of 2006, the open pension funds managed a total of PLN 116.6 billion in assets. This was PLN 30.5 billion, or 35%, more than in 2005.



## Net assets of the open pension funds market in Poland, 2000-2006 (PLN billion)

Source: The PFSA



## Fund members and transfers

At the end of 2006, OFEs operating in Poland had 12.4 million members, that is 700,000 (6%) more than in 2005.

The total transfer of pension fund members during all transfer sessions in 2006 amounted to 329,000 people, or 2% more than the year before. This meant that from the end of 2005 on average 3% of fund members changed their funds in 2006.





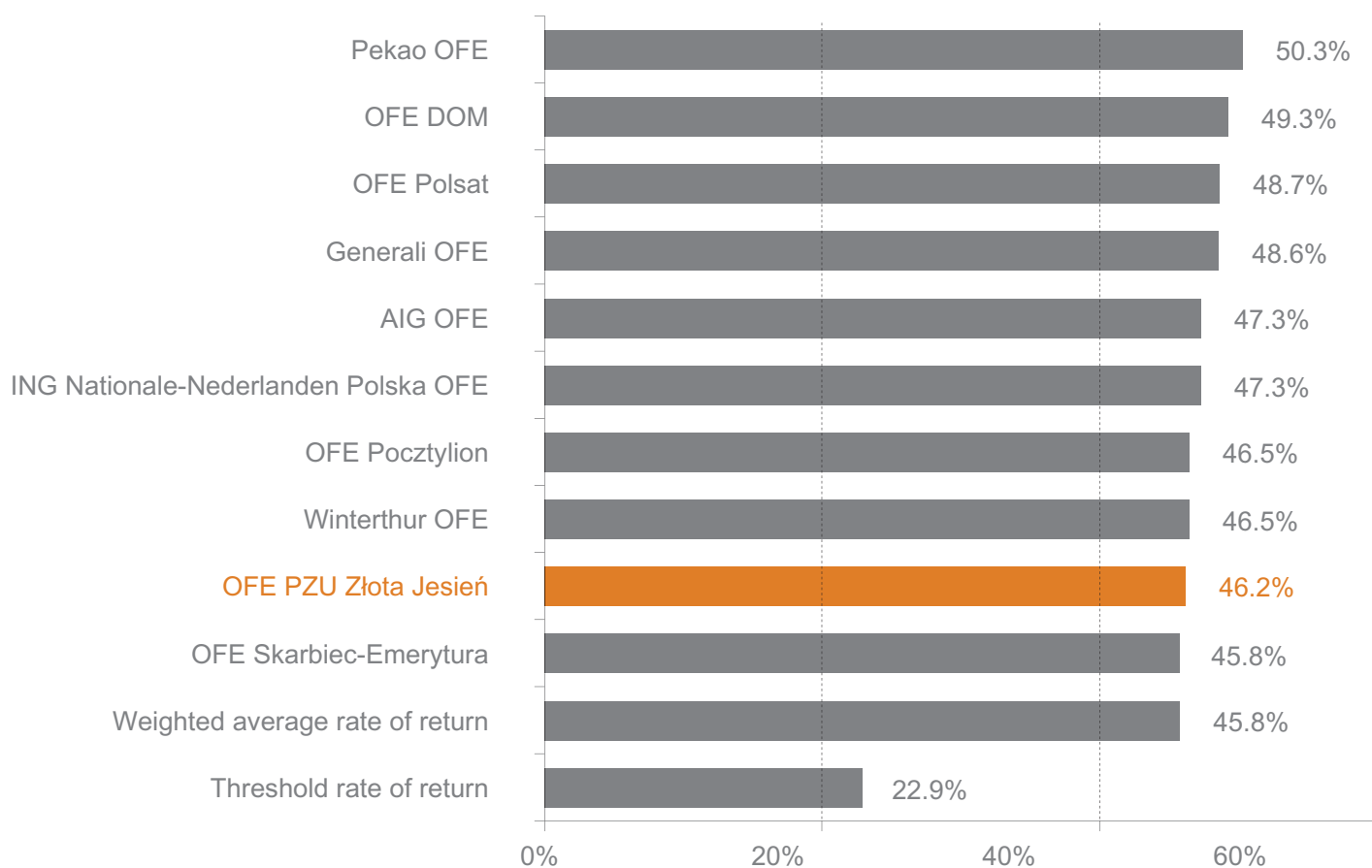
## Efficiency of investment activity and rate of return

At the end of the year, the weighted average of OFE accounting units was worth PLN 26.88, or 4% more than in 2005.

In September 2006, the PFSA calculated the three-year rate of return for all OFEs, putting the overall weighted average figure at 45.833%, which was approximately 7 points less than the year before. All funds exceeded the required minimum rate of return (22.917%) and the spread between the best and worst performing funds was close to 11 percentage points.

Top OFEs in terms of the three-year rate of return during the period from 30 September 2003 to 29 September 2006 (%)

Source: The PFSA



## Financial results

The total net profit of all open pension funds amounted to PLN 590.4 billion, or PLN 131.3 million (29%) more than the year before. A clear majority of the companies closed the year showing profits.

### 4.4.3 The investment fund market

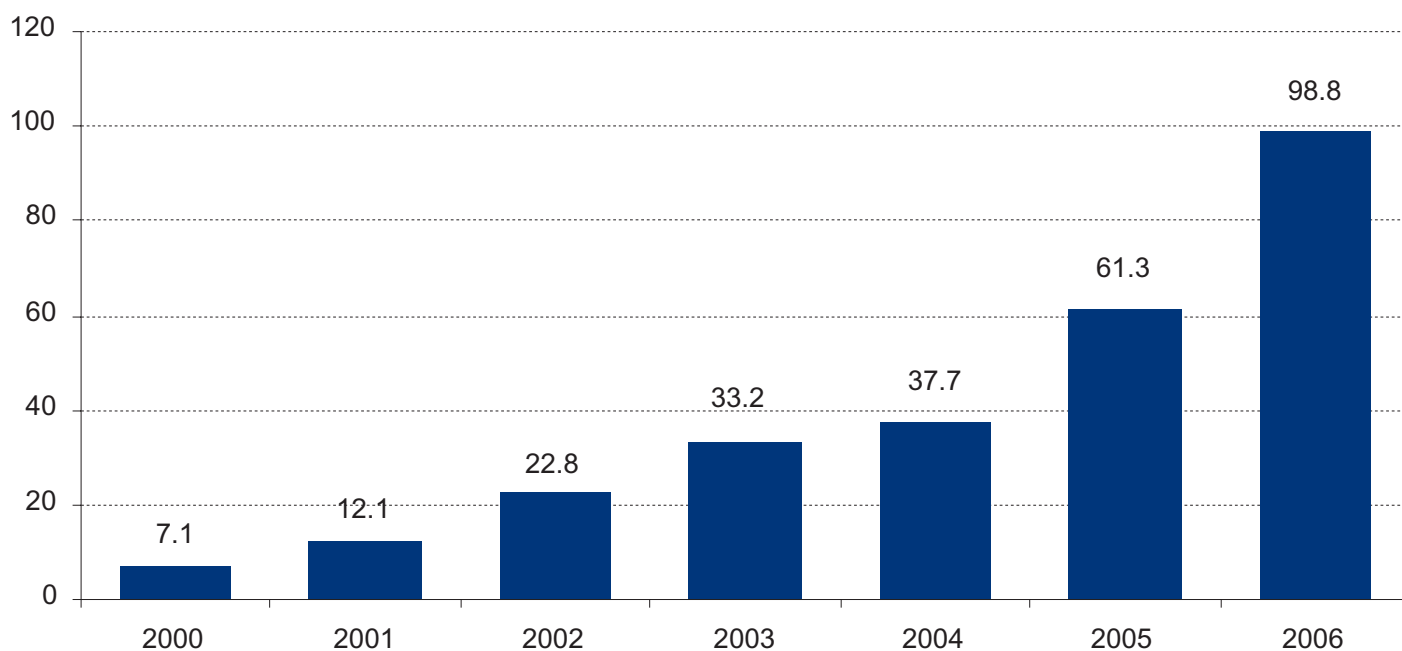
#### Investment fund companies and their assets

At the end of 2006, there were 26 actively operating investment fund companies (TFIs) on the Polish market, managing 241 investment funds. During the year, the PFSA granted permits to three new TFIs.

**This was yet another year of dynamic growth for investment funds, boosting assets to ca. PLN 99 billion, or up 61% year-on-year.**

Net assets managed by investment funds in Poland, 2000–2006 (in PLN billions)

Source: The PFSA

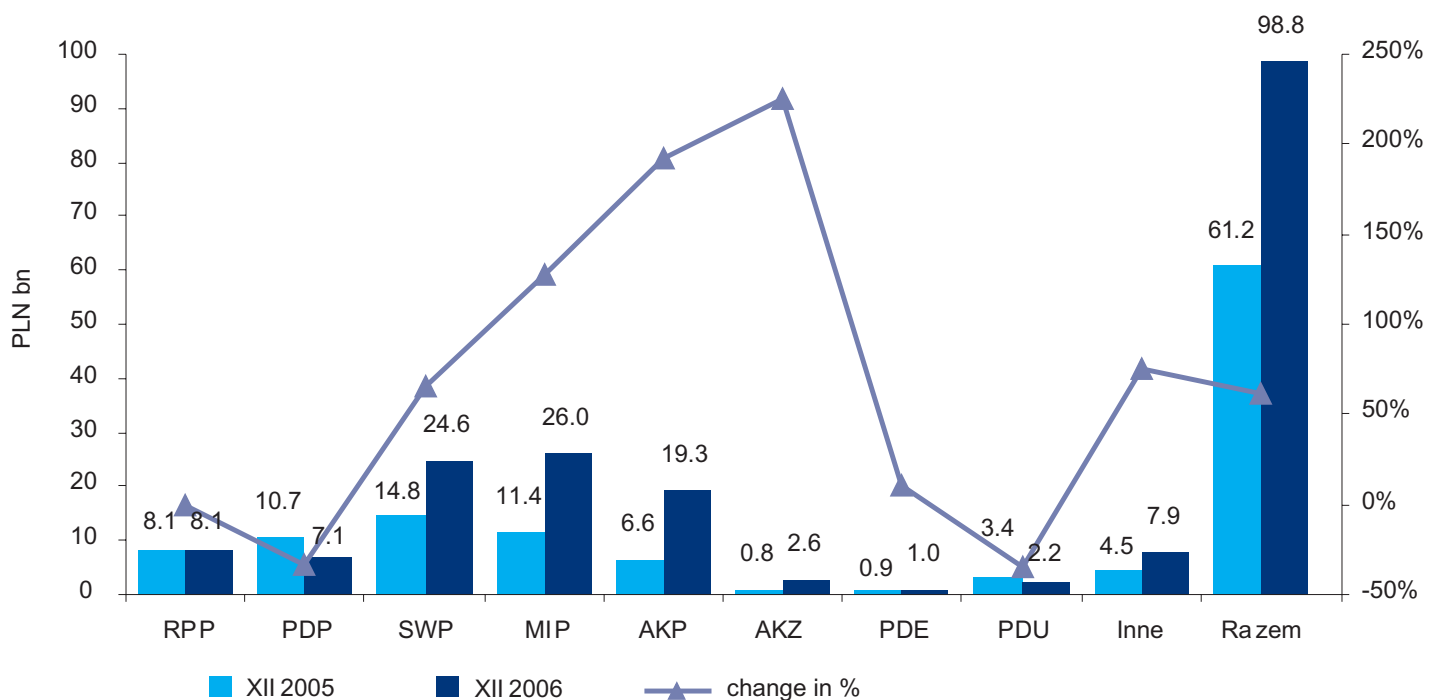


Investment funds' growth rates varied from segment to segment in 2006. Analysis of the growth rates shows that in 2006, the groups defined by similar investing policies were led by foreign equity funds (AKZ). However, despite tripling their assets, they still continued to be one of the smallest groups of funds on the Polish market. Second place went to the Polish equity funds (AKP), which also nearly tripled their assets, benefiting from the opportunities afforded by

an excellent year on the Warsaw Stock Exchange (the WIG broad-market index rose close to 42%). At the end of the year, Polish equity funds were managing one in every five zlotys invested on the investment fund market, thus becoming the third largest group of funds in Poland. The mixed funds (MIP) came third in terms of growth rate, after seeing their assets double in 2006.

### Polish investment fund market development in 2006

Source: The PFSA



Key: RPP – money-market funds; PDP- Polish debt securities funds; SWP – stable growth funds; MIP– mixed funds with half assets in domestic stocks on average; AKP – Polish equity funds; AKZ – foreign equity funds; PDE – Euro debt funds; PDU –USD debt funds.



#### Investment funds results

In 2006, investment funds increased their incomes from investments to PLN 3.2 billion, or by 45%, as compared to 2005. Their costs nearly doubled to PLN 2.3 billion. The resulting net income generated on investments amounted to PLN 832.4 million (down 11.3% vs. 2005). The funds also generated ca. PLN 2 billion in profit on investments sold (up by 65%) and PLN 8.4 billion profit on placement pricing (up by 176.7%). As a result, the funds generated PLN 11.2 billion of operating profit, as compared to PLN 5.2 billion in 2005.

#### 4.5 Major events impacting the PZU Group's operations and performance in 2006

In 2006, the PZU Group pursued a number of strategic initiatives to integrate and reorganize its distribution channels in order to improve customer service quality. These initiatives included the development of a common model of agency network management to help agents adapt to sell life and property and casualty products and increase the role of field branches in sales, while reducing it in sales processing and

operations. Very fast growth was reported by the "contact centre" sales channels, where customers were able to receive comprehensive information about the Group's products, purchase travel insurance (in a single telephone call) and make an appointment with an agent to get a full product offer.



The number of factors impacting the operations of the PZU Group companies included:

- **dynamic growth of the domestic insurance market well above the GDP growth rate** (21% vs. 6.1% GDP growth rate), especially the investment-linked life insurance market (up by 38%) contributed to the PZU Group's sales growth resulting in a considerable upswing in the premium increase compared to figures of 2005, in particular at PZU Życie SA,
- **strong cooperation between insurers and banks gave a competitive edge to players with capital links with banks.** Without such links, PZU Życie SA found its position on the bancassurance market considerably undermined and negotiating insurance deals harder. In the bancassurance market, there was **a fast growth of investment products** linked to bank deposits and investment funds, as well as to loans, especially mortgages,
- **growth on the financial insurance market** helped by the economic upturn, mortgage boom and the growing absorption of the EU funds (contributing to higher investments in Poland) stimulated product offer expansion at PZU SA, with mortgage loan insurance, insurance for non-own equity contributions, insurance guarantees and domestic and export trade credit. Altogether, this helped PZU SA generate triple-digit growth in written premiums from financial insurance and boosted its market share to more than 10%,
- **the continued process of diminishing market shares of the top players** in favour of smaller companies conducting aggressive acquisition activities to gain market share,
- **a refocus of product strategy and change in premium calculation for car-dealer customers** to maintain market position in the new car segment and win more careful drivers, and, as a consequence, bring this portfolio's profitability to an adequate level,
- **revitalization of the agency network and the PZU Group's agency servicing model:**
  - completion of efforts aimed at improving the efficiency of the Group's sales process and customer servicing, including "micro" sales reform aimed at strengthening sale structures and separating sales and back-office operations, as well as centralization of the IT system involving data from several product systems being integrated into a single system, which will ensure efficient customer servicing regardless of where a contract is concluded, using access to the customer's history,
  - completed implementation of the "PZU TeleAssistance" service and handling of vehicle claims by Mobile Experts as a vehicle claim submission process,
  - completion of these projects provides a starting point for further efforts to improve the quality of products and customer service,
- **centralization of PZU SA IT systems**, a platform for the centralization of business processes resulting in improved effectiveness of software development, operating security; this also marks the beginning of work aimed at improving the quality and availability of operating data.



#### 4.6 Factors which may have an impact on the PZU Group's operations in 2007

The two principal companies, PZU SA and PZU Życie SA, will remain crucial for the Group's competitive advantage as well as for its revenue and income generation. Typically for emerging markets, the Polish insurance market, and the life insurance market in particular, have displayed sustainable potential for growth. There is increasing demand for insurance services, while the property insurance and health insurance segments are still underdeveloped. The PZU

Group is well positioned to actively participate in the growth of these markets.

In 2007, the PZU Group is following an efficient growth path with the support of a sales network that has already grown very strong and will continue to reduce its costs (in comparison to competitors) by continuing the Group's restructuring and modernization processes.

In 2007, the Group's performance may be affected mainly by:

- **growing competition across the insurance sector**, which restricts the written premium growth rate, whereas a strong economic upturn may lead to high competitive pressure from other insurers,
- **growing competition from new financial institutions** offering investment products, i.e. investment fund families that are beginning to win large numbers of customers in the Employee Pension Programmes (PPEs), which means that when choosing PPE some customers holding life policies drop the protective portion of the offer in exchange for a higher allocation to investment,
- **tougher monetary policy**, increasing the reference interest rates, as a result of ongoing inflationary pressure, affects short-term and, subsequently, long-term interest rates on the financial market,
- **a major slowdown on the stock market**, which would lower returns from investment activity after the sustained record-level performance in 2006,
- **a slowdown in motor insurance** (dominating in the PZU SA portfolio) in comparison to other groups of insurances, which might result in PZU SA's written premium growth falling below the entire property insurance growth rate,
- **potential legal and regulatory changes**, especially in insurance, accounting and tax activities, which may require important modifications to the current operating models of PZU Group members.



## 5. Structure and activity of the PZU Group

### 5.1 Structure

As of 31 December 2006, the PZU Group consisted of 25 entities incorporated as either joint stock or private limited liability companies.

Entities fully consolidated in the PZU Group's financial statements for 2006 included:

- Powszechny Zakład Ubezpieczeń SA (PZU SA), the parent company,
- Powszechny Zakład Ubezpieczeń na Życie SA (PZU Życie SA), a subsidiary,
- Powszechne Towarzystwo Emerytalne PZU SA (PTE PZU SA), a subsidiary,
- PZU Tower Sp. z o.o., a subsidiary,
- Centrum Informatyki PZU Group SA (CIG PZU SA), a subsidiary,
- OJSC IC PZU Ukraine, a subsidiary,
- UAB DK PZU Lietuva, a subsidiary.

Other PZU Group companies have been excluded from consolidation due to the fact that their financial data are insignificant in relation to the overall financial data of the PZU Group, according to the criteria set out in Article 4 items 1 and 4 of the Accounting Act of September 29, 1994 (Journal

of Laws No. 76/2002, item 694, as amended, hereinafter referred to as the "Accounting Act"). These companies are recognized in the consolidated financial statements at cost less impairment allowances.

The method outlined above was applied in reporting:

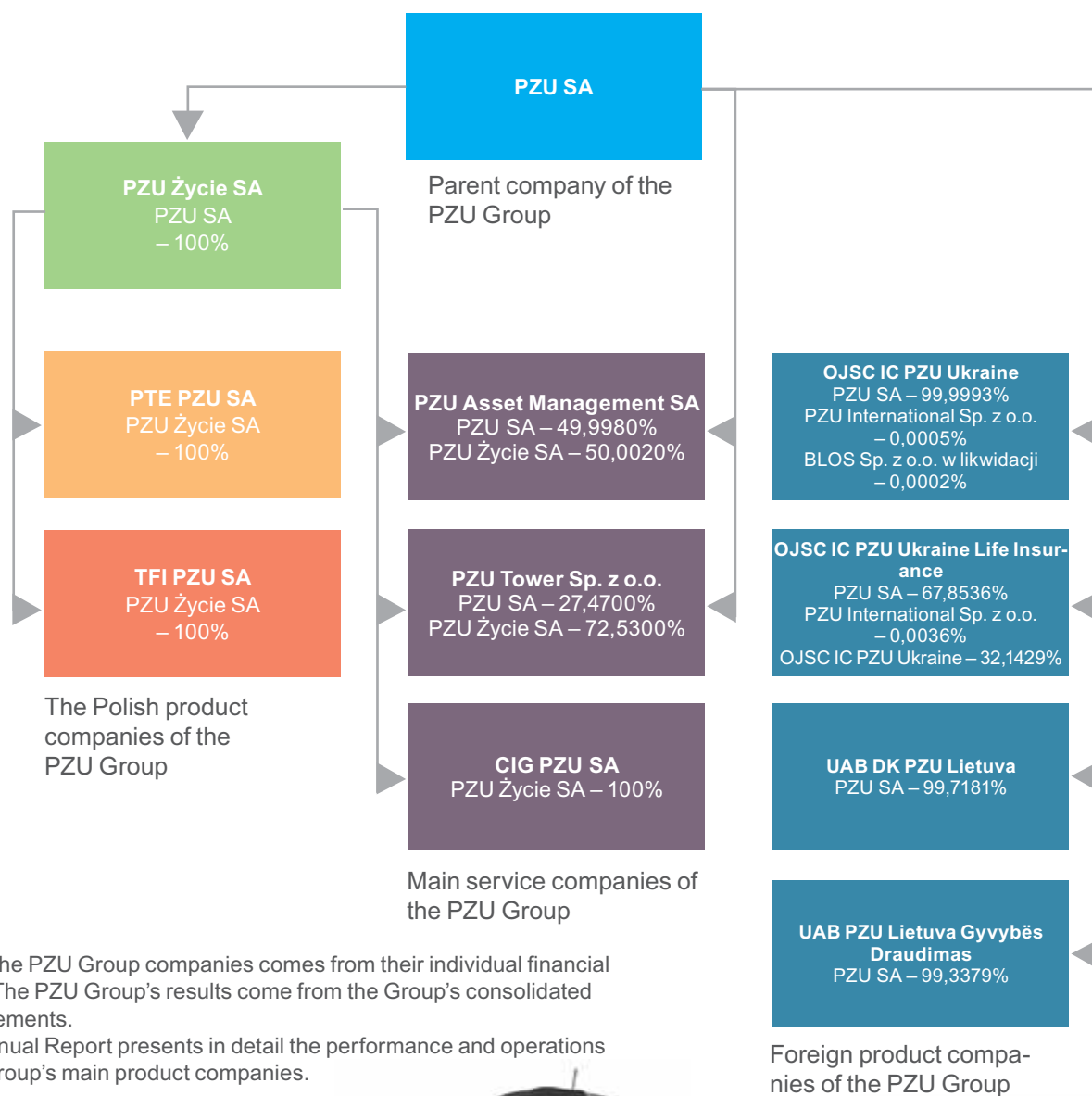
- Other subsidiaries valued at cost less impairment allowances:
  - Towarzystwo Funduszy Inwestycyjnych PZU SA (TFI PZU SA),
  - UAB PZU Lietuva Gyvybės Draudimas,
  - OJSC IC PZU Ukraine Life Insurance,
  - LLC SOS Services Ukraine,
  - Company with Additional Liability Inter-Risk Ukraine,
  - Międzyzakładowe Pracownicze Towarzystwo Emerytalne PZU SA (MPTE PZU SA),
  - PZU Asset Management SA,
  - PZU International Sp. z o.o.,
  - SYTA Development Sp. z o.o. w likwidacji,
  - Sigma Investments Sp. z o.o.,
  - Biuro Likwidacji i Obsługi Szkód Sp. z o.o.,
  - Krakowska Fabryka Armatur SA,
  - ICH Center SA,
- Other associates evaluated at cost less impairment allowances:
  - Kolej Gondolowa Jaworzyna Krynicka SA,
  - Nadwiślańska Agencja Ubezpieczeniowa SA,
  - Polskie Towarzystwo Reasekuracji SA,
  - PPW Uniprom SA w upadłości,
  - VIS-Inwestycje SA.





## The PZU Group structure as of 31 December 2006

Source: The PZU Group



The data on the PZU Group companies comes from their individual financial statements. The PZU Group's results come from the Group's consolidated financial statements.

The 2006 Annual Report presents in detail the performance and operations of the PZU Group's main product companies.



## 5.2 Principal business entities – scope of operations

The PZU Group offers a comprehensive insurance service with its companies active in life insurance, property and casualty insurance, as well as managing customers' assets through an open pension fund and a collection of investment funds.

### Powszechny Zakład Ubezpieczeń SA

PZU SA is the parent company of the PZU Group. The company is active in **property and casualty insurance**. It was established as a public company on 23 December 1991 when its predecessor, state owned enterprise Państwowy Zakład Ubezpieczeń, was turned into a commercial company (pursuant to the Insurance Activity Act of 28 July 1990, uniform text, Journal of Laws of 1996, No. 11 item 62 as amended).

### Powszechny Zakład Ubezpieczeń na Życie SA

PZU Życie SA is active in **life insurance**. The company also offers **marriage insurance, annuities, accident insurance and investment-linked insurance policies, both for individuals and groups**. PZU Życie SA is a subsidiary of PZU SA. The company started its operations in 1991 after its life-insurance portfolio was spun off from the then state owned Państwowy Zakład Ubezpieczeń.

### Powszechne Towarzystwo Emerytalne PZU SA

PTE PZU SA is the company managing the **Otwarty Fundusz Emerytalny PZU "Złota Jesień"** ("Golden Autumn" open pension fund) operating within the framework of the **2nd pillar of the Polish pension system**. PTE PZU SA was established in 1998 as a subsidiary of PZU Życie SA.

### Towarzystwo Funduszy Inwestycyjnych PZU SA

TFI PZU SA manages a group of **nine investment funds** with various investment strategies. TFI PZU SA offers investment products and services to individual and institutional customers, as well as savings plans in the **framework of the 3rd pillar of the Polish pension system**. The company was established in 1999 as a subsidiary of PZU Życie SA.



## PZU Asset Management SA

PZU Asset Management SA was incorporated into the PZU Group in 2001. It focuses on **the management of securities portfolio for its customers**. In 2005, PZU Asset Management SA took over the management of some asset portfolios and funds of the PZU Group.

## PZU Group SA IT Centre (Centrum Informatyki Grupy PZU SA)

CIG PZU SA was established to provide **auxiliary services in the handling of insurance and pension funds**. It keeps registers, accounts and settlements of investment and pension funds. The company also offers IT services (such as consultations on hardware and software, data analysis, database building and data processing), call-centre services, mass printing, document processing and storage, as well as mailing. The company joined the PZU Group in June 1998.

## PZU Tower Sp. z o.o.

PZU Tower Sp. z o.o. is the Group's SPV, established in August 1998 to **operate on the property market, to develop and manage property and rent office space**.

## UAB DK PZU Lietuva and UAB PZU Lietuva Gyvybės Draudimas

On the **Lithuanian market**, PZU offers its **life and property and casualty insurance** services under the PZU Lietuva brand. The PZU Group has been present in Lithuania since February 2002. The Lithuanian companies are subsidiaries of PZU SA.

## OJSC IC PZU Ukraine and OJSC IC PZU Ukraine Life Insurance

In February 2005, the PZU Group also entered **the Ukrainian market** with its companies offering both **life and property and casualty insurance**. The two companies are subsidiaries of PZU SA.



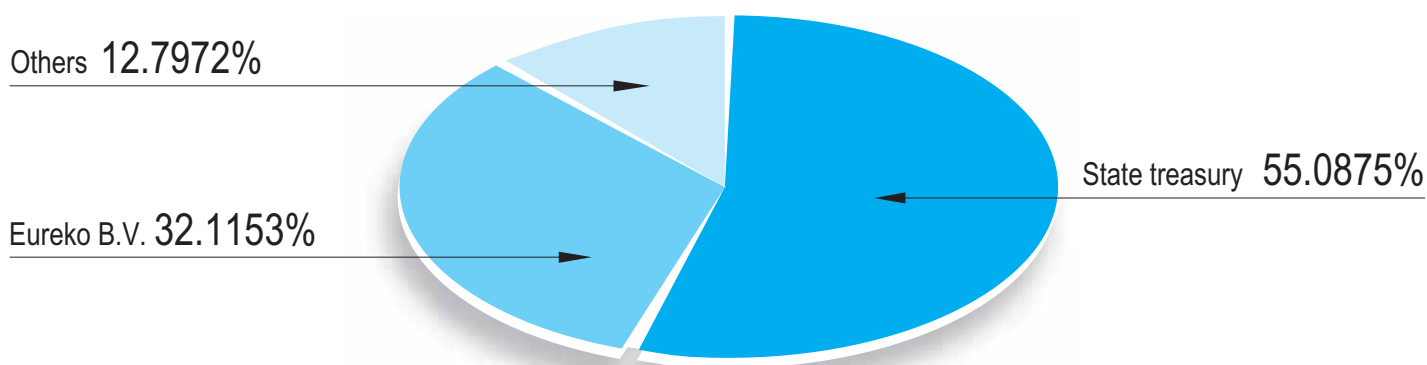
## 5.3. Shareholders

### Ownership structure

PZU SA has PLN 86,352,300 of share capital divided into 86,352,300 registered shares of the A and B series with a nominal value of PLN 1 each.

### PZU SA ownership structure as of 31 December 2006

Source: PZU SA Book of Shareholders



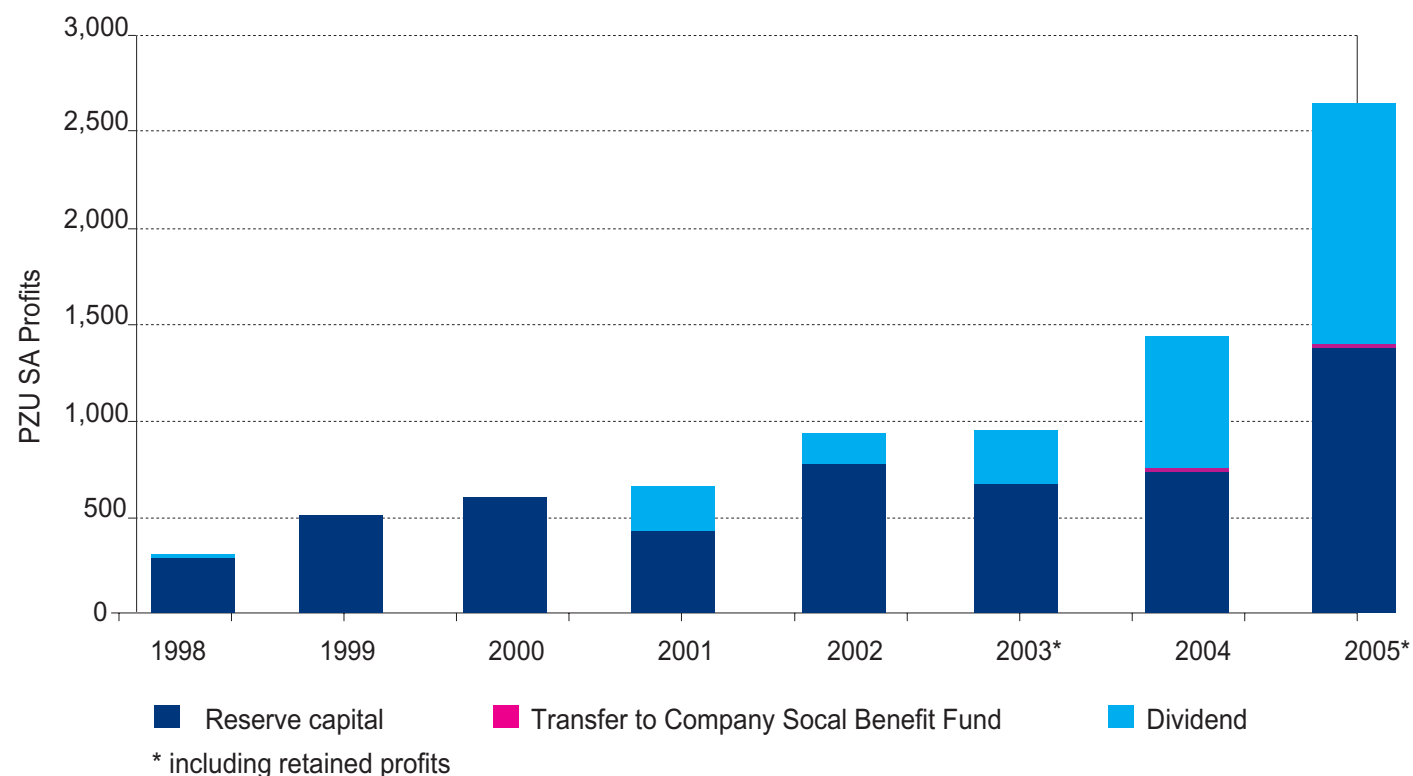
### Appropriation of profit

PZU SA outlined its dividend policy in the Group Strategy 2006–2010 adopted by the PZU SA Management Board Resolution No. UZ/531/2005 dated 17 November 2005, subsequently approved by the PZU SA Supervisory Board Resolution No. URN/28/2005 dated 29 November 2005. On 12 July 2006, the PZU SA Annual General Meeting adopted a resolution dividing the company's retained profits from previous periods and net profits for 2005. The gross dividend was set at PLN 15.60 per share and a total of PLN 1,347 million was paid out. The dividend payment ratio was 50%.



## PZU SA net profit appropriation 1998–2005 (PLN m)

Source: PZU SA



## Investor relations

In 2006, the PZU SA Management Board continued to pursue its existing investor relations policy. The company provides reliable and efficient information about its activities, products and intentions to ensure that all capital market players, shareholders and analysts have the best possible conditions to comprehensively evaluate the company's situation and take relevant decisions.

The PZU SA publishes financial performance data on Group members on a quarterly basis, meeting with analysts and other financial market participants and organizing conferences to present its operations and results. Up-to-date information about members of the PZU Group is also available on the Group's website.



## 5.4 The directing bodies of the PZU Group companies

### The directing bodies of the PZU Group major companies

#### PZU SA Management Board

Jaromir Netzel	President (since 8 June 2006)
Piotr Kowalczewski	Vice-President (suspended in his responsibilities since 1 November 2006)
Jolanta Strzelecka	Board Member (since 26 June 2006)
Mirosław Panek	Board Member (since 30 August 2006)
Joyce Deriga	Board Member (since 17 July 2006, suspended in her responsibilities from 1 November 2006)

Cezary Stypułkowski	President (until 2 June 2006)
Mirosław Szturmowicz	Board Member (until 16 August 2006)
Ryszard Bociong	Board Member (until 26 June 2006)
Witold Walkowiak	Board Member (until 14 July 2006)

#### PZU SA Supervisory Board

Aleksander Chłopecki	Chairperson (until 27 October 2006)
Agata Rowińska	Deputy Chairperson
Ernst Jansen	Deputy Chairperson
Maciej Bednarkiewicz	Secretary
Beata Kozłowska-Chyła	Supervisory Board Member (since 26 April 2006)
Marcin Majeranowski	Supervisory Board Member (since 21 June 2006)
Eryk Zbigniew Pyra	Supervisory Board Member (since 21 June 2006)
Gerard van Olphen	Supervisory Board Member
Michał Nastula	Supervisory Board Member (since 10 August 2006)

Kick van der Pol	Supervisory Board Member (until 10 August 2006)
Anita Ryng	Supervisory Board Member (until 26 April 2006)
Wojciech Dąbrowski	Supervisory Board Member (until 26 April 2006)
Paweł Antosiewicz	Supervisory Board Member (until 7 February 2006)

#### PZU Życie SA Management Board

Jerzy Kochański	President
Henryka Rupik	Vice-President (since 20 June 2006)
Wojciech Grzybowski	Vice-President (since 20 June 2006)
Krzysztof Rosiński	Vice-President (until 20 June 2006)
Magdalena Nawłoka	Vice-President (from 7 July 2006 until 31 October 2006)
Roelfina Banus	Vice-President (until 31 October 2006)

#### PZU Życie SA Supervisory Board

Eugeniusz Kowalewski	Chairperson (since 19 June 2006)
Joyce Deriga	Deputy Chairperson
Jolanta Strzelecka	Secretary (since 19 June 2006)
Krystyna Gawlikowska-Hueckel	Supervisory Board Member (since 19 June 2006)
Janusz Olędzki	Supervisory Board Member (since 19 June 2006)
Ane Ate Sijsma	Supervisory Board Member

Andrzej Wieczorkiewicz	Chairperson (until 19 June 2006)
Margriet Tiemstra	Supervisory Board Member (from 19 June 2006 until 22 September 2006)
Witold M. Góralski	Secretary (until 19 June 2006)
Reinoud C.J. van den Broek	Supervisory Board Member (until 19 June 2006)
Bolesław Samoliński	Supervisory Board Member (until 19 June 2006)
Jerzy Tomaszewski	Supervisory Board Member (until 19 June 2006)



## PTE PZU SA Management Board

Piotr Rzeźniczak	President (since 11 December 2006)
Stanisław Rataj	Vice-President
Andrzej Sołdek	Vice-President

Jakub Tropiło	President (until 31 July 2006)
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## PTE PZU SA Supervisory Board

Ludwik Florek	Chairperson (since 16 November 2006; between 30 May 2006 and 15 November 2006 Member of the Supervisory Board)
Jerzy Kochański	Deputy Chairperson
Piotr Kowalczewski	Supervisory Board Member
Krystyna Dziworska	Supervisory Board Member (since 20 December 2006)
Marek Kalinowski	Supervisory Board Member (since 6 December 2006)
Jerzy Lipski	Secretary (since 18 December 2006, between 6 December 2006 and 17 December 2006 Member of the Supervisory Board)

Wiktor Askanas	Chairperson (until 26 October 2006)
Ewa Frątczak	Secretary (until 26 October 2006)
Frederik Hoogerbrug	Supervisory Board Member (until 26 October 2006)
Władysław Jaworski	Supervisory Board Member (until 21 April 2006)
Jerzy Zdrzałka	Supervisory Board Member (until 26 October 2006)

## Management Board TFI PZU SA

Dariusz Jesiotr	President (since 8 November 2006)
Cezary Burzyński	Vice-President (since 8 November 2006, between 1 January 2006 and 7 November 2006 President)
Maciej Rapkiewicz	Board Member (since 8 November 2006)

Michał Nastula	Vice-President (until 23 May 2006)
Paulina Pietkiewicz	Vice-President (from 24 May 2006 until 7 November 2006)
Marek Żytniewski	Board Member (until 7 November 2006)

## Supervisory Board TFI PZU SA

Henryka Rupik	Chairperson (since 26 October 2006)
Aldona Wojtczak	Deputy Chairperson (since 8 November 2006, between 26 October 2006 and 7 November 2006 Member of the Supervisory Board)
Jacek Dmowski	Supervisory Board Member (since 26 October 2006)
Jerzy Glanc	Supervisory Board Member (since 26 October 2006)
Tomasz Rynarzewski	Supervisory Board Member (since 26 October 2006)

Krzysztof Rosiński	Chairperson (until 30 September 2006)
Frederik Hoogerbrug	Deputy Chairperson (until 25 October 2006)
Paulina Pietkiewicz	Supervisory Board Member (until 22 May 2006)
Paweł Durjasz	Supervisory Board Member (until 25 October 2006)
Piotr Osiecki	Supervisory Board Member (until 25 October 2006)
Roelfina Banus	Supervisory Board Member (from 23 May 2006 until 25 October 2006)





## 5.5 The PZU Group portfolio of products and services

PZU Group provides the broadest insurance offer on the Polish market. There are nearly 200 insurance products for individual customers, small and medium enterprises and

corporate customers. Alongside property and casualty insurance and life insurance, the PZU Group offers a number of attractive pension and investment products.

### 5.5.1 Property and casualty insurance – PZU SA

In 2006, PZU SA continued its efforts to develop clear customer segmentation and development of offers for newly defined groups. The company is now offering its products to three main segments: the mass customer segment, SMEs and corporate customers. PZU SA has products spanning all of the 18 statutory insurance classes defined by law and including: motor, property, agricultural, general third party liability, accident and health, tourist and financial insurance.

#### The Individual customer offer

In 2006, PZU SA offered more than 80 products to this segment, but was working to add new products and solutions meeting the needs of this segment.

Motor insurance, including obligatory motor third party liability insurance, remains the main product PZU SA offers to individuals. On 1 January 2006, the company introduced new premium rates for this group, featuring additional risk factors included in calculation of the premium, also covering the brand and model of car. This move brought the insurance products up to modern standards and made them more attractive, especially to customers with no history of claims.

One of the most important changes in the motor insurance offer was the addition, in late 2005, of a free Assistance Polska insurance (part of the Mini plan) to the obligatory motor third party liability insurance. The additional package covers the hauling of both third party's and holder's cars from the site of the accident. This unique product combines obligatory insurance with an additional practical benefit.

In 2006, PZU added new products to its property insurance offer for individuals, including new third party insurance

(business and property-related general third party liability for mass customers and professional indemnity insurance). The company also developed third party liability products targeted at sports and education segment customers and, finally, introduced updated insurance products on the market.

Within personal and accident insurance, PZU modified its general terms and conditions of accident policies for children, young people and the staff of schools and other facilities, as well as for children and youth camp participants. We also introduced an innovative insurance against adverse consequences of surgical operations.

Agriculture insurance products saw some significant modifications following the introduction of a new law on subsidies for crops and farm animals insurance. On 21 July 2006, we started offering two new products, subsidized crops insurance and subsidized farm animals insurance. We also introduced significant changes to the insurance on farm movables, including options for insuring farm animals and equipment against burglary and theft.



## SME offer

In 2006, PZU SA continued building its offer for small and medium enterprises. The company defined the target segment and its internal composition. The upper value of a SME was set at PLN ten million and the segment was further broken down into three sub-segments depending on company size and insurance needs. Each of the sub-segments received a targeted insurance package: *PZU Partner*, *PZU Doradca* i *PZU Ekspert*.

With its new *PZU Hotel* product, PZU SA embarked on the path towards building a portfolio of sector-specific packages targeted at the most promising customers. It provides comprehensive coverage and is tailored to the needs of hotel businesses.

The product-package philosophy for the new SME insurance offer helps to tailor it to customer needs and expectations.

Another approach to the development of the PZU SA's SME offer is modification of existing products to the needs of this segment. This is dictated by a wide variety of customer expectations in terms of coverage, service and risk assessment. PZU SA has already made this kind of modification to motor insurance and various third party liability products.



## Corporate offer

2006 was a breakthrough year for corporate motor insurance at PZU SA. As of 1 January 2006, the company introduced its new general terms and conditions and premium rates on motor owner damage insurance and obligatory motor third party liability insurance for corporate customers. The changes were intended to introduce solutions tailored to large companies. The new terms and conditions were also introduced for leased car insurance, thus bringing such terms and conditions for all potential leasing partners into a uniform offer.

As part of the company's corporate motor insurance offer, another important project was launched and executed in 2006; it consisted of initiating a series of meetings under the "Fleet Safety" programme, intended to promote safe driving.

The PZU Group's offer dedicated to corporate customers goes far beyond motor insurance, with a range of more than 30 products, such as property, loss of profits, general and professional third party liability, engineering, cargo and cas-co insurance.

In this group of products, the company modified the general terms and conditions of its property insurance (fire and other acts of God, all-risk insurance) and corporate loss of profit insurance. These products, together with the general terms and conditions for corporate obligatory motor third party liability insurance introduced the year before, constitute the core of PZU SA's constantly updated corporate customer offer.

In 2006, PZU SA reported dynamic growth in financial insurance, including insurance guarantees. The company offered this type of products to both SMEs and corporate customers. PZU SA was the first insurer on the market to offer co-operation with a bank in granting payment for a construction works bond.

2006 was also a landmark year for insurance linked to banking products for retail customers. PZU SA considerably strengthened its position as a provider of mortgage credit/loan insurance prior to formal mortgage registration. The company reported strong sales growth after the three general insurance contracts were concluded in 2005 with the largest Polish bank, PKO BPS SA. In 2006, the company continued these initiatives with another three banking insurance contracts concluded with Bank Gospodarki Żywnościowej SA (holding contracts for: i) pre-formal mortgage registration credit/loan insurance; ii) mortgage credit/loan insurance to the amount of leveraged own contribution; and iii) pre-formal mortgage registration for commercial mortgage credit/loan insurance).

PZU SA also offers trade credit insurance products, including newly introduced export and domestic trade credit insurance for SMEs.



## 5.5.2 Life insurance – PZU Życie SA

PZU Życie SA offers more than 60 life insurance products and packages, both cover insurance products and unit-linked products (including main covers and riders). The company has offers for individuals and group customers with products in all 5 statutory regulated insurance classes.

In 2006, the company continued its activities intended to consolidate its position on the corporate market, the key segment due to its profitability. As part of implementation of the Central Database of Institutional Customers project, detailed customer identification was performed, allowing – among other things – the introduction of clearly defined customer segmentation.

In view of the growth in the small and medium enterprises segment, the company prepared a reviewed offer targeted specifically to companies from this segment. The new offer includes life coverage for the insured and the co-insured, with the possibility of coverage extension by adding health and medical coverage.

### Group insurance

The core of PZU Życie SA's activity is group cover insurance products with regular premiums. This type of insurance is aimed primarily at customers who value a broad range of coverage, such as life insurance supplemented by accident, disease and family riders. These products, known as "P" group products (*Group life insurance "P" and Group employee insurance "P Plus"*), and their individual continuation constitute the best selling products of PZU Życie SA.

The offer of these core products is further extended by rider products that guarantee the benefit payment in the case of various health and life events.

PZU Życie SA also offers group unit-linked insurance products. The most popular of these is the group life insurance with a capital fund known as *Pogodna Przyszłość* ("Bright Future"), which is a form of an Employee Pension Programme.

In 2006, the company developed new comprehensive offers for small and medium enterprises (*PZU Ochrona Plus*, "Protection Plus", *PZU Ochrona Maksimum*, "Protection Max").

These include a package with a range of basic coverage options, which may be expanded by adding medical and health rider packages. The product offer for existing customers was expanded, with group rider products, such as the assistance-type *Doraźna Ochrona Medyczna* ("Emergency Health Care"), a group rider in the case of hospital treatment Plus and a group rider for specialized hospital treatment. The latter two riders are an extension of the hospital treatment coverage, very popular among group product customers. The existing medical rider *Opieka Medyczna* ("Health Care") was redeveloped. The offer was further extended by adding a group life and health coverage known as *Opieka Medyczna S* ("Health Care S") and a coverage programme for farmers and their families *Przezorny Gospodarz* ("Prudent Farmer"). The dynamic growth of group health coverage in 2006 resulted in increased attractiveness of PZU Życie SA's cover insurance product offer.



## Individually continued insurance

In 2006, the company took several initiatives intended to develop the individual customer segment, continuing group insurance and to boosting the number of customers taking out individually continued policies.

To increase sales of the *NW Plus* rider to continued insurance policies, a mass mailing campaign was staged featuring the offer. This helped to reach sales number of 461,000 new *NW Plus* riders.

## Individual insurance

PZU Życie SA offers cover and unit-linked insurance products for individual customers.

The cover products offered by the company include *Optima*, *Credo* (expired in 2006) and *Futura* – endowment insurance, Maximum whole life insurance and *Terminowe ubezpieczenie PZU* term life insurance.

For individuals, PZU has a number of unit-linked products, including Indywidualny Program Inwestycyjny *Strefa Zysku* (“*Strefa Zysku Individual Investment Programme*”) and *Prestiż Gwarancja* (“*Guarantee Prestige*”), which combine potentially high and unlimited returns on investment with a capital guarantee.

IPI *Strefa Zysku* is a unit-linked product (developed in cooperation with TFI PZU SA), which provides a comprehensive investment offer based on 32 investment funds (including a

In addition, works have been started to introduce a new rider covering the hospital treatment as a result of accident. At first, the rider is to be sold by mail.

guaranteed fund) and is characterised by high level of flexibility, dynamic management of investment and an investment bonus.

In 2006, the company developed rider products to complement individual investment products. A new rider product was implemented, covering death of the insured caused by a traffic accident; it was offered to existing customers in the form of mail sales.

Among health products, a thorough redevelopment was carried out on the life and health insurance *Opieka Medyczna* (“*Health Care*”).



### 5.5.3 Bancassurance – PZU SA and PZU Życie SA

The PZU Group offers a wide range of bancassurance products distributed through bank channels. Both life and property and casualty products are offered closely linked to banking products, such as credit/loans, bank accounts, payment and credit cards and investment products (including unit-linked and structured products) addressed to a large group of bank customers.

In 2006, the PZU Group focused on expanding its relationships with its existing partners. The customer portfolio of PZU Group companies was also further extended to include other banks, e.g. Bank Gospodarki Żywnościowej SA, which resulted in the introduction of a life insurance with insurance capital fund, known as *Kapitał Plus* (“*Capital Plus*”), and a number of property and casualty insurance products.

The variety of the PZU Group's products targeted to specific customers contributed to expanding the product offers of the Group's banking partners.

The PZU Group cooperated with PKO BP SA in developing a special product with an insurance capital fund called *Program Inwestycyjno-Ubezpieczeniowy* (“*Investment and Insurance Programme*”), based on the investment profile of the bank's customers. The Group also continued to sell its regular cover products, both life and property, included in the offer from previous years.

A special offer, *Program Inwestycyjny Prestige* (“*Prestige Investment Programme*”), was developed in cooperation with Bank Millennium SA for its Prestige Bank Millennium SA customers. In 2006, there was a continued growing trend in written premiums from insurance products linked to mortgage credits/loans, as the latter proved to be very popular.

The product offer developed together with Deutsche Bank PBC proved to be a winner yet again. The PZU Group added an investment product offered in the form of insurance policy – *db Gwarancja*, the structure of which is based on the benefits of structured products.

In 2006, two new insurance products were introduced to the offer of Bank Ochrony Środowiska SA for personal bank account holders.





## 5.5.4 Pension insurances and products – PZU Życie SA, PTE PZU SA and TFI PZU SA

Among its products, the PZU Group also offers pension-related plans and products. Individual customers are offered Individual Pension Accounts (“IKE”) developed by PZU Życie SA and TFI PZU SA. In 2006, the PZU Group successfully built up its position as IKE market leader.

Individual customers are also able to participate in the offer of PTE PZU SA, manager of the open pension fund OFE PZU “Złota Jesień” (“Golden Autumn”). The fund is offered under the 2nd pillar of the Polish pension system, which is obligatory for all citizens born after 1968. OFE PZU “Złota Jesień” has members among people starting their first jobs (primary market) and members of other pension funds wishing to switch funds (secondary market).

The PZU Group offers also include pension programmes, such as Pogodna Jesień (“Bright Autumn”), and group life insurance with an insurance investment fund, Pogodna Przyszłość (“Bright Future”), in a form of an employee pension programme. Over several years these plans have enjoyed an established position on the product market, which has been accumulating and increasing customers’ funds. The PZU Group also offers employee pension programmes in the form of an agreement on investment fund premiums managed by TFI PZU SA.

## 5.5.5 Investment products – TFI PZU SA

Both individual and corporate customers of the PZU Group can profit from a broad range of investment products. TFI PZU SA offers nine different open investment funds with diverse portfolios on offer. In 2006, the fund management company enhanced its offer with two new funds: *PZU FIO Akcji Małych i Średnich Spółek*, (SME equities fund), and *PZU Specjalistyczny FIO Funduszy Zagranicznych* (a specialized foreign fund of funds). The latter has four sub-funds: PZU Subfundusz Stabilnego Wzrostu Zagraniczny (stable growth fund), PZU Subfundusz Zrównoważony Zagraniczny (balanced fund), PZU Subfundusz Akcji Zagraniczny (foreign equities fund), and PZU Subfundusz Wielu Klas Aktywów (multi-asset fund). The specialized foreign fund of funds is recommended to customers interested in active investments on global markets through the best foreign funds of various categories and seeking to optimise their tax returns at the same time.

Alongside investment funds, TFI PZU SA offers specialized investment programmes and Individual Pension Accounts for individual customers as well as Occupational Investment Plans and Employee Pension Programmes.





## 5.6 The market position of the PZU Group Companies

The PZU Group has a long record of leadership on the Polish insurance market. At the end of 2006, the Group's overall market share, measured by gross premiums written, amounted to 40.7%, or 3.7 points down from 2005.

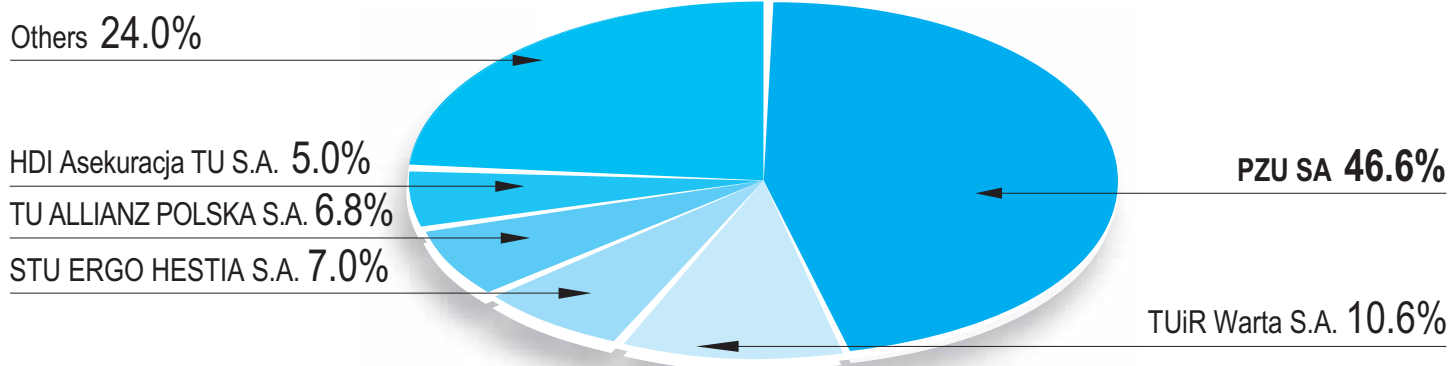
PZU SA leads the property and casualty insurance segment (Segment 2) with a 46.6% share of the market. While this represents a 2.1 point drop, caused by lower sales, mostly in the motor insurance, including Motor Own Damage and obligatory Motor Third Party Liability, the company reported very good sales growth in other insurance products, mainly bank loans, which resulted in a multiplying of its share of the market for this type of insurance.

In 2006, PZU Życie SA maintained its leading position on the life insurance market (Segment 1) and dominated in group insurance. Its share of the market at the end of 2006 was 36% after a 3.8 point drop from the 2005 figure. The company improved its position in the area of life individual insurance, with an 11.1% share (up by 2.2 points), as a result of excellent sales of investment-linked insurance products.

At the end of 2006, OFE PZU "Złota Jesień" was ranked third on the Polish open pension fund market both in terms of the number of members (a 15.3% market share) and assets under management (13.7% market share).

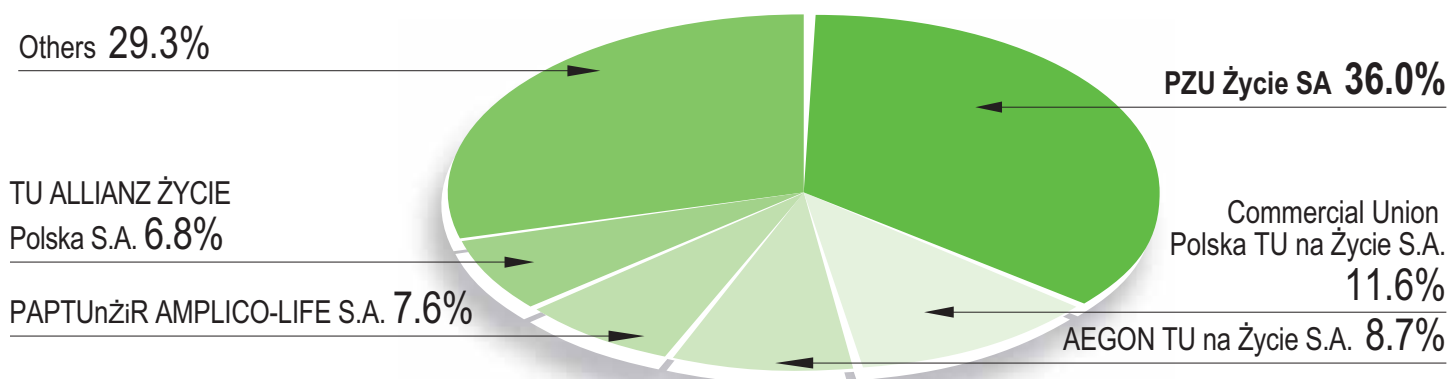
Market share of PZU SA in the property and casualty insurance market by gross premium written, (as of 31 December 2006)

Source: The PFSA



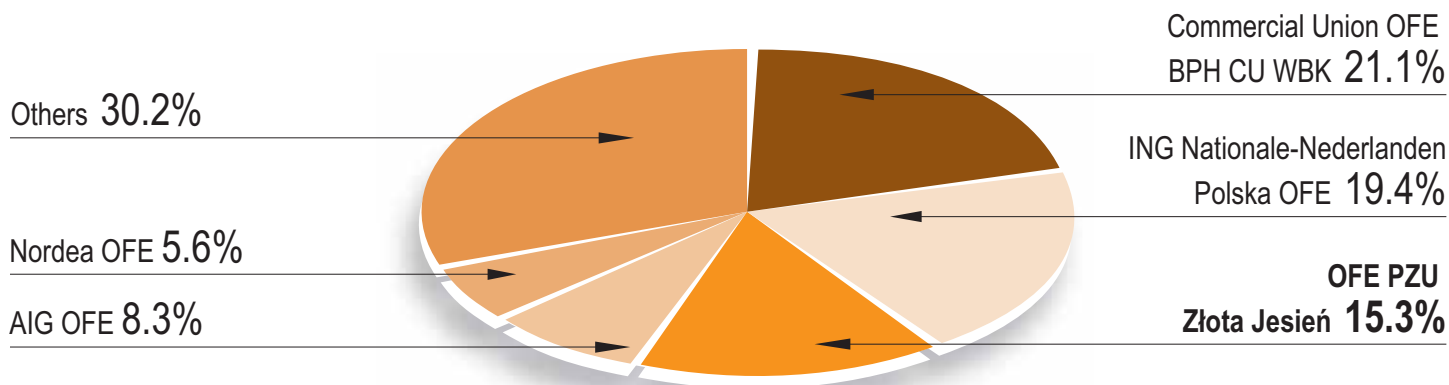
## Market share of PZU Życie SA in the life insurance market by gross premium written (as of 31 December 2006)

Source: The PFSA



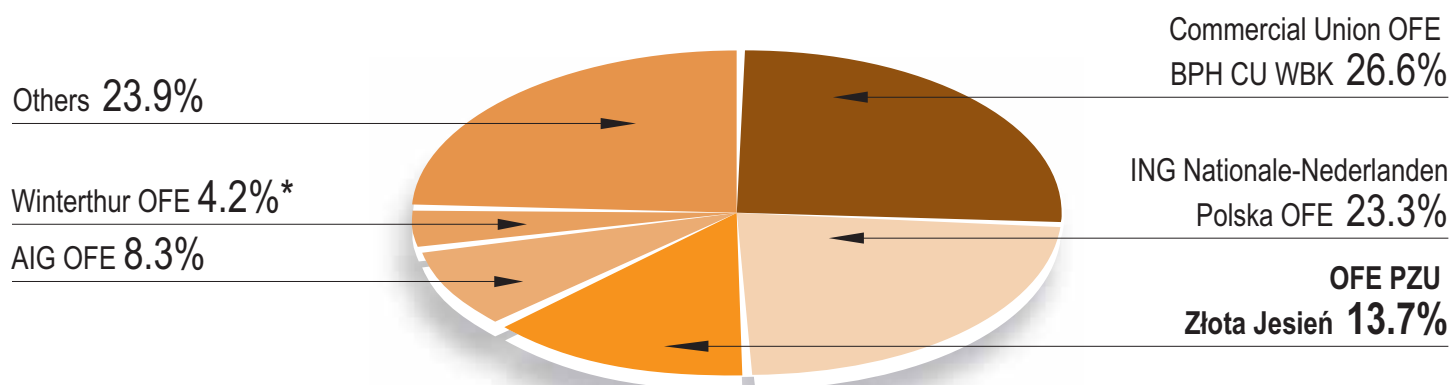
## Market share of OFE PZU "Złota Jesień" in the open pension fund market by number of members (as of 31 December 2006)

Source: The PFSA



## Market share of OFE PZU "Złota Jesień" in the open pension fund market by assets under management (as of 31 December 2006)

Source: KNF



\* Since 19.03.2007 Winterthur OFE changed its name to AXA OFE

### 5.7 Marketing and advertising

As in the previous year, in 2006 the PZU Group focused its advertising and promotion activities on direct support for its sales process.

The PZU Group centred its image promotion on two television campaigns. In November, the Group presented the completeness of its insurance and investment offer and highlighted the vast experience of its member companies in Polish economic and social conditions. The other campaign, in December, took the opportunity to bring the season's greetings to the Group's customers.

The PZU Group continued to develop its corporate website, [www.pzu.pl](http://www.pzu.pl). New features included on-line claims for corporate customers and a practice/placement application form on the "Career" tab for those seeking PZU job experience.

The PZU Corporate Communication and Marketing Office appointed an e-marketing team responsible for handling the placement of PZU SA and PZU Życie SA and their products in the electronic media.



## Promotion of property and casualty insurance

In the area of property and casualty insurance, PZU SA focused on promoting its motor insurance products with three media campaigns in 2006.

In January and February, the campaign promoted a system of discounts and rebates on the accompanying assistance service market and publicised its nationwide claims handling network called Sieć Naprawcza ("Repair Network"). From June to August, PZU SA ran a campaign to promote complete insurance packages of motor insurance with motor own damage, motor third-party liability and accident policies. Finally, at the end of the year, there was the "OC w PZU oswaja emOCje" ("Taming emotions with PZU") campaign for the obligatory motor third party liability insurance, accompanied by a highly popular on-line competition.

Other marketing campaigns in 2006 were timed during the peak tourist season to promote the Wojażer travel insurance and highlighting a telephone option to conclude contracts (*Telepolisa Wojażer*).

In the same year, PZU SA also conducted multidimensional promotional activities aiming to support sales of its products targeted at the SME segment. The activities included a number of sales conferences for SME customers and the "Wielka mała firma" ("Big Small Company") competition.

To support plans for dynamic growth of financial insurance products, PZU SA launched marketing activities principally aimed at building up awareness of product availability and benefits. Together with the Ministry of Regional Development, the Group arranged a series of nationwide conferences devoted to utilization of European aid under the pre-accession PHARE programme "Economic Cohesion – Human Resource Development" and under the New Financial Perspective 2007-2013.

Apart from nationwide campaigns, the company also conducted several smaller-scale advertising and promotion activities. These included local sales actions based on the agency network and promotions supporting individual product sales.



## Promotion of life insurance and other products

In October 2006, PZU Życie SA started offering its *Indywidualny Program Inwestycyjny Strefa Zysku* (Strefa Zysku Individual Investment Programme). This was accompanied by PZU Życie SA's largest advertising campaign of 2006. The campaign started in mid-October and lasted for two months, with advertising on television, in the press, on the radio and the Internet.

Individual Pension Accounts (IKEs) received a non-standard promotion using direct marketing tools. The campaign ran from October to December 2006.

A pilot direct marketing campaign supported group life insurance sales.

A health insurance sale was reinforced by motivation competitions for agents and PZU Group's own staff.

In 2006, the Group paid particular attention to support, motivation and recruitment across its sales network and to the development of its relationships with people cooperating with PZU Życie SA at employer outlets. Agent recruitment was supported by BTL activities and an information campaign on the new recruitment principles, aimed at the agency network management. The Agent Elite Club continued to provide incentives for the agency force.

In 2006, the company developed and rolled-out the *Znamy się* ("Knowing each other") partner programme aimed at people handling group insurance at employer outlets. The programme is designed to streamline information flows between PZU Życie SA and those cooperating in handling the group insurance process, as well as supporting this process.

## Marketing research and analysis

Both PZU SA and PZU Życie SA focused their marketing research and studies largely on products and consumer needs and preferences. The results were used to improve ongoing operations and develop long-term operating strategies.

The most important research projects involved new concepts of Long Term Care (LTC) insurance and investment products, i.e. the *IPI Strefa Zysku*. Surveys intended to support marketing activities were focused on evaluating the creation and reception of promotion and advertising campaigns.

In 2006, PZU SA and PZU Życie SA received and implemented a customer satisfaction assessment programme. The overall customer satisfaction score comprises five assessment fields, including the product offer, service in the sales process, service in the adjustment process, ongoing service, as well as image and confidence. The programme will become cyclical and will monitor indicator changes. The PZU Group performed regular insurance market analyses and surveyed the market positions of the Group's main companies.



## 5.8 Major awards for the PZU Group and its products and services

The long-established presence of the PZU Group on the financial markets and in the cultural, social and economic life of Poland has been recognized with numerous awards

for the Group's companies. In 2006, the group's companies were granted awards for current activity, marketing and corporate social responsibility.

### Recognition of the market position

The PZU Group among the most valuable companies

As one of Poland's top 100 companies, the PZU Group was ranked second in the survey prepared by Newsweek and A.T. Kearney.

No. 1. of Top 100

PZU SA ranked first in the ranking of the "Top 100 Financial Institutions in Poland by 2005 Revenues". In the same ranking the open pension fund, OFE PZU "Złota Jesień", was highly rated at 24th overall and 3rd among pension fund.

Best call centre

The Home & Market economic magazine carried out a survey of financial institutions' call centres. PZU SA came first among insurance companies offering property and casualty products. The company was particularly appreciated for its friendly attitude to customers, pleasant service and general atmosphere of conversation. TFI PZU SA was also highly rated.



## Major awards for the PZU Group

### European Medal for Polonez

PZU FIO Papierów Dłużnych Polonez investment fund (debt securities) has frequently been recognized in press rankings for its excellent performance. This time round, it received the Medal Europejski (the European Medal), which is a combined recommendation of the Office of the Committee for European Integration and Business Center Club, given to products that meet the highest European standards.

### Opieka Medyczna ("Health Care") best among health insurances

Opieka Medyczna ("Health Care"), the individual life and health insurance of PZU Życie SA, was named the "Best Individual Private Health Policy". The ranking took into account the general terms and conditions and other product information submitted by insurers. Ratings were awarded with the "Dobra Polisa" (Good Policy) Insurance Product Quality Certificate in mind.

### Laurels for the Loss Adjustment System

The Loss Adjustment System used by PZU SA was named the "Implementation of the Year 2005" (Wdrożenie Roku 2005) by BEA Systems Poland. The best scores were given for smooth and quick implementation of the system, its advanced technology and, most importantly, for the expertise and work quality of the design team responsible for the project.

### Quality laurel for PTE

PTE PZU SA, the Group's pension fund company, was recognized for the second time with the Polska Nagroda Jakości (the Polish Quality Award) in the category 'Mid-sized Manufacturing and Service Organizations'. Polska Nagroda Jakości is the most prestigious Polish award in quality management. It was established in 1995 and modelled after the European Quality Award (EFQM Excellence Award) and the Japanese Deming Prize.





## Brand recognition

### PZU in the eyes of students

PZU SA took 10th place in the “Career with the Employer 2005” ranking, ahead of companies such as Unilever Polska SA, ING Group, Ernst & Young and PKN Orlen SA. The survey involved students of 125 schools of higher education and universities and their careers’ offices.

### PZU, the trusted brand

Reader’s Digest magazine published the ranking of the most trusted brands in Europe and Poland in 2006. The “Trusted Brands 2006” ranking was the result of a survey in 14 European countries. In Poland, PZU SA took first place among insurance companies.

### PZU Życie in the Pearl Club

Instytut Nauk Ekonomicznych Polskiej Akademii Nauk (Institute of Economics, the Polish Academy of Sciences) and the Polish Market magazine awarded PZU Życie SA a certificate of “the Polish Economic Pearl” in the category “Great Pearls”. The title was given for consistence in pursuing company policies and strategies and for leadership among the most dynamic and efficient companies in Poland. This certificate provided confirmation of the Group’s membership at the Polish Economic Pearls Club.



## Recognition for the corporate social responsibility of the PZU Group

### PZU SA committed to society

In its Report “Responsible Business in Poland 2005. Best Practices.” the Socially Responsible Business Forum presented 60 most interesting initiatives of companies. These examples included two initiatives of PZU SA: “STOP wariatom drogowym” (“STOP Mad Drivers”) programme and “Bezpieczna szkoła z PZU” (“Safe School with PZU”). The report also mentioned a competition organized by the PZU Foundation “Rozwijanie społecznej aktywności niepełnosprawnych dzieci i młodzieży” (“Developing Social Activity of Disabled Children and Youth”).

### Golden Arrow for the “Safe School”

The “Bezpieczna szkoła z PZU” (“Safe School with PZU”) initiative won top place in the Golden Arrow competition in the non-profit campaign category. In general, there were 20 categories, including sales promotion, loyalty programme, web campaign and telemarketing.

### PZU SA 2006 Patron of Culture

PZU SA was for the second time awarded the prestigious title of Mecenat Kultury (“Patron of Culture”) by the Minister of Culture and National Heritage in the Sponsor category. The award is the most prestigious of its kind and is granted for the most significant efforts in supporting Polish culture. The company was recognized for its unique protection programme of wooden churches providing such historic temples with modern fire and anti-burglar security systems.

### PZU Życie SA Patron of Culture in Sopot

PZU Życie SA was honoured with the title of the Mecenat Kultury Sopotu (“Patron of Culture in Sopot”). This prestigious annual award is granted by the Mayor of the City of Sopot for the most effective and interesting way of involvement in the development of the city’s culture. PZU Życie SA received the award for its support for the city’s Teatr Atelier (theatre) and for active participation in cultural activities promoting Sopot.

### PZU SA Friend of Rewal Municipality

PZU SA was awarded the title of “Przyjaciel gminy Rewal” (“Friend of Rewal Municipality”) at the 3rd Tourism Gala in Pogorzelica. PZU SA was recognized for its consistent involvement in water-related safety.



## 6. Corporate social responsibility

By providing financial support to numerous community initiatives and public charities, the PZU Group follows the principles of corporate social responsibility. The areas supported by the Group include health care, education and public safety. For years, patronage of Polish culture and the arts has been part of the PZU Group's strategy of sponsorship and preventative policy. The Group is also one of the country's largest employers.

### 6.1 Preventive activity

#### PZU for safety

For years, the PZU Group has been following a preventive agenda to reduce general risks to human health and life and to property. In 2006, PZU SA and PZU Życie SA spent PLN 72.2 million on its preventive activity.

In this area, PZU SA continued to focus on improving traffic safety, both for drivers and pedestrians. On 21 June 2006, PZU launched the second edition of its preventative campaign "STOP wariatom drogowym" ("Stop Mad Drivers") aimed at making drivers aware that nobody is immune from irresponsible and dangerous behaviour on the road and persuading them to change such negative attitudes.

The company also launched a new preventative programme "Fleet Safety – bezpieczne auto firmowe" ("Fleet Safety") together with Internet Prasa Media Publishing House and the Polish Motor Association. This is the first project in Poland of this size aiming to improve fleet driver safety and reduce general fleet operating costs to entrepreneurs. The programme is targeted at companies with fleets, at managerial staff and executives, company drivers, municipal companies and specialized services. The programme involves a series of training courses and educational meetings.

Out of concern for the youngest road traffic participants, PZU SA continued its educational and preventative "Bezpieczna szkoła z PZU" ("Safe School with PZU") programme. This is principally intended to reduce the number of road accidents

The PZU Group finances its corporate social responsibility agenda using a preventative fund and, to some extent, also sponsorship money. The PZU Foundation is an important element in this area supporting pro publico bono activities in the areas of education, culture and the arts, social help and health care.

involving children and teenagers and to mitigate their effects. Thousands of schools across the country have joined the programme.

The preventative agenda of PZU SA also includes the Group's initiatives intended to improve mountain safety. PZU SA and PZU Życie SA donated PLN 1.5 million to Tatrzańskie Ochotnicze Pogotowie Ratunkowe (Tatra Voluntary Mountain Rescue, TOPR) in a prevention subsidy. The PZU Group signed an agreement to financially support TOPR in its statutory activity until 2010. PZU SA also supports similar statutory activities of the GOPR (Voluntary Mountain Rescue).

In yet another of its preventative programmes "Bezpieczne lato z PZU" ("Safe Summer with PZU"), the company addressed education and the promotion of safe behaviour on water and at the beach, reducing accident rates and providing rescue equipment to 38 municipalities. In 2006, the programme, a continuation from previous years, was expanded by the addition of Akademia Ratownictwa PZU ("PZU Rescue Academy"), a professional training course for municipal services and police in water rescue and operating rescue equipment.

As in previous years, in 2006 PZU SA donated prevention subsidies to the National Fire Department and Volunteer Fire Service. The PLN 8 million were spent to purchase fire engines across Poland.



## PZU for health

In 2006, the PZU Group launched a new programme financed from the prevention fund called “Aktywuj się z PZU Życie” (“Get Active with PZU Życie”) aimed to encourage Poles to take up active and healthy lifestyles, but also to educate the target groups about the benefits of physical activity in the prevention of chronic dis-

eases and to promote preventive attitudes in society.

“Aktywuj się z PZU Życie” consists of three components targeted at different groups, i.e. companies with group insurance in PZU Życie SA, primary and secondary school students as well as students and lecturers of medical colleges.

## 6.2 Sponsoring activity

### PZU for Culture and the Arts

After many years, support for culture and the arts remains a strategic area of PZU Group sponsorship and preventative policies. Since 2005, this activity has been carried out as part of the long-term programme “PZU dla kultury i sztuki” (“PZU for Culture and the Arts”).

In 2006, together with the Secretariat of the Polish Episcopate and the Centre for the Protection of Public Collections, PZU SA started the second step of its programme “PZU for Culture and the Arts”. This initiative aims at protecting historic wooden churches against burglary and fire; each year, Poland loses priceless monuments of architecture to thieves and fire. In order to counteract these phenomena, modern fire protection and anti-burglar systems have been installed in wooden churches around Poland. Two steps of the programme covered 27 sacral buildings and the amount spent on protective measures in 2006 was PLN 800,000. PZU SA was awarded with the title of the Benefactor of Culture for its programme of wooden churches protection.

In pursuing its sponsorship policy, the PZU Group has for many years been active in the organization of numerous cultural events, such as exhibitions, concerts and festivals. In 2006, PZU SA spent PLN 1,250,000 on cultural sponsorship, while PZU Życie SA – nearly PLN 700,000. The companies supported many high-profile artistic events, including exhibitions at the Royal Castle in Warsaw (“The glow of silver... Silverware from 16th –19th century in the Republic of Poland and Lithuania, and contemporary Poland, collections from the State Hermitage Museum of St. Petersburg, the Kremlin and Historical Museum in Moscow”, “Portraits. Rembrandt and...” – presentation of Rembrandt’s paintings; “At the throne of the Queen of Poland. Jasna Góra in Poland’s cultural and spiritual life” – an exhibition devoted to works of art collected by the Pauline Order in Jasna Góra).

In summer 2006, PZU Życie SA became a patron of the annual summer event “Theatre in summer Sopot 2006”. This project won PZU Życie SA the title of the Patron of Culture in the City of Sopot in recognition of the company’s key role in supporting cultural life in the city. The PZU Group sponsors prestigious jazz concerts under the Era of Jazz series.

### PZU for Sports

The PZU Group continued to sponsor sports initiatives during 2006. PZU SA spent a total of PLN 6,400,000 and PZU Życie SA spent PLN 340,000 supporting sporting activities.

PZU SA also sponsored the men’s volleyball team PZU AZS Olsztyn and the Polish Tennis Association, providing insurance cover for the players and their trips to competitions abroad.



## 6.3 The PZU Foundation

The PZU Foundation has been launched to support activities of non-governmental organizations aimed at the public benefit.

On 9 February 2007, a Register Court recorded changes in the PZU Foundation's Articles of Association, with prior approval of the Foundation Board and its founding body. According to the new Articles of Association, the Foundation aims to work for the public benefit within the following areas:

1. social welfare, including support for families and people in difficult situations and providing them with equal opportunities,
2. charity work,
3. preservation of national traditions, promotion of Poland's national heritage and creation of national, civic and cultural identity,
4. health care and promotion,
5. work for the disabled,
6. support of local communities,
7. support of national minorities,
8. science, education and upbringing,
9. active leisure for children and young people,
10. culture, arts, protection of cultural heritage and tradition,
11. promotion of physical culture and sport,
12. environmental and animal protection, protection of natural heritage,
13. public order and safety and counteraction of social pathologies,
14. life-guard and people protection,
15. support for victims of catastrophes and natural disasters, armed conflicts and wars in Poland and abroad,
16. promotion and organisation of voluntary work, as long as it relates to the objectives of the Foundation.

In 2006, the Foundation activities consisted of direct grants allocated to other non-governmental organizations to finance various programmes and projects, and in partner programmes implemented in cooperation with valued social partners. The Foundation also allocated individual grants to

employees of the PZU Group who found themselves in difficult situations due to illness of their closest family members.

The total amount of grants allocated by the Foundation equalled PLN 4,670,710.38.





Over 33% of this sum, i.e. PLN 1,541,878, was spent on partner programmes implemented in cooperation with organizations that have been working with the PZU Foundation for some years. They include:

- the Association for Creative Initiatives "ę" (Towarzystwo Inicjatyw Twórczych "ę"),
- the Educational Foundation of Entrepreneurship (Fundacja Edukacyjna Przedsiębiorczości),
- the Polish Union for Oncology (Polska Unia Onkologii),
- the Modern Poland Foundation (Fundacja Nowoczesna Polska),
- the Academy for the Development of Philanthropy in Poland (Akademia Rozwoju Filantropii w Polsce),
- the Polish Foundation of Children and Young People (Polska Fundacja Dzieci i Młodzieży).

Under the partnership programmes, the PZU Foundation, together with the Academy for the Development of Philanthropy in Poland, organized the second step of the initia-

tive "Linking generations". The Contest Committee selected projects submitted by 25 organizations, which received grants totalling PLN 728,789.38.

An amount of PLN 1,030,580 was donated in the form of grants to projects submitted outside of the competition. Financial support was hence granted to ten organisations:

- "Polityka" weekly,
- the Association for Special Education in Tczew (Stowarzyszenie na rzecz Szkolnictwa Specjalnego w Tczewie),
- the "Pro-Physica" Foundation (twice),
- the ABCXXI Foundation,
- the Association of Mathematics Teachers (Stowarzyszenie Nauczycieli Matematyki),
- the Foundation for the Promotion of Skilled Children "Odysseus" (Fundacja Promocji Dzieci Zdolnych "Odysseusz"),
- the Center for Educational Initiatives (Centrum Inicjatyw Oświatowych),
- the "Social Support SOS" Foundation (Fundacja "Pomoc Społeczna SOS"),
- the "Tratwa" Association,
- the Caritas of Zielona Góra and Gorzów Diocese.

In 2006, three competitions were held: two for grants and an actuarial one. The total amount spent on competitions was PLN 1,275,291.50. During the grant-winning competition entitled "Enhancing educational offer in rural areas and small towns", the competition board selected 35 organizations, which were granted PLN 640,278. At the competition entitled "Developing social activity of disabled children and young people", the expert committee initially selected 25 organizations but eventually the number shrank to 24, as Halina Sroczyńska Foundation from Opatówek resigned from the competition for reasons not related to the PZU Foundation.

The total amount of PLN 596,013.50 was distributed among the competitors. During the actuarial competition, organised together with PZU SA, the pool of awards reached PLN 39,000.

The Foundation Management Board adopted nine resolutions on granting financial assistance to PZU Group employees. The total amount of funds spent on medical treatment, rehabilitation and medical devices reached PLN 94,172. Financial support was also extended to the children of the Group PZU's employees.

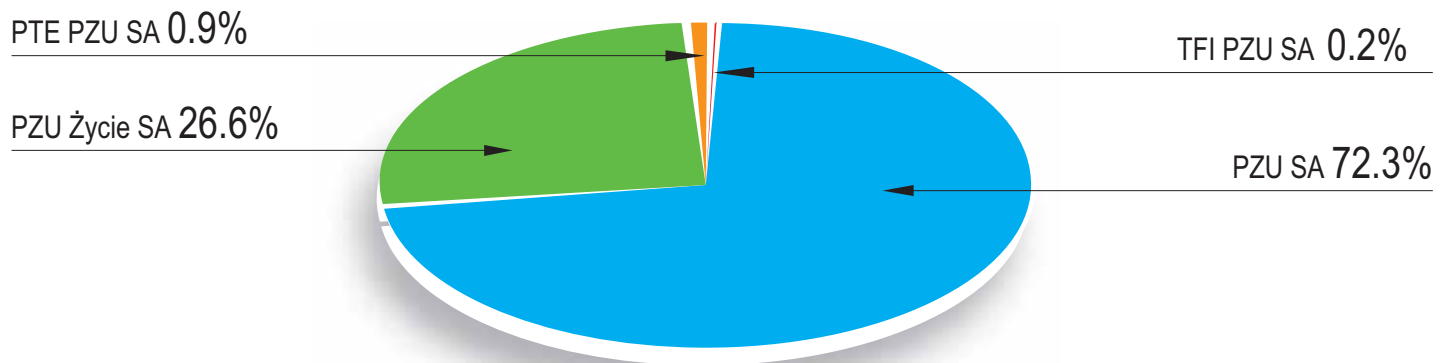


## 6.4 The PZU Group as a good employer

The PZU Group is one of the biggest employers in the financial sector in Poland. At the end of 2006, four main companies of the PZU Group employed over 16,000 people.

The structure of employment broken down into the main companies of the PZU Group as of 31st December 2006.

Source: The PZU Group





## Training and professional development system

In 2006, PZU SA and PZU Życie SA conducted 5,534 training courses, whereby over 42,000, people were trained during 8,647 training days. Thus, on average every employee participated in 2.9 training sessions. Statistically, 7.6 people took part in every training session of 1.5 day. The type of training was adjusted to the needs of the trainee groups and to the topics selected on the basis of prior analyses of training needs. The scope of training was related primarily to new products as well as products within the existing offers of PZU SA and PZU Życie SA, and also to optimizing sales tech-

niques. Moreover, the Group organized training sessions related to implemented IT solutions and aimed at improving the qualifications and professional competencies of PZU SA and PZU Życie SA employees. The senior management of both companies took part in many training sessions and conferences, both in Poland and abroad. Moreover, the second step of apprenticeship and internship programmes was launched and co-operation was initiated with student organizations in order to attract students and graduates to work or train at the PZU Group companies.

## Introduction of the Collective Labour Agreement

In 2006, agreement was reached with trade unions on the introduction of the Collective Labour Agreement. The change was aimed at unifying the rules on remunerating employees and enabling common remuneration policy within the PZU Group. The new rules are more beneficial to both the em-

ployees and the employer: an incentive-driven bonus fund to be used up in full, a higher annual award, higher jubilee awards and severance pays, along with additional benefits for employees.

## Internal communication

In 2006, the PZU Group's internal communication activities focused on building a corporate culture based on openness and integration of the Group's employees.

The process of developing an internal communication strategy for important projects within the Group companies has been optimized and consistent information campaigns organised both within the organization and outside.

To this end, internal communication tools enhancing mutual communication have been used, i.e. an internal newsletter "PZU world" and an insert "PZU Agent's World" ("Świat Agenta PZU"), an electronic newsletter "Straight from the horse's mouth" ("Z pierwszej ręki"), intranet pzu24 website,

workshops for mid-level management and regular workshops with Opinion Leaders from all over Poland.

In 2006, an electronic issue of the "PZU World" was launched.

The Group undertook efforts aimed at increasing employee activity and satisfaction, along with loyalty to the employer. Integration picnics were organized in 11 Polish cities, focusing on the values of the Group's employees. An innovative competition "Enlighten us with your ideas" was organised for PZU SA and PZU Życie SA employees. Before Christmas, a charity campaign called "Christmas action of PZU employees" was launched, consisting of collecting sweets for children from orphanages.



## 7. Organization and infrastructure of the PZU Group

### 7.1 Sales network, distribution channels and customer service

#### The PZU Group sales network

The PZU Group has the most extensive sales network on the Polish insurance market. After integrating the regional structures of PZU SA and PZU Życie SA at the end of 2005 (under the “macro” field reform), the PZU Group has nine regional offices of PZU SA and nine regional offices of PZU Życie SA, with overlapping geographical reach. Branch units borders were co-coordinated with national administrative divisions, and operating areas were allocated to individual voivodships. The PZU Group's sales network consisted of 354 local branch units for PZU SA and 380 local branches of PZU Życie SA.

The PZU Group offered its property and casualty products through a network of more than 7,000 tied agencies and over 1,700 multi-tied agencies. With regard to selling motor insurance in 2006, PZU SA cooperated with over 960 car dealers and 1,040 second-hand outlets. The Group companies co-operated with the majority of brokers operating on the Polish market. This distribution channel is constantly gaining in importance, especially for insurance products sold to corporate customers. In 2006, 632 out of 744 brokers cooperating with PZU SA worked for the Corporate Customer Division.

Nearly 5,200 insurance agents were actively selling life insurance contracts (including 1,815 IKE agents – selling Individual Pension Accounts). The PZU Group's bancassurance

and financial insurance products were also offered via banking delivery channels. The Group's companies entered into active cooperation with the leading banks operating on the Polish market, such as PKO BP SA, Bank Millennium SA, Bank Gospodarki Żywnościowej SA, Deutsche Bank PBC and Bank Ochrony Środowiska SA.

Sales of OFE PZU “Złota Jesień” pension fund units are based on the PZU Group distribution network. Agreements can be signed in every branch of the Group, while ca. 9,500 sales representatives are engaged in new acquisitions. It is also possible to conclude “Złota Jesień” Fund agreements on-line via PZU Group internet portal.

TFI PZU SA investment funds worked mainly through the Group's distribution channels. TFI concluded cooperation agreements with nearly 1,200 authorized representatives. In 2006, TFI PZU SA products were also available at BRE Group's internet banks, in the networks of Elite Finance & Consulting and Expander financial advisors as well as on the internet platforms of Dom Maklerski AmerBrokers, Dom Maklerski Polonia NET SA, Beskidzki Dom Maklerski, Krakowski Bank Spółdzielczy, International Risk & Corporate Advisory (IRCA) and Secus Asset Management SA.



## Reform of the sales network

2006 saw the continuation of three coordinated projects within the area of sales and customer relations. The “micro” reform project was developed with the aim of defining a new model of sales processes and creating a new sales administration organization. The immediate objective behind the project was to achieve standard high quality agent and customer service across all PZU SA local branch units. Other sales projects implemented in 2006 included reforming mass sales and corporate sales. These initiatives were based on the Company's business strategy, with its principal objective of sales structure enhancement, and thus consolidating the company's market position. The basic objectives behind these projects were to ensure that the Group's companies generate regular and constant increases in sold policies and to mitigate against reductions in market share. These targets can only be achieved when the sales administration is separated from sale processes, and after individual divisions are deemed responsible for implementing and supervising processes allocated to them. 2006 saw the comprehensive implementation of changes stemming from these projects. A new project, aimed at revitalizing the agency network, was also started, aimed to improve sales efficiency of agents

cooperating with PZU SA. Having achieved this, it will be possible to integrate non-life and life agency structures and adjust the sales requirements of both Companies and accommodate customer segments. The Group is also working on developing PZU Group agencies, which in the future will operate as model sales and services entities, cooperating with PZU SA on the basis of agency agreements.

**In order to improve customer service standards at organizational units offices, PZU SA introduced qualitative changes in mass sales solutions for both PZU customers and employees. The concept of office agency management increases the efficiency of customer contacts guaranteeing a top level of services provided by the insurance agency.** This management model provides direct coordination of sales people, thus enabling the Group to be able to better adjust its model to mass customer needs, while improving the technicalities of the sales administration process. The PZU SA office agency acts as an insurance agent for PZU SA and delivers acquisition services for the Open Pension Fund (OFE) managed by PTE PZU SA, i.e. so-called cross selling.



## 7.2 Claims and benefits

In the loss adjustment area, 2006 saw a continuation of process-related activities and organization, aimed at optimizing services for customers and PZU SA employees. Priority was given to activities ensuring a high level of customer service and reduction in average loss adjustment time. Three products/services intended to ensure top quality of services for PZU SA customers were fully launched:

- **TeleAssistance PZU (Telepomoc PZU).** At present, all losses on vehicles can be reported by telephone, 24 hours per day, 7 day per week by calling 0 801 102 102. The service will also include confirmation of vehicle loss report, appointments for vehicle viewing and towing of a damaged vehicle from collision sites if needed. The customer will be instructed about steps in the loss adjustment procedure.
- **Mobile Experts (Mobilni Eksperci).** A group of 209 selected technical adjusters (experts), who by appointment view the damaged vehicles in any place reported by the customer. At the vehicle park location, the Mobile Experts take pictures to document the damage and calculate its value. The launch of the Mobile Experts contributed largely to shortening customer-waiting time for viewing the damaged vehicle from one week to 2-3 days.

- **Implementation of CSI-SLS system (Loss Adjustment System) to adjust losses in vehicles nationwide.** SLS makes loss adjustment process much more efficient both in substantive and technical terms. As it is a central system, it enables the adjusters to track down all losses in Poland. Moreover, it allows for loss "linking", thus curbing insurance fraud. Furthermore, the system supports the loss adjustment process by generating templates of letters to customers and other entities involved in the loss adjustment process. The system reminds adjusters of overdue losses. Currently, all motor insurance losses are covered by the SLS system. The next step will be the launch of a property loss adjustment system in 2007.

In relation to the changes pertaining to loss adjustment, the second version of the following procedures was introduced: *"Procedures for vehicle loss adjustment with SLS application, TeleAssistance and Mobile Expert in the transitional organisation"*, optimizing loss adjustment solutions in substantive and technical terms. All improvements are aimed at shortening loss adjustment times and improving customer service quality.



The new loss adjustment organization project also included adjustment of property losses. This concept covers the following preparatory work:

- development of target organisation of property loss adjustment,
- development of draft uniform procedures of property loss adjustment,
- development of Mobile Experts concept for property adjustment,
- operational segmentation of property losses.

The implementation of these solutions will considerably improve the quality of property loss adjustment, thus optimizing customer service and reducing loss adjustment time, which will also enhance the image of PZU SA.

quality garages were allowed to accept losses, to view damaged vehicles and calculate the costs of repair and then submit them to PZU SA by electronic mail for approval of technical adjusters.

2006 was a year of continued activities aimed at developing cooperation with the Repair Network garages. New high

In 2006, PZU Życie SA launched the analytical phase of a project aimed at centralizing and optimizing the benefits adjustment processes. The main concept behind the project was to develop the best processes and organisation of benefits adjustment to accommodate the following objectives:

- to reduce process costs,
- to increase customer satisfaction,
- to reduce the value of benefits from fraud.

These objectives will be achieved due to process modification, implementation of a modern IT system and electronic document flow.

The next project phases will include:

- pilot launch of benefits adjustment model in a selected organisational unit,
- nationwide implementation of the benefits adjustment model.



## 7.3 The IT solutions for the PZU Group processes and other business initiatives

In 2006, the PZU Group continued to develop strategic projects initiated in the previous years.

The basic activities aimed at optimizing the PZU Group sales process and customer service were finalized, including the already mentioned "micro" sales reform and centralization of the PZU SA IT system. System works consisted of integrating product systems data into a single system, enabling efficient customer services regardless of where agreements are concluded, with the use of customer relation history. This was a huge project supporting organizational changes within PZU SA, and triggering the need to build a modern wide-area network and data processing centre.

2006 saw the finalization of the first phase of the creation of the Financial and Accounting Centre (Centrum Finansowo-Księgowe CFK). Most of the tasks related to booking PZU SA administrative charges were transferred to the Centre. CFK's tasks will be expanded in 2007 with HR and payment administration of selected Company branch units. The positive financial effects of these activities will be fully visible only in the years to come. In PZU Życie SA, activities aimed at separating booking and payment functions from organizational unit structures and moving them to the newly created joint services centres were conducted under the booking services reorganization initiative.

The Group also engaged in works related to implementation of an IT system to support PZU agents. The launch of this solution will be highly beneficial both in terms of data quality and the costs of policy administration in PZU SA (introducing data to the system, verification and agent settlement processes). Given the implementation timetable, the financial benefits from this project will be fully visible in 2008–2009.

PZU SA is also pursuing other important projects, such as implementation of a new administration system for corporate customers insurance (Corpo) and building the Central Database of Institutional Clients (CBKI).

The main development task of 2006 was continued implementation of target architecture for the integrated IT system in PZU Życie SA, performed primarily with the following projects: GraphTalk A.I.A. (central product system), Document and Cases Maintenance System (BPM), Central Commission System, Rejestrator Project and Info Bus project. The project IT Governance was also started.





# 06

## 8. Significant risk factors in PZU Group operations – Risk Management

Business operations are always related to risk. Depending on the type of factors influencing it, risk can be higher or lower and can pertain to wide groups of stakeholders,

such as employees, trading partners or stockholders and shareholders.

Risk management is one of the key priorities of the PZU Group. All management activities are aimed at optimizing financial results within the limit of acceptable risk.

The main indices of acceptable risk are:

- ensuring the long-term and short-term solvency of the PZU Group,
- ensuring stable and predictable financial results and adequate returns on equity.

The risks of particular concern to the Management Boards of the PZU Group Companies include:

- in the area of insurance risk: product offer and premium rating risk, risk of technical reserve adequacy and risk of reinsurance program adequacy,
- in the area of market risk: risk of interest rate changes and risk of assets price changes,
- in the area of credit risk: risk of insolvency or deterioration of the financial standing of partners and/or issuer of purchased financial instruments,
- in the area of operational risk: risk of inadequacy of procedures defining relevant control to counteract abuses, while maintaining adequate business flexibility.

### 8.1 Insurance risk

Insurance risk is managed in three main areas:

- product and premium rating risk,
- risk of technical reserves adequacy,
- risk of reinsurance programme adequacy.





## 8.1.1 Product and premium rating risk

### Property insurance

Product construction and premium ratings fall within the responsibility of the Product Management Office at PZU SA. The product manager is responsible for the product and coordination of works related to it. The legal aspects, i.e. the text of the general insurance terms and conditions are worked out by the product manager's team. Premium rating is developed by the Section of Premium Calculations, in cooperation with the product manager. This is a two-step process: actuarial risk assessment followed by market risk assessment. Market risk assessment is performed together with the product manager, and accounts for additional factors and market conditions, as well as marketing guidelines not covered by actuarial risk distribution analysis.

Final premium scheduling is always based on the following elements:

- the text of the general insurance terms and conditions,
- technical reserves value and reserve policy guidelines agreed upon by the Actuarial Department,
- guidelines pertaining to target insurance group and marketing policy.

Along with the premium ratings, the company also develops simulations of projected insurance results for future years.

Regular analyses of premium adequacy and portfolio profitability for specific insurance products are conducted during the year. The frequency of these analyses depends on product size and potential result fluctuation. If a negative trend is detected, actions are taken to regain the relevant profitability level, consisting of modifying premium rates or even changing the profile or insured risk by modifying relevant provisions of the general insurance terms and conditions.

The 2006 change in the corporate customer service model, and especially adjustments in the product offer, resulted in works aimed at unifying and structuring activities related to insurance risk assessment in the Corporate Customer Division. Depending on customer classification activity and related risk category, the assessment is performed by employees of PZU SA organizational units or specialists from the Risk Assessment Team within the Corporate Sales Office of the PZU SA headquarters.

The assessment covers risks related to customer property location, technological process, general organization and other additional conditions constituting potential threat of loss to the insured or to be insured property. Further to the customer location audit, the Group is developing guidelines for the reduction of identified risks via technical and organizational measures. For the insurance company, these guidelines serve as basis for developing risk management policy together with the customer.



## 8.1.2 Risk of technical reserves adequacy

### Life insurance

The premium rating is coordinated by the Actuarial Team in the Product Management Office of PZU SA. It forms part of the new product development process, coordinated by a senior line manager.

The premium rating documentation consists of the following elements:

- an insurance technical plan, containing, among others, a brief description and product characteristics, description of used data sources and analyses, net premium ratings, rules of building technical reserves,
- insurance business plan projecting future insurance course with financial flows method.

Within the technical plan, the rules of creating and calculating technical reserves are agreed upon and consulted with the Actuarial Department.

The company carries out regular analyses of premium adequacy and portfolio profitability further to various types of analyses and reports, including:

- evaluation of underwriting results for products for a given reporting period,
- product profitability assessment further to insurance portfolio evaluation under the Embedded Value calculation within the part pertaining to current value of discounted future profits.

The risk of technical reserves adequacy is managed by the Actuarial Departments of PZU S.A. and PZU Życie SA.

The policy of creating technical reserves in the PZU Group is based on the following elements:

- a conservative approach to defining the value of technical reserves,
- continuation principles, i.e. technical reserves building methodology should not be changed unless significant circumstances dictate its necessity.

### Property and casualty insurance

The ultimate loss is estimated at the PZU SA head office based on loss triangles at the end of each balance-sheet year for each product, broken down into accident years.

Ultimate loss estimation methods are as follows:

- Chain Ladder,
- Cape Cod,
- Bornhuetter-Ferguson.



The choice of method depends on the type of loss within a given product. The reserves are estimated by the Chief Actuary and reviewed by an external expert.

#### Life insurance

The reserves are estimated by the Chief Actuary

#### 8.1.3 Risk of reinsurance programme adequacy

The risk of reinsurance programme adequacy is managed by the Reinsurance Office. In PZU SA business, the most significant risks pertain to losses that may appear due to natural disasters and catastrophes. PZU SA protects itself against such risks mainly through an optimized reinsurance programme. Over the fifteen years of its reinsurance policy, PZU SA has changed the form and scope of protection, but has always been oriented to providing for the Company's maximum financial security.

During the last couple of years reinsurance activity has been aimed at the following targets:

- transfer of risk to protect the underwriting results of property and casualty insurance,
- covering individual insurance groups with protection against single large losses, catastrophe-related losses or loss accumulation,
- guaranteeing the financial stability of PZU SA.

#### 8.2 Market risk

Market risk is managed by the Assets Liabilities Committee (ALCO) of the PZU Group, the Treasurer Office and the PZU Asset Management SA, all within their own competences.

Market risk management is based on two main pillars:

- managing the risk of interest rate changes,
- managing the risk of assets price changes.



In the PZU Group, risk, and market risk in particular, is managed with the use of financial models and a system of limits stemming from these models, along with binding legal regulations.

The ALM model for PZU S.A. is based on the idea of replication of the liabilities portfolio and duration of assets and liabilities. The ALM model for PZU SA is a deterministic one.

The ALM model for PZU Życie SA is based on the concept of defining the optimum structure of assets within the acceptable level of risk. Risk is mainly measured by the probability of insolvency (lack of adequate assets to cover dues and solvency margins) within the adopted time period. The ALM model for PZU Życie SA is a semi-stochastic one.

## 8.3 Credit risk

Credit risk in the PZU Group is managed within two main areas:

- investment activity,
- reinsurance activity.

### 8.3.1 Investment activity

Within the scope of placement activity, credit risk is managed and controlled by the Treasurer Office and Assets Liabilities Committee of the PZU Group. Credit risk management and control is performed in two main areas: the banks cooperating with the PZU Group and issuers of financial instruments.

Credit limits are defined for each bank, financial instruments issuer or programme.

### 8.3.2 Reinsurance activity

Within the scope of reinsurance activity the PZU Group's credit risk is managed in the following way:

- participation offers for obligatory treaties are presented only to reinsurance companies that are highly evaluated by Standard & Poor's, AM Best, Moody's and Fitch rating agencies, therefore the dominant share in reinsurance premiums belongs to reinsurers with top ratings (e.g. for Standard & Poor's – with ratings above "A"),
- the portfolio is being diversified to avoid accumulation of potential receivables from a single reinsurance company.



## 8.4 Operational risk

Operational risk is monitored by the Internal Audit Office. The main areas of operational risk to which the PZU Group is exposed are as follows:

- The HR area – due to high level of employment, including specific sales network (insurance agents) and dispersed organizational structure, as well as the proneness of basic processes in insurance activity (acquisition and loss adjustment) to potential abuses,
- The IT area – due to critical dependence of basic operational processes on IT support.

### 8.4.1 Risk of human resources

The mechanism mitigating human resources risk applied in PZU Group companies includes in particular: rules on employees recruitment, a system of employee training and assessment, incentive systems, agreements on data confidentiality and a ban on the use of acquired knowledge for a specific period of time, loyalty agreements, a Code of Ethics for PZU Group employees, rules on good practice in financial and capital investments to be applied by PZU employees and conditions of agency agreements.

### 8.4.2 Management and control risk

Management and control risk is mitigated by the following elements: an internal regulation system, powers of attorney and competencies for insurance risk assessment, division of tasks (separating functions), organizational structure (middle management levels), obligation to use holiday leave, internal audits in the context of the risk management system and identifying potential gaps, internal control of abuses and fraud.

Any identified cases of poor control are reported to the management along with recommendations supporting their elimination.

### 8.4.3 IT system risk

The mechanisms aimed at mitigating IT system risk applied in PZU Group companies include, among others: division of tasks (separation of functions), system embedded controls, central change management in the system, policy of data storing, warehousing and reading, developing system authorization and access rights policy, business continuity planning, agreements standardization activities, conditions of agreements concluded with software and hardware suppliers, use of a specific IT environment, works on service components in application architecture, diversification of suppliers and training sessions.



### Reinsurance policy of PZU Group

In 2006, PZU SA and PZU Życie SA undertook steps aimed at centralizing reinsurance activities in both Companies. Centralization of reinsurance will enable construction of efficient reinsurance programmes to protect both Companies' insurance portfolios and should also ensure coherent control over the processes of planning and execution in this respect.

**In 2006, PZU SA continued the reinsurance policy started in previous years aimed at replacing proportional programmes with non-proportional agreements.** PZU SA had one proportional agreement in its portfolio in 2006 to cover credit and surety insurance portfolio. The reinsurance cost as a percentage of premiums ceded to gross premiums written amounted to 1.6% in 2006. In 2005, the relation was ca. 5.2%. Changes in the reinsurance structure had a major impact on improvement in underwriting flexibility. PZU SA successfully managed to achieve beneficial changes in the technical conditions of various agreements, matching reinsurance cover to evolving portfolio requirements.

The PZU SA reinsurance programme consisted of seven obligatory reinsurance treaties, approximately 150 facultative reinsurance agreements and a number of service agreements supporting sales processes and risk assessment.

Similarly to previous years, PZU SA cooperated with leading reinsurance companies (including Munich Re, Lloyd's, Hannover Re, SCOR Re and AXA Re). In 2006, obligatory reinsurance treaties were placed with over 35 reinsurance companies. Over 94% of reinsurance premiums were ceded to reinsurance companies with Standard & Poor's rating of "A" or above.

In 2006, PZU Życie SA was not engaged in the inward reinsurance business, but acted as a party to two outward reinsurance agreements. Reinsurance in the Company is mainly aimed at protecting the whole portfolio against risk accumulation (catastrophe treaty). In future years, the number of reinsurance agreements is expected to grow due to new insurance product launches supported by reinsurance companies' know-how.

### Catastrophe risks

As part of the risk accumulation project, in 2006 PZU SA continued to analyse the scale of the Company's insurance portfolio exposure to the risk of flooding and hurricanes.

The results of the work were used in the renewal process, allowing for negotiation of better price conditions for a catastrophe treaty.

### Inward reinsurance

Similarly to previous years, with regard to inward reinsurance, PZU SA supported domestic insurance companies, mainly with facultative reinsurance.

In 2006, PZU SA coordinated the process of building a reinsurance programme and developing its structure together with UAB DK PZU Lietuva and OJSC IC PZU Ukraine. The Company also continued its involvement in reinsurance for its subsidiaries as their reinsurer.





## 10. Asset Management

### Activities of PZU Asset Management SA

2006 was the first calendar year in which PZU Asset Management SA ran operations in the area of PZU Group asset management. Asset management was the only type of brokerage activity performed by the Company. Within this

remit, PZU Asset Management SA managed the assets of basic product companies of the PZU Group, i.e. PZU SA, PZU Życie SA, TFI PZU SA funds and assets of the *Employees Pension Fund Słoneczna Jesień*.

In 2006, PZU Asset Management SA began to manage three new funds of TFI PZU SA:

- PZU FIO SME stocks fund,
- PZU SFIO Property Protection Fund,
- PZU SFIO Foreign Funds (an umbrella fund, covering of four sub-funds: equities fund, balanced fund, stable growth fund and multiple assets class fund).

*PZU Asset Management SA* actively manages the *PZU FIO SME stocks fund*, while in the case of the *PZU SFIO Property Protection Fund* it developed an investment model concept and carries out regular adjustments, whereas for PZU SFIO Foreign Funds it executes a strategy defined by an external advisor appointed by TFI PZU SA.

In 2006, the PZU Asset Management SA was an active participant in the development of new insurance and investment products for PZU Życie SA: *db Guarantee Asian Basket* and *db Harmony II*.

In 2006, the Company's Management Board adopted a resolution on the implementation of the PZU Asset Management SA Code of Best Practices for institutional Investors, which was developed and approved by the Chamber of Fund and Asset Management and the Commercial Chamber of Pension Funds.

The tasks executed in 2006 by the Management Board of PZU Asset Management SA also included changes in internal regulations governing brokerage activity and its support, and works on solutions enabling the management of new asset classes. In the nearest future, PZU Asset Management SA is planning to launch a Real Estate Team to manage the real estate sector fund, which will initially be available only to a selected group of investors.

At the end of December 2006, the PZU Asset Management SA employed 47 people, including seven investment advisor license holders.





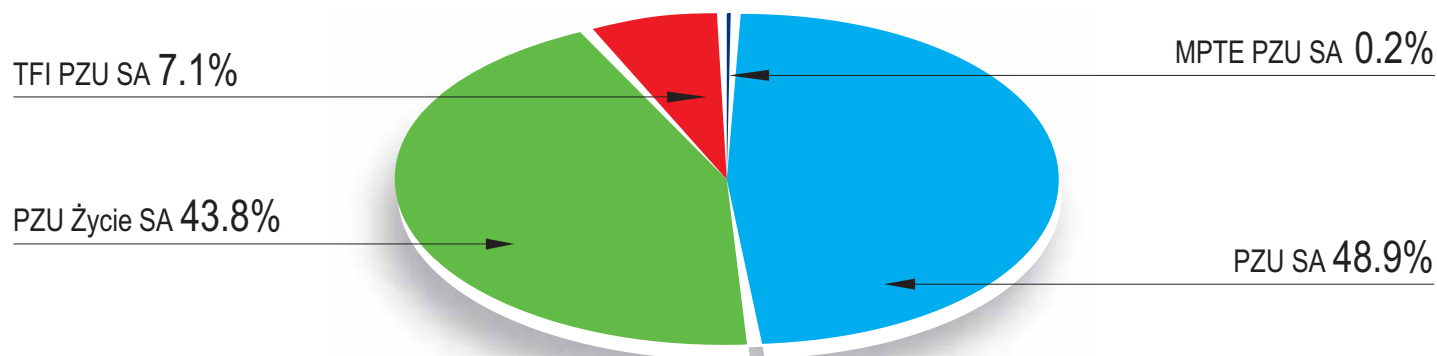
## The asset portfolio managed by PZU Asset Management SA

As of 29 December 2006, PZU Asset Management SA managed assets amounting to PLN 23.2 billion. In 2006, assets under management grew by 18%. The share of TFI PZU SA's assets in the portfolio rose significantly – at the end

of 2005 it amounted to 4.2%, while at the end of 2006 it exceeded 7%. The share of PZU SA assets in the portfolio remained at the same level, whereas the share of PZU Życie SA assets dropped.

## Assets managed by PZU Asset Management SA broken down into PZU Group companies as of 31 December 2006

Source: The PZU Group



## 11. Rating

On 5 June 2006, Standard & Poor's confirmed its "A–" rating for the main insurance companies of the Group (PZU SA and PZU Życie SA), but downgraded its outlook from stable to negative.

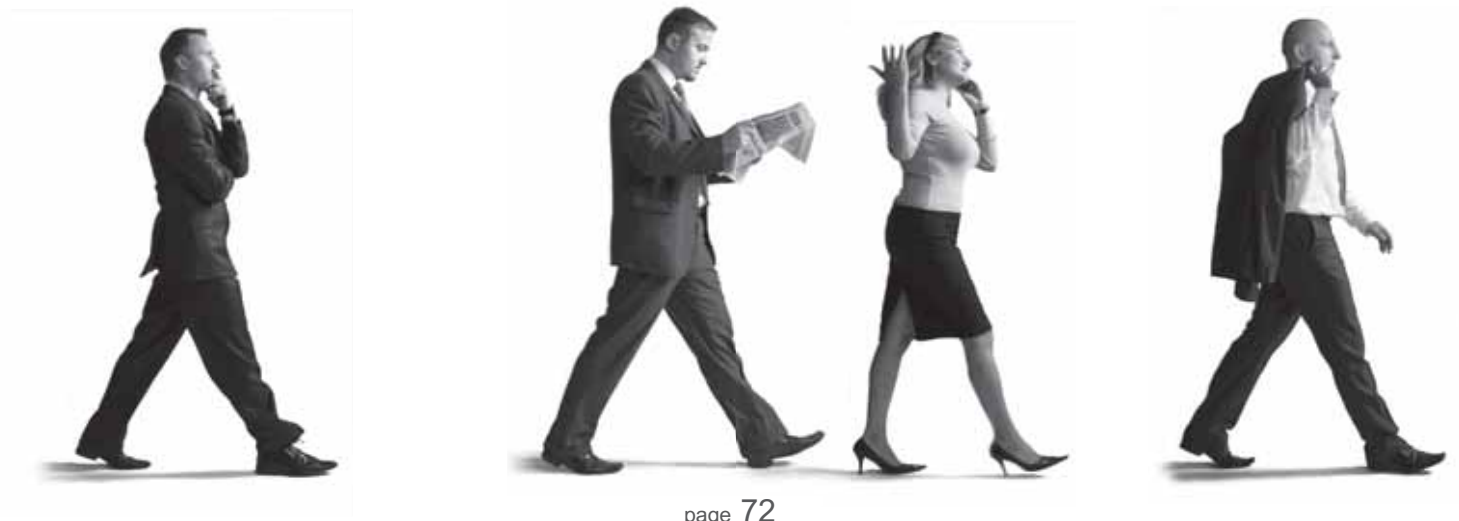
Justifying its position in the report of 24 July 2006, the agency cited the strong competitive position of the PZU Group and its excellent operating performance, which enhanced the rating. The PZU Group's strong competitive position stems mainly from its leading position on the Polish insurance market, very strong sales potential and high brand awareness in Polish society. Both PZU SA and PZU Życie SA

reported very good operational results, which is attributable to its leading position in both property and casualty, as well as life, insurance segments and low costs compared to the company's competitors.

The outlook downgrade from stable to negative was caused by the agency's uncertainty about PZU SA's future development directions and potential changes in the Group's top management positions. Standard & Poor's analysts were also concerned about the impact of political risk on operations in the context of a shareholder conflict.

Standard & Poor's stated that if these concerns are not confirmed, the rating outlook should be brought back to stable. This, however, can only happen if the following agency expectations are fulfilled:

- it is expected that PZU SA will continue to generate a very good operating performance, maintaining the Combined Ratio at an average level of 95% and ROE considerably higher than 15%,
- it is expected that the PZU Group will maintain a high capitalization level, as required for "AA" rating (in line with Standard & Poor's capital model requirements) and high quality of funds, along with adequate reinsurance cover and reserves level.



### 12.1 The Group's strategy and execution

2006 was the first year in which the PZU Group implemented its 2006-2010 strategy, the main objective of which is to maintain its status as the leading financial institution in Poland and Central and Eastern Europe.

#### Customer oriented sales organisation

The PZU Group continued to work towards consolidating its market position by improving its existing customer relations, for example by introducing additional sales of non-motor insurance products, individual life insurance and pension products to mass individual customers as well as to small and medium enterprises. The Group also enhanced its relations with corporate customers by introducing more efficient customer information management via a dedicated IT system.

The PZU Group implemented changes to its organization, management processes and competence development, which used to be product-oriented, refocusing them on customer needs and building a comprehensive offer addressed to various customer segments, such as medium net worth individual customers - in the scope of health insurance, Individual Pensions Accounts and modern investment products offered via banks and insurance agents.

As part of the strategy's implementation, the company conducted activities in four basic areas of key importance for the Group's level of revenues and efficiency.

In 2006, the PZU Group executed many strategic initiatives with a view of integrating and reorganizing the Group's distribution channels to improve the quality of customer service. The Group continued to develop a global Group model of managing the agency network to prepare agents to sell both life and property and casualty products, and increase the sales role of the Group's branch units, while reducing their role in sales and operations administration. 2006 saw the dynamic development of the "contact centre" and a direct sales channel. With a single telephone call, customers can receive comprehensive information on PZU Group products, purchase tourism insurance or make an appointment with an insurance agent to gain insight into the complete product range.

Within the banking distribution channel, the PZU Group was actively continuing consolidation of its existing relationships with banks.



## Operational efficiency

Along with developing the organisational concept of the PZU Group based on customer segments, work is progressing on the back-office model, which will, among other things, help develop a consistent interface between sales, sales handling and operation processing for PZU Group companies. In 2006, work continued on all key initiatives aimed at raising operational effectiveness.

PZU SA and PZU Życie SA are developing the capability of obtaining a uniform image of the customer with regard to products subscribed to, premiums paid and any rebates the customer is entitled to. Both Companies worked to centralize and bring their product systems closer together.

Centralizing the product system, in the case of property insurance, made it possible to access individual customer data and provide service to every customer at any branch outlet in the country. Simultaneously, works are being carried out to deploy a similar functionality for life insurance. Independently of improvements in individual customer service, corporate customer service is being improved by implementing the Corpo system.

## Foreign expansion

In 2006, the PZU Group focused on developing its foreign Companies in Ukraine and Lithuania. The main objectives of its activities were to adjust the product portfolio to customer needs, raise productivity at the level of branch units and head offices of those Companies and optimize management processes. At the same time, works were carried out to adjust the IT solutions to the Companies' needs.

Along with streamlining the handling of sales, works were conducted to optimize the adjustment processes of property and casualty insurance and life insurance. In the case of property and casualty insurance, these have yielded their first effects, namely a cut in the time for adjusting motor losses and tailoring adjustment methods to customer needs (involving the Contact Centre in the loss adjustment process, deploying Mobile Experts, developing a Repair Network co-operating closely with PZU and introducing a centralized IT system supporting every stage of the loss adjustment process). In the field of life insurance, a model for benefit adjustment meeting customer needs and improving the operation by centralizing processes was developed.

In 2006, works on streamlining areas supporting the core business of the companies were carried out. A Finance and Accounting Centre was launched and gradually started taking over the handling of accounting processes in the property and casualty company. Simultaneously, works were conducted to identify and optimize financial and personnel processes for PZU Życie SA.

The PZU Lietuva is in the final stage of financial system implementation and in the midst of rolling out a sales administration system. PZU Ukraine is also implementing a financial system and working on applying an IT system to administer sales, products and claims adjustment.



## Efficient management

In 2006, works in the field of management systems focused on Corporate Governance, IT and HR management. As part of the New Corporate Governance project, the majority of corporate functions were unified at Head Office.

With regard to IT in the company, an organizational model and the rules for supervising IT were developed. A model for cooperation of IT and business was also developed, to ensure efficient communication of needs; the Business and Technology Committee (KBT) was appointed at PZU SA and the IT Steering Committee at PZU Życie SA.

In the human resources area, works continued to optimize personnel processes and update HR management tools, which included the implementation of management by an objectives system for the managerial staff of the Group. Steps were taken to implement the Employee Pension Programme for all Group staff. In addition, the centralization of personnel and payroll processing in both the property and casualty companies and the life company continued to progress.

## 12.2 New Corporate Governance

2006 was the first complete year of operations of the unified offices ] of PZU SA and PZU Życie SA, the establishment of which was brought about by integration activities carried out as part of the New Corporate Governance (NCG) project. Areas of shared services were introduced within the PZU Group, which cover purchasing organization, marketing, supplies, real estate management, asset management, personnel management and services for statutory bodies. The opportunities for integrating further areas of shared services and corporate functions are being analysed. These steps are bringing the Group closer to the planned goals of improving cost synergies, thus making better use of the Group's potential and achieving greater savings.

Due to the lack of interpretation as to the legality of raising the equity of an insurance company by contribution in kind, PZU SA decided to apply to suspend proceedings to grant PZU Majątek SA permission to run an insurance business; the latter is a company that was supposed to take over the insurance business of the current PZU SA. This led to a halting of work aimed at transforming the PZU Group into a two level holding structure. A review of the NCG Project was performed.



## 12.3 Foreign investments of PZU Group

The PZU Group started its insurance business on foreign markets in February 2002. Currently, the portfolio of foreign companies of PZU SA is comprised of two insurance companies in Ukraine and two insurance companies in Lithuania.

In 2006, the PZU Group focused mainly on developing its existing foreign investments in Ukraine and Lithuania as well as improving the methods of managing international operations. In this field, the PZU Group has set itself the goal of turning its foreign companies into efficient operators on developing markets, which use modern technologies, meet customers needs by developing the product range and

offering the highest quality of service, thus creating stable value for their shareholders.

Once it has developed an effective and efficient model of cooperating with foreign companies, based on the one hand on analysing their operations and on the other on transferring its know-how and experience, the PZU Group may consider further acquisitions and operational expansion onto other Central and Eastern European markets.

### 12.3.1 Operations of UAB DK PZU Lietuva and UAB PZU Lietuva Gyvybės Draudimas

To raise its rate of return, UAB DK PZU Lietuva hiked its premium ratings in 2006 to a level among the highest on the market. Regardless of its difficult financial standing, mainly due to events in previous years, the insurance portfolio quality improved markedly.

The Company is currently launching a new system of sales and product maintenance and is near to completing implementation of the financial system, which will make interim reporting much easier.

### Financial results and market positions of UAB DK PZU Lietuva and UAB PZU Lietuva Gyvybės Draudimas

#### UAB DK PZU Lietuva

**Gross premiums written** in 2006 amounted to LIT 114 million and were 5% higher than the premium collected in 2005 (LIT 108.7 million).

**Net profit** of 2006 reached LIT 29.2 million, compared to LIT 9.8 million in 2005.

**Market share** as of the end of 2006 was 12.7%, making the company the third largest property and casualty insurer in Lithuania.





## 12.3.2 Operations of OJSC IC PZU Ukraine and OJSC IC PZU Ukraine Life Insurance

### UAB PZU Lietuva Gyvybės Draudimas

**Gross premiums written** in 2006 amounted to LIT 9.3 million, 21% up on 2005 (LIT 7.7 million of premiums collected).

**Net profit** of 2006 amounted to LIT 3.9 million compared to LIT 4.4 million in 2005.

**Market share** as of the end of 2006 was 2%, giving the company the seventh position in the Lithuanian life insurance market.

The PZU Ukraine group of companies is currently at an advanced stage of restructuring. Products have been made more profitable by introducing new ratings and changing the general terms and conditions of insurance. A network of agents is being built: as of 31 December 2006 there were 1,176 agents working for the Companies on a cross-selling basis (agents sell both property and casualty and life products). The existing network of branches covers the entire Ukrainian territory, so customers from all regions of the country can access the offer. Steps are being taken to improve the quality of loss adjustment, also by implementing a specialized IT system. PZU Ukraine companies also plan to launch a new, universal product system.

### Financial results and the market position of OJSC IC PZU Ukraine and OJSC IC PZU Ukraine Life Insurance

#### OJSC IC PZU Ukraine

**Gross premiums written** in 2006 totalled UAH 184.3 million, 55% more premiums than were collected in 2005 UAH (118.9 million).

**Net profit** of 2006 amounted to UAH -88.9 million\* against UAH 26.6 million in 2005

**Market share** reached 4.5% at the end of 2006, growing by 0.4 p.p. since the end of 2005 (4.1%)

#### OJSC IC PZU Ukraine Life Insurance

**Gross premiums written** in 2006 totalled UAH 11.2 million, up 71% on premiums collected in 2005 (UAH 6.5 million).

**Net profit** of 2006 amounted to UAH -8.5 million against UAH -3.1 million in 2005.

**Market share** reached 2.5% at the end of 2006, growing by 0.5 p.p. since the end of 2005 (2%).

\* As shown in the individual statements of OJSC IC PZU Ukraine executed in accordance with Ukrainian Accounting Standards. According to the Polish Accounting Standards, the net result was UAH -115.4 million.





## 12.4 Development projects and the main objectives of PZU Group companies in 2007

The PZU Group aims at maintaining its status as a leading financial institution in Poland and Central and Eastern Europe as well as at strengthening its market position by maintaining growth of revenues from the main business line, and in particular reducing the gap between the growth rate of PZU SA's insurance premium and the entire insurance market in Poland.

In 2007, PZU SA takes steps to reduce claims and thus retain the basic lines of motor insurance – own motor damage and theft and motor third party liability insurance – which are highly profitable and will have a major impact on the financial result of the Company. PZU SA is a leader in this regard both in terms of revenues and underwriting results. The steps taken in 2006 and planned for 2007 are aimed at maintaining the dominant position of PZU SA in this market

segment while retaining a high rate of return, as in previous years. In this insurance product group, written premiums in 2007 should be kept at a level similar to those achieved in 2006.

With regard to the remaining insurance lines, written premiums are forecast to grow while claims should be kept relatively low. The main groups of insurance products generating growth will be the remaining property and casualty insurance and non-motor liability. It is also planned that financial insurance operations will grow significantly in scale in 2007. Due to steps taken in relation to non-motor insurance, PZU SA should report an almost 1.9% growth in premiums written for direct insurance in 2006, regardless of the projected almost 0.6% drop of this premium for motor insurance.

Various actions are planned in 2007 to streamline the customer management of the Company and cut operating costs. The main steps in this area will include:

- Continued reorganization of the loss adjustment process of PZU SA by extending reforms to cover the processes of adjusting non-motor claims,
- Continuing the process of establishing the PZU SA Financial and Accounting Centre,
- Developing and rolling out systems helping PZU agents to acquire insurance and optimize settlements between the agent and the PZU,
- Continuing the process of organizational changes with regard to financial insurance,
- Developing tools that support insurance cross-selling addressed to customers of PZU SA,
- Implementing sales support software in the corporate insurance segment (the Corpo system) and in financial insurance,
- Keeping costs under control, particularly overheads related to the current operations of PZU Group companies.



In 2007, a package of projects will be launched aimed at raising the sales of PZU SA products, mainly by making the basic distribution channel, i.e. the agent network, more active. Activities planned as part of this package include:

- Launching a new product training programme,
- Developing an agent development programme, ,
- Developing a model to acquire experienced agents from competitors,
- Extending cooperation with car dealership networks,
- Streamlining the sales administration process.

In the longer term, these activities should yield measurable financial benefits, namely improved results of insurance acquisition and a cut in the cost of processing insurance acquisition and loss adjustment, while maintaining the safety ratios.

2007 will see further dynamic growth in the product offering of PZU Życie SA, across all sales channels, focused on medium net worth and mass customers through all delivery channels, as part of both group and individual insurance.

In 2007, it is also planned to undertake activity in the segment of corporate customers and continuing individual customers, aiming to maintain PZU Życie SA's strong position on the group insurance market. These will include, in particular:

- Continuing customer segmentation activities,
- Developing and launching the Rejestrator tool to support electronic processing of group life insurance, which will ultimately allow a discontinuation of paper documents,
- A changed approach to the sales process with the aim of streamlining the processes of entering into and servicing group insurance as well as improving customer service quality. Due to the package sales of insurance, documents necessary to conclude contracts and insurance maintenance forms will be simplified,
- Implementing a tool helping to build on the spot offers at the employer, thus making the process of concluding insurance contracts more flexible,
- Activities aimed at increasing sales of new products launched by the Company in 2006,
- A development of the product offering – mainly new riders.



Preparations are under way to extend the offer addressed to customers with individual continuations of group covers: the launch of a new rider is planned.

Further mailing campaigns are planned for 2007, which will involve the mailing of offers for individual continuation customers, as well using other channels aimed at reaching the target groups with insurance offers, e.g. via the hotline.

To improve the supervision of concluding individual continuation insurance policies and the insured flow, a project for the central entry of contracts of individually continued (IC) insurance is being prepared. Centralizing ICs will support the offering of individually continued insurance without the need for direct contract with the customer's point of sale, saving the time both of consumers and employees.

It is planned in 2007 to improve the competitive position of PZU Życie SA in the individual insurance sector by expanding its offer of coverage products, investment products and Individual Pension Accounts, finding new delivery channels, as well as extending and improving the throughput of traditional channels.

Work on developing product range is focused on development of offers for medium net worth consumers. These offers are being extended with several sales channels in mind:

the agent network, the customer service branch network and third-party networks. The product can be offered at the same time via different sales networks.

Health insurance products will change rapidly due to increasing competition, deterioration of the public health service and increasing customer expectations. PZU Życie SA will develop key product competencies: it will offer a varied range of medical services, extend and integrate the network of service providers, provide customers with high quality medical services and customer service, and it will monitor quality. In 2007, this will apply to outpatient, hospital and assistance products.

The PZU Group maintains its bancassurance plan ambitions for 2007. PZU Życie SA intends to pursue them by continued cooperation with strategic partners and activities leading to new acquisitions.

PZU Życie SA will work to develop modern and interesting solutions within its insurance range and the accompanying processes to match increasing demands of bank customers. The main drive will be to develop a modern and attractive range of investment insurance. Development of those products is to a great extent dependent on agreements with partner banks.

In 2007, the Company will continue development in the directions laid out in the strategy of the PZU Group. The following activities will be of key importance to the development of PZU Życie SA:

- Continued restructuring of the Company and of available IT resources,
- Further work to develop and improve the efficiency of the sales structure, e.g. by continuing efforts to revive the agency network with particular emphasis on customer segmentation,
- Adapting the Company to meet international operating standards with regard to financial reporting and capital management (Solvency II),
- Further work to implement an integrated corporate IT system, both in terms of software and upgrading the hardware infrastructure.



# 06

## 13. The financial performance of PZU Group companies

### 13.1 Gross premiums written

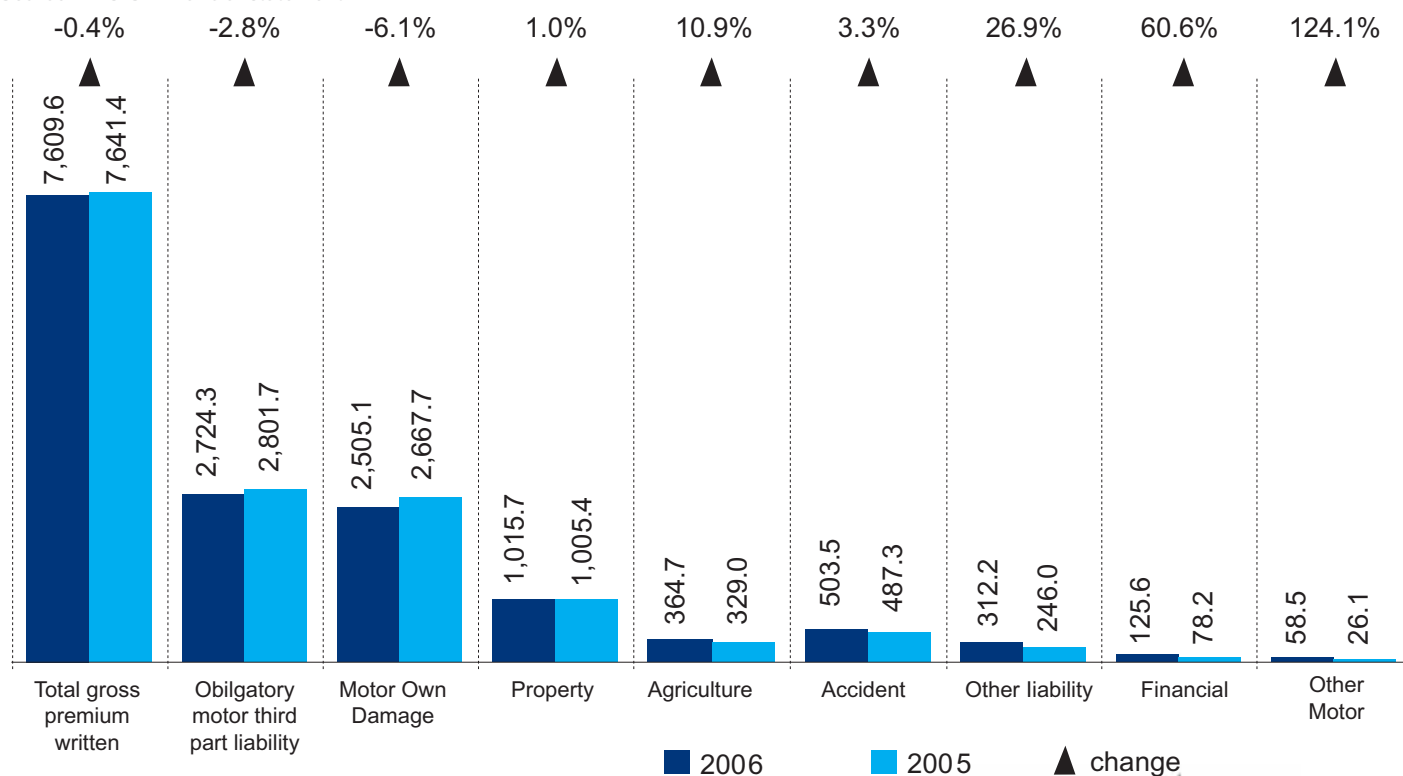
Gross premiums written by the PZU Group for life insurance as well as property and casualty insurance, after consolidation adjustments, amounted to PLN 15,454.1 million in 2006, and was 12.4% higher than in 2005.

Total gross premiums written by PZU SA amounted to PLN 7,677.4 million in 2006, which represents a growth of 0.3%. Written premiums for direct insurance was only PLN 7,609.6 million. Motor insurance still formed the dominant item in the

PZU SA portfolio, representing direct insurance, accounting for 69.5% of written premiums, a drop of 2.4 points on 2005. The proportion of other liability insurance grew significantly (by 0.9 points) in the breakdown of written premium compared to 2005, as did the proportion of agriculture insurance (0.5 points). The share of financial insurance grew from 1% to 1.7% of total premiums. Property and casualty insurance accounted for 13.3%, while accident and health insurance represented 6.6% of total written premiums.

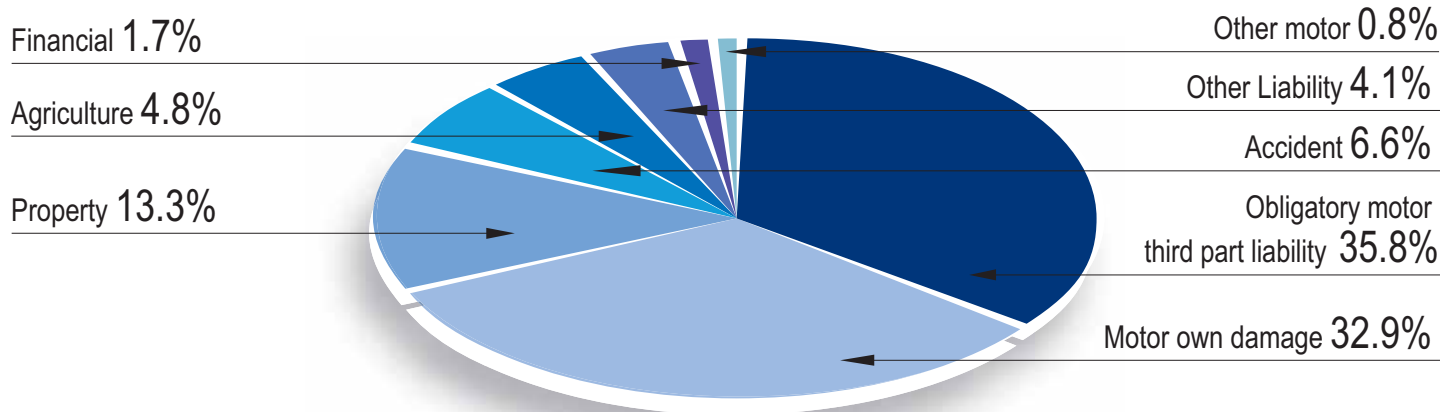
#### Gross premiums written by PZU SA for direct insurance broken down into main insurance groups (in PLN million)

Source: PZU SA financial statement



## Gross premiums written by PZU SA for direct insurance broken down by main insurance groups as of 31 December 2006

Source: PZU SA financial statement



Gross premiums written by PZU SA for inward reinsurance totalled PLN 67.7 million in 2006.

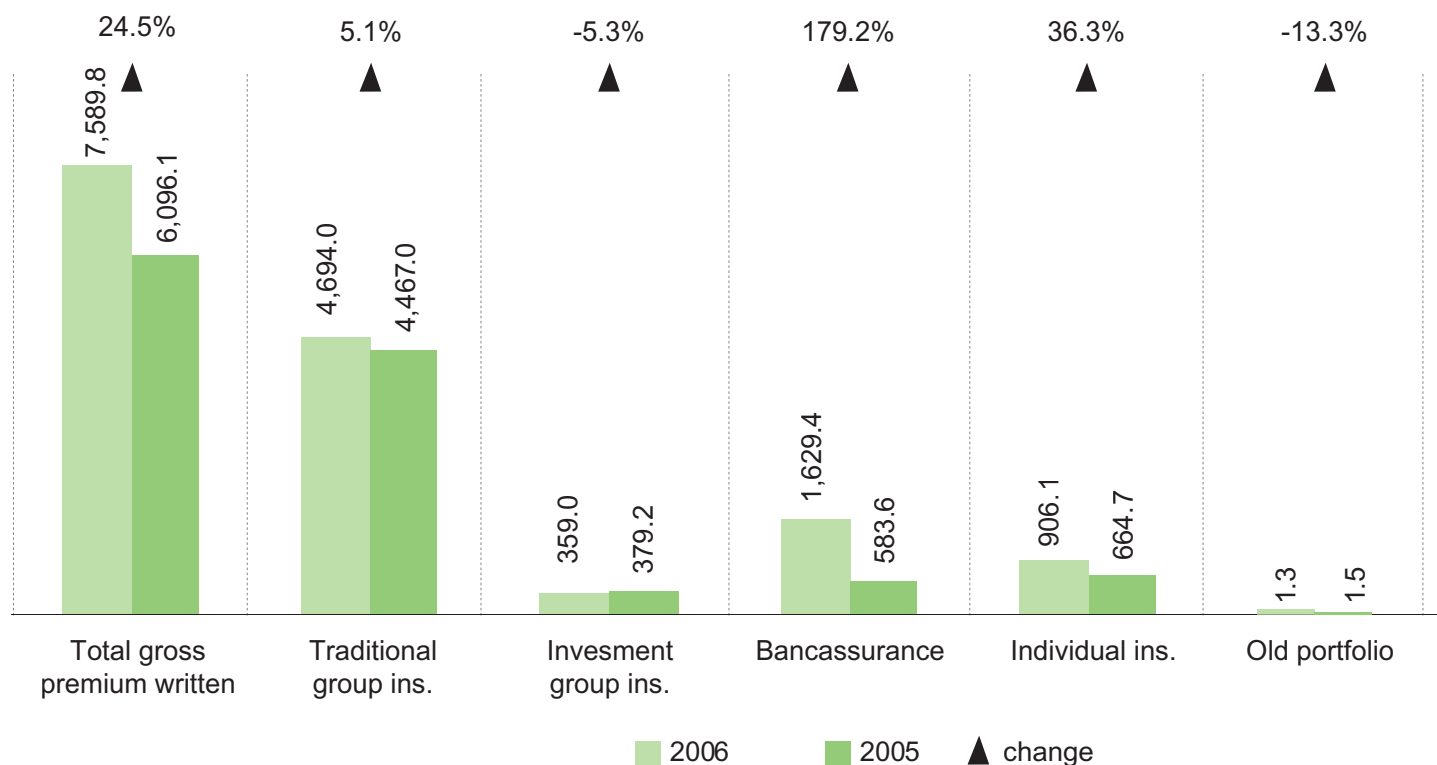
The number of insurance contracts concluded by PZU SA rose by 6.4% to 43,969.7 thousand. The premiums averaged PLN 173.1, 6.4% less than in 2005.

Gross premiums written by PZU Życie SA in 2006 amounted to PLN 7,589.8 million, representing a 24.5% growth on 2005. Just as in the previous period, the fastest growing products were bancassurance (up 179.2% and PLN 1,045.8 million). Written premiums for traditional group insurance rose by 5.2%. An increase of 36.3% was reported in individual insurance. On the other hand, premiums for group investment insurance shrank by 5.3%.



## Gross premiums written by PZU Życie SA broken down by main insurance groups (in PLN million)

Source: PZU Życie SA financial statement



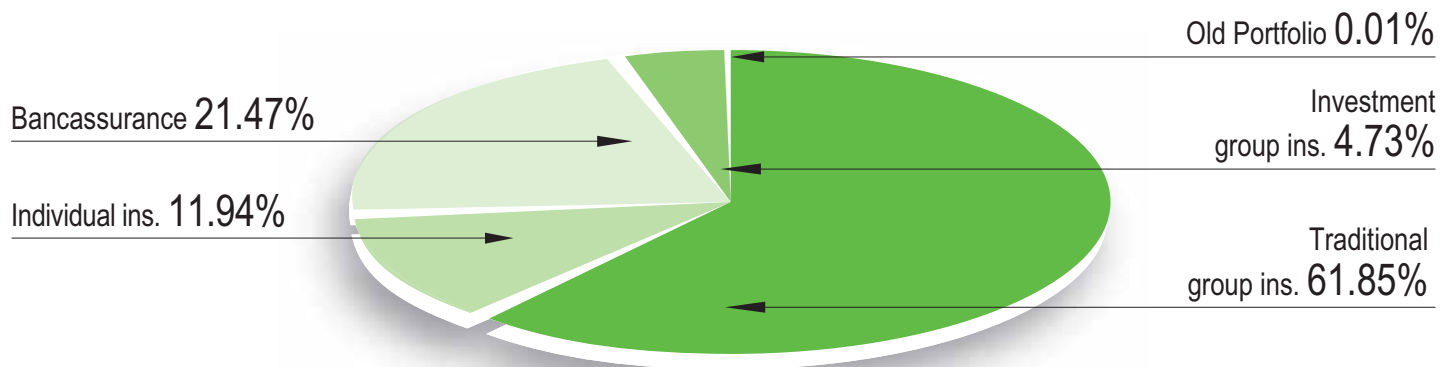
As in previous years, traditional group insurance accounted for the highest proportion in the breakdown of the premiums of PZU Życie SA, as its total written premium represented 61.9% of total premiums. Individual insurance accounted for

11.9% of total written premiums. Bancassurance grew compared to 2005. Its share as of the year-end 2006 amounted to 21.5%.



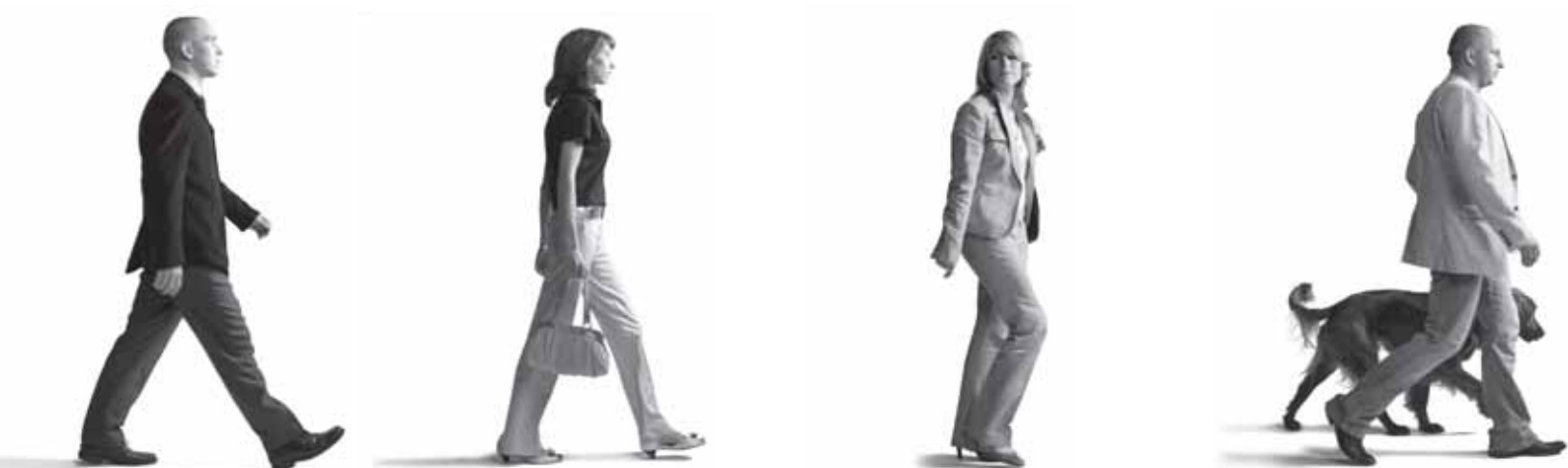
Gross premiums written by PZU Życie SA broken down by main insurance groups as of 31 December 2006.

Source: PZU Życie SA financial statement



Regardless of the reduction in the number of risks for traditional and investment group insurance and for the old portfolio (closed portfolio), customers insured with PZU Życie SA

stood at 13,837 thousand, an increase of 301,000 on 2005. This was due to the increase in the number of individual risks and bancassurance.





## 13.2 Claims and benefits

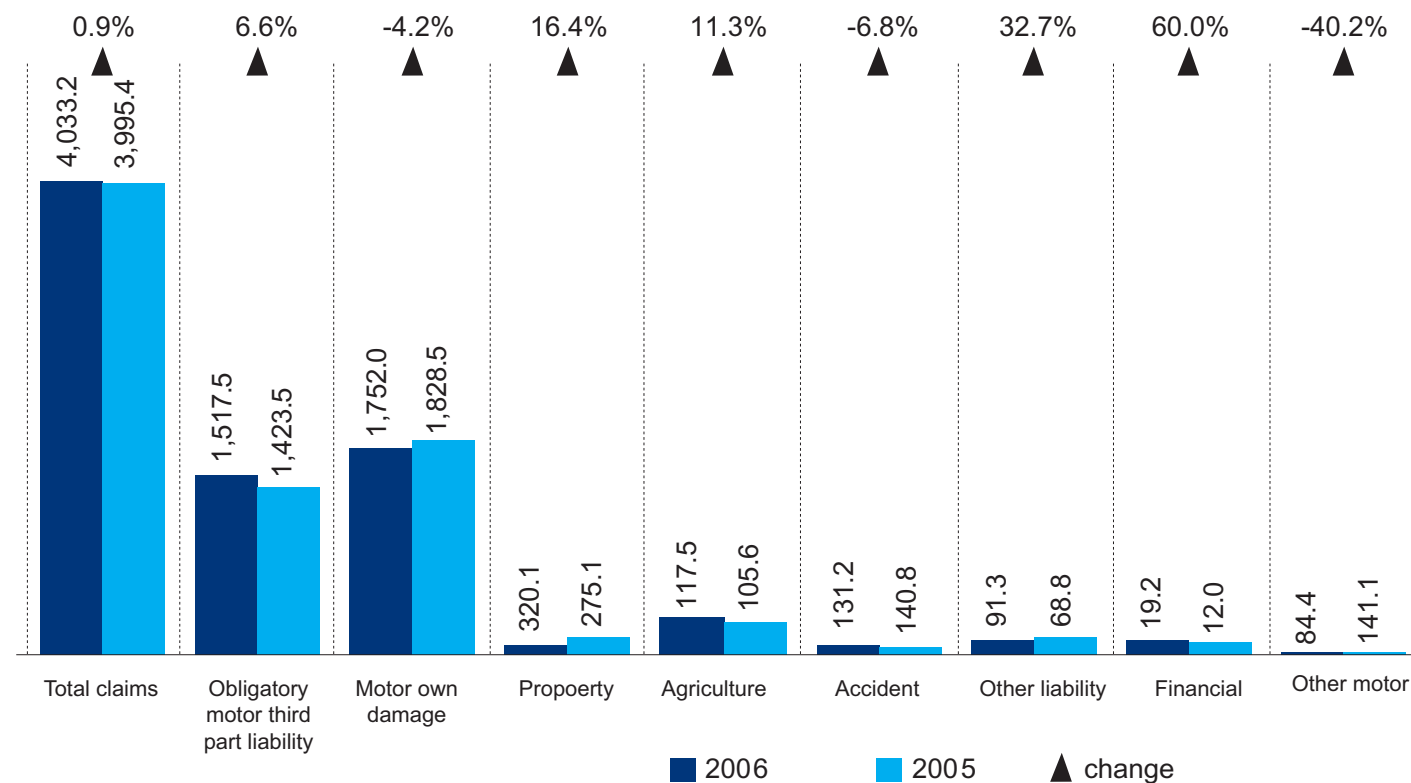
Gross claims and benefits paid out by the PZU Group in 2006 totalled PLN 8,775.4 million, 6% more than was paid out in 2005.

Gross claims and benefits paid by PZU SA, including loss adjustment expenses, amounted to PLN 4,368.4 million

in 2006, of which the payments themselves in virtue of gross claims and benefits under direct insurance (excluding loss adjustment expenses) accounted for PLN 4,033.2 million. This represents an increase of 0.9% on 2005. Claims fell in the following insurance classes: own motor car damage, other motor insurance and accident.

Gross claims and benefits paid by PZU SA under direct insurance (excluding the cost of adjustment and recourses) broken down by main insurance groups (in PLN million)

Source: PZU SA financial statement

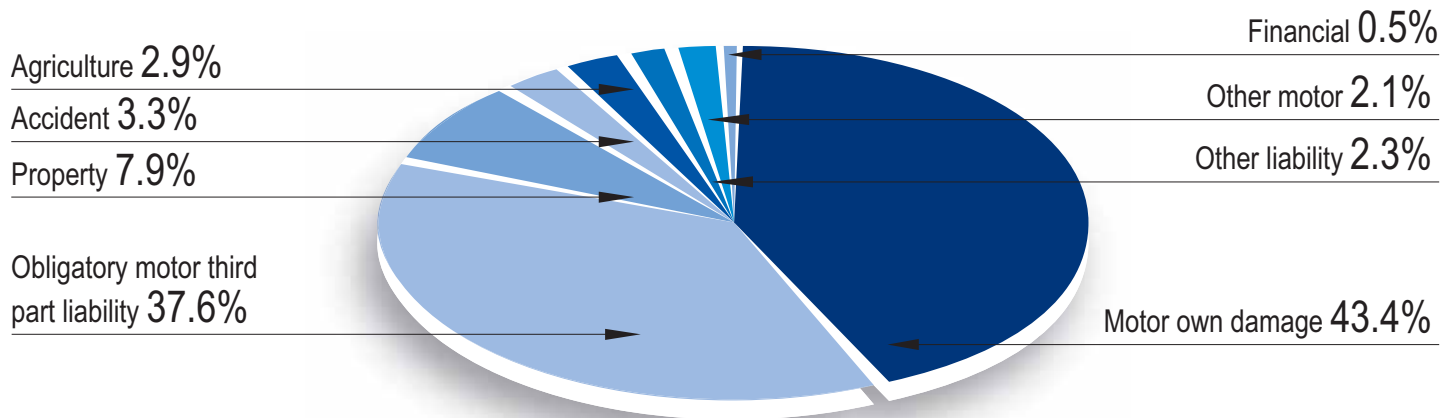


No significant changes were reported in the breakdown of claims and benefits paid by PZU SA compared to 2005. As usual, motor insurance dominated with 83.1% of total pay-

ments. Payments under property insurance accounted for 7.9% of the total, with accident insurance at 3.3% and agriculture at 2.9%.

Breakdown of gross claims and benefits paid by PZU SA under direct insurance (excluding adjustment costs and recourses) by main insurance groups as of 31 December 2006.

Source: PZU SA financial statement

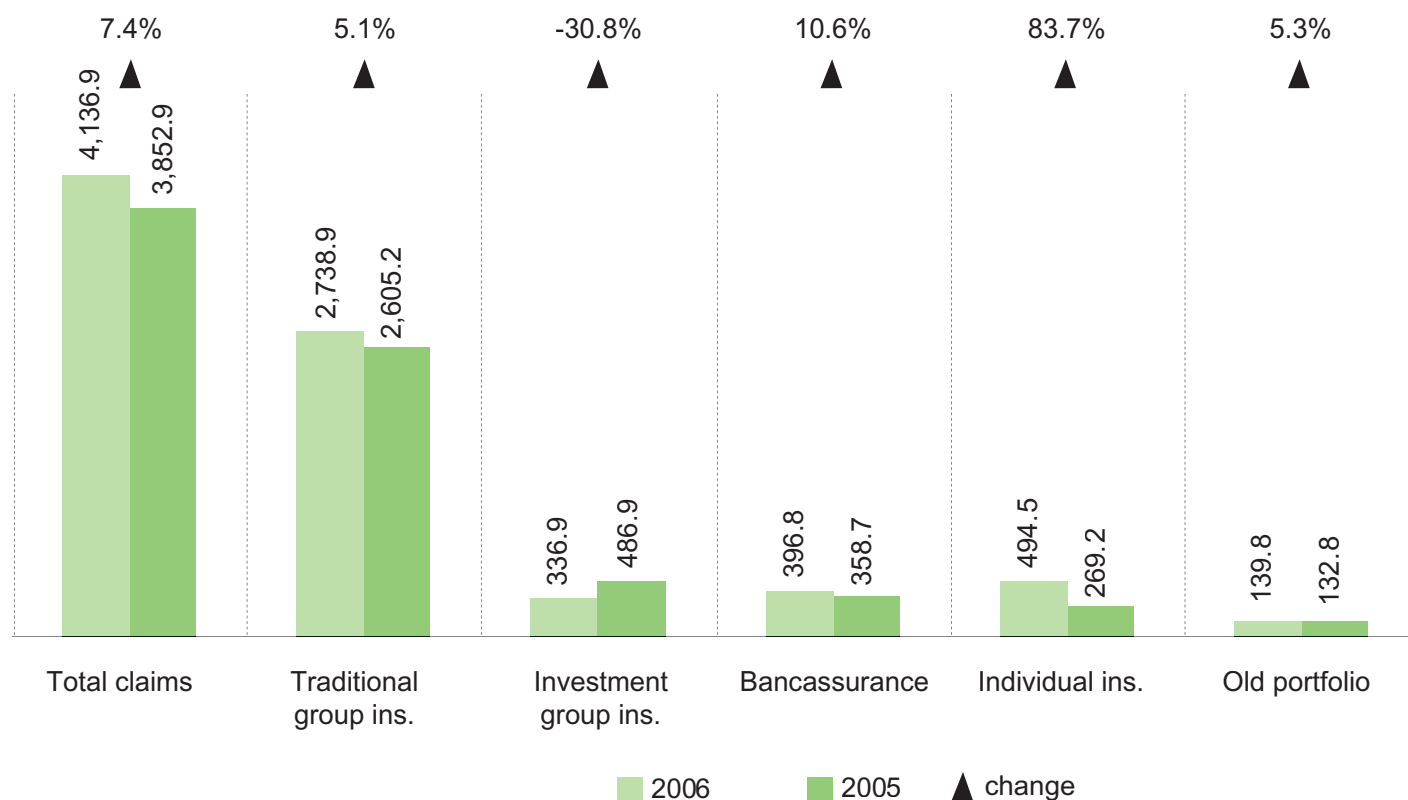


There were 1,311.6 thousand claims paid out by PZU SA, 0.2% more than in 2005. The value of the average claim paid was PLN 2,986.6, 0.5% more than in 2005. The direct costs of loss adjustment incurred by PZU SA in 2006 totalled PLN 430.1 million, 5% more than in the previous year.

On account of gross claims and benefits, PZU Życie SA paid PLN 4,276 million in 2006, 7.4% more than a year earlier. The cost incurred by PZU Życie SA on account of paying benefits net of reinsurer's share reached PLN 4,276 million against PLN 3,980.7 million in 2005, meaning growth of 7.4%. However, the increase in benefits paid out was low compared to the growth of written premiums, which went up 24.5%. PZU Życie SA paid a net amount of PLN 4,135.9 million in benefits in 2006.

## Net claims and benefits paid by PZU Życie SA broken down by main insurance groups (in PLN million)

Source: PZU Życie SA financial statement

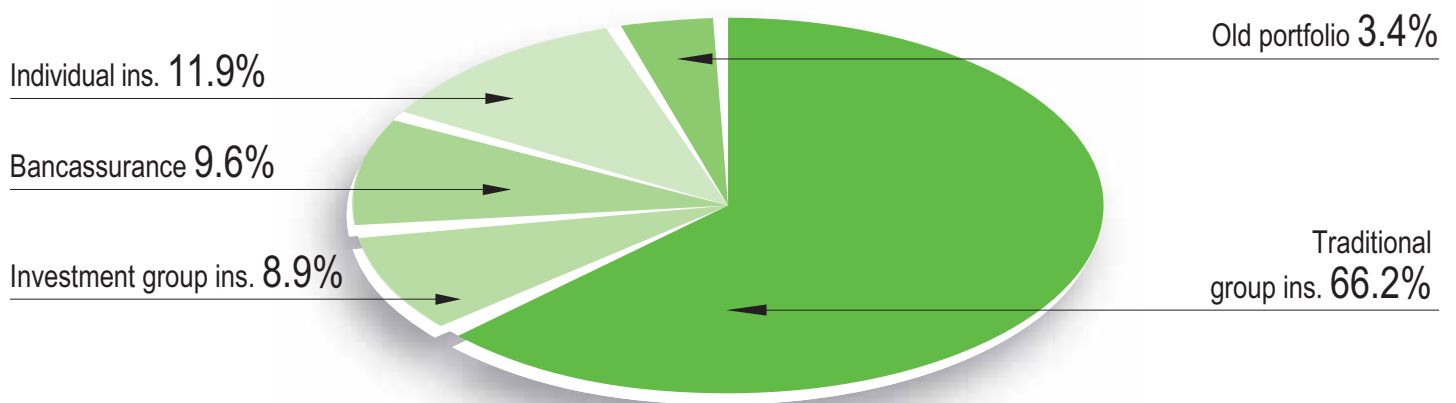


In 2006, as in the previous year, the highest proportion in the structure of net claims and benefits was that of protective employee insurance (66.2%) and of individual

insurance (11.9%). The proportion of banking insurance rose to 9.6% at the end of 2006.

Breakdown of net claims and benefits paid by PZU Życie SA into main groups of insurance as of 31 December 2006.

Source: PZU Życie SA financial statement



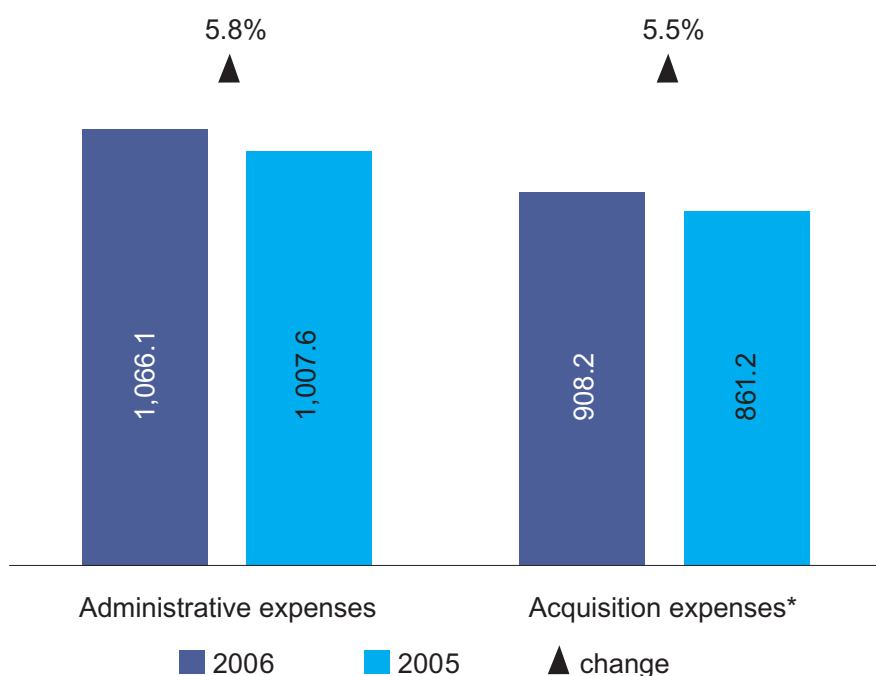
## 13.3 Cost of insurance activities

The costs of the PZU Group's insurance activities, which include acquisition expenses and administrative costs incurred in 2006, amounted to PLN 2,952.9 million, up 9.6% on 2005.

In the same period, PZU SA's insurance activities costs totalled PLN 1,974.3 million, an increase of 5.6% on the previous year.

### Insurance activities costs of PZU SA split into administrative expenses and acquisitions expenses (in PLN million)

Source: PZU SA financial statement



\* reinsurers' commissions and the share in reinsurers' profits were deducted from acquisition expenses.

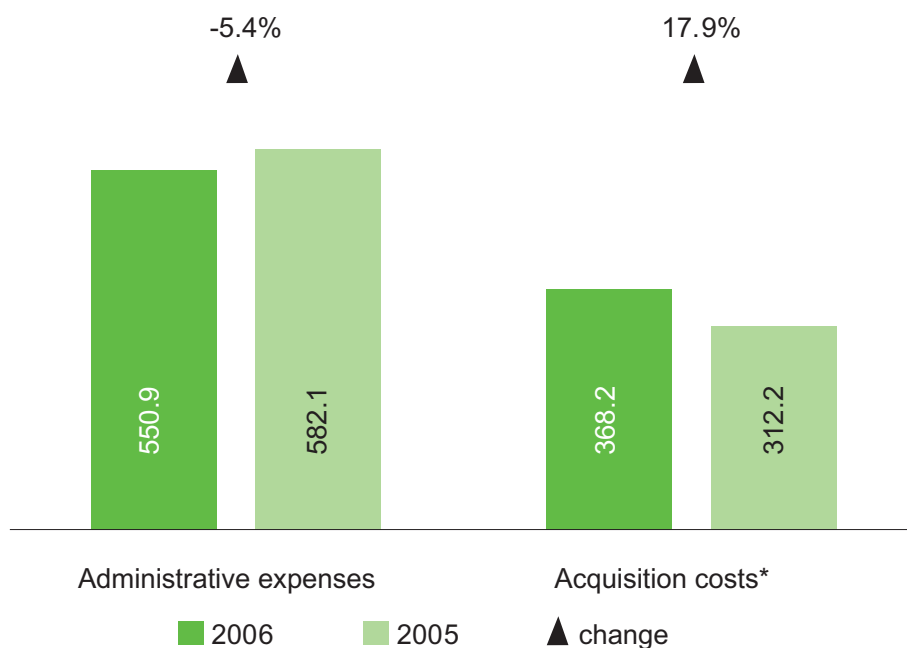


The ratio of insurance activities costs to the gross premiums written by PZU SA in 2006 was 25.7%.

After allocation, the costs of insurance activities of PZU Życie SA amounted to PLN 919.1 million in 2006, a growth of 2.8% on 2005. Administrative expenses fell and amounted to PLN 550.9 million at the end of the period discussed here (down 5.4%). Compared to 2005, the acquisition expenses rose by 17.9%.

## Insurance activities costs of PZU Życie SA split into administrative expenses and acquisitions expenses (in PLN million)

Source: PZU Życie SA financial statement



\* reinsurers' commissions and the share in reinsurers' profits were deducted from acquisition expenses

The ratio of insurance activities costs to the gross premiums written by PZU Życie SA rose in 2006 compared to the previous year. At the end of 2006, that ratio stood at 14.7%.



### 13.4 Underwriting results

The gross underwriting results of the PZU Group transferred into the consolidated profit and loss account at PLN 3,577.2 million in 2006, a rise of 35.9% on 2005.

A significant growth in the underwriting result was reported by both insurance companies of the PZU Group, mainly as a result of:

- An increase in written premiums in both insurance segments,
- Optimization activities in property loss adjustment,
- Changes in the reinsurance protection,
- Keeping the costs of running the core business line under tight control.

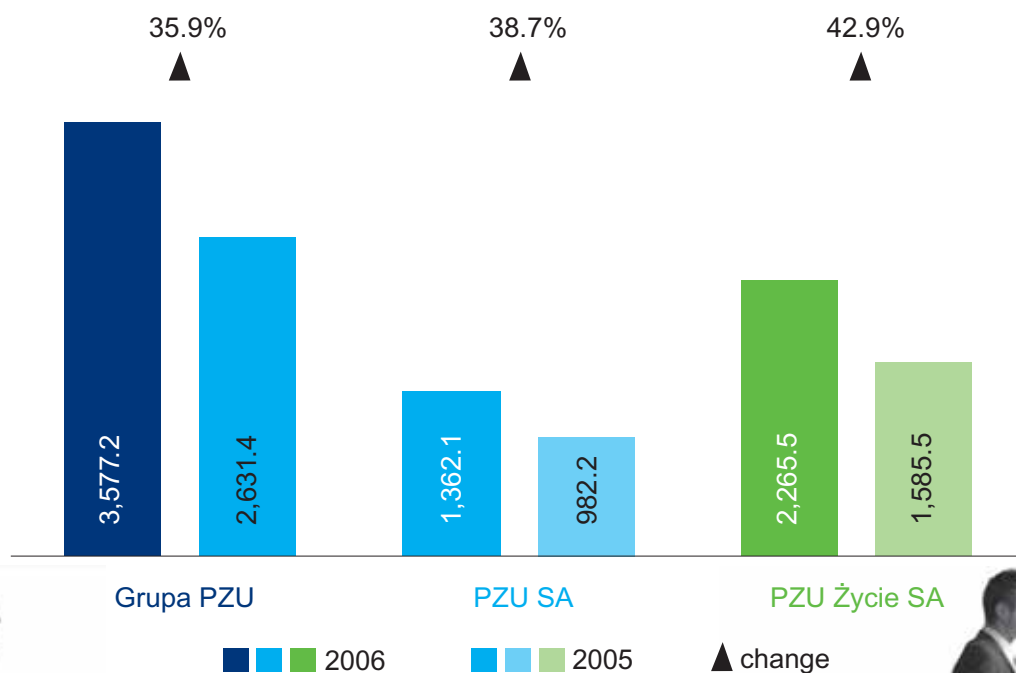
PZU SA achieved an underwriting result of PLN 1,362.1 million in 2006. This represented a huge jump of 38.7% on the previous year and was mainly the result of changing the reinsurance program for 2006 (reducing proportional protection in motor insurance), lower costs of reserves and a lower loss ratio than in previous years.

Positive underwriting results were reported in all major insurance groups with the exception of other motor insurance products.

PZU Życie SA also reported a huge upswing in its underwriting result (which went up by 42.9%), taking it to a level of PLN 2,265.5 million. The main drivers lifting results so high were the increase in gross premiums written and a very good result on investment activities.

Underwriting results of PZU Group, PZU SA and PZU Życie SA (in PLN million)

Source: The PZU Group financial statements





## 13.5 Investment activity

In 2006, as in preceding years, the PZU Group's investment activities were oriented towards finding the right match between asset and liability structures, maintaining a required level of security, profitability and liquidity of investments. **The balance of PZU Group's investments as of year-end 2006 amounted to PLN 43,453.1 million (excluding net assets of unit-linked policies worth PLN 3,161.7 million), which represents a 12.2% increase on 2005.**

The PZU Group's investment income reached PLN 3,286.3 million, which constitutes a 4.3% drop on the previous year. In 2006, investment activities of the Group companies were mainly focused on securities issued by the State Treasury, i.e. T-bonds and T-bills. At the end of the year, these instruments represented 60.1% of the total investment portfolio value, compared to 59.8% as of year-end 2005, while at PZU Życie SA they accounted for 71.2% of the investment portfolio value against 79.2% at the end of 2005.

The Companies were also active on the listed share market. The percentage of listed equities in the PZU SA investment portfolio shrank from 7.6% in 2005 to 7.4 in 2006 but exposure grew by value. The percentage of listed equities in the investment portfolio of PZU Życie SA slid from 8.7% at the end of 2005 to 7.6% at year-end 2006.

The large proportion of unlisted equities in PZU SA's investment portfolio was mainly represented PZU Życie SA's shares held in that portfolio, which were valued at PLN 4,517.3 million as of 31 December 2006 (this represented 95.5% of the value of the unlisted share portfolio of PZU SA). The proportion of unlisted equities moved up slightly in 2006 to 19.7% (against 19.8% in 2005), while their value grew. This was mainly due to the higher valuation of PZU Życie SA shares.

2006 saw a decrease in PZU SA's exposure to non-treasury debt securities. Their share dropped from 2.2% at year-end 2005 to 1.3% at year-end 2006.

The value of term deposits (deposits and repos) at the end of 2006 constituted 9.7% of the total value of PZU SA's investment portfolio (against 8.6% in 2005).

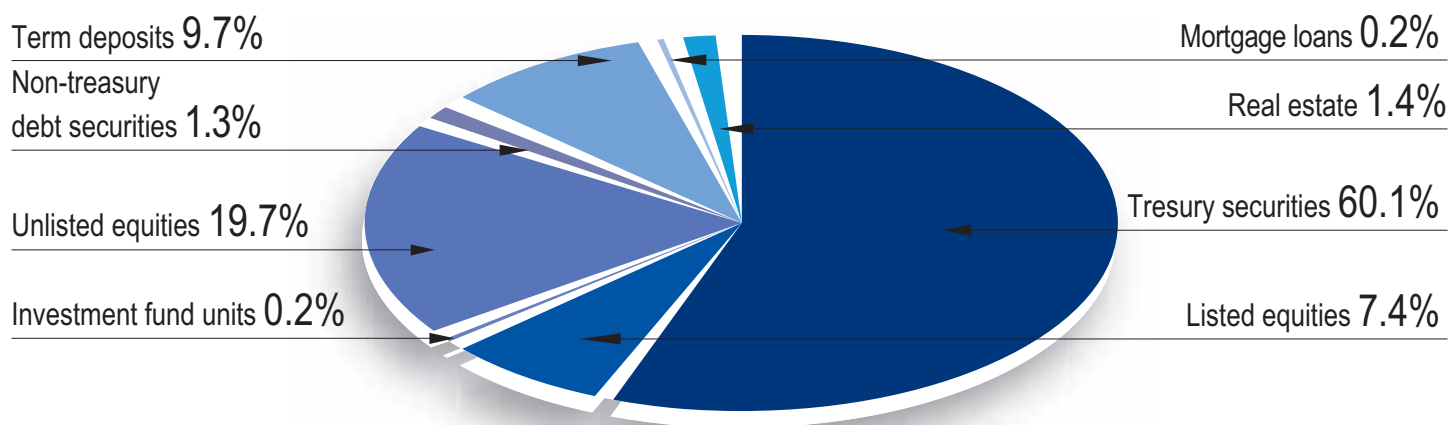
The percentage shares of other types of investments did not change significantly compared to the end of 2005.

**In 2006, the income on PZU SA investment activities amounted to PLN 2,583.8 million, 11.8% more than in 2005. This growth in 2006 was to a significant extent the result of the dividend received from PZU Życie SA, worth PLN 1,405.2 million (compared to PLN 956.1 million in 2005). The result on PZU SA's investment activities for 2006 excluding the dividend from the life insurance company amounted to PLN 1,178.6 million, 13% less than a year earlier.**



## Breakdown of PZUSA's investment portfolio as of 31 December 2006

Source: PZU SA



Exposure to non-treasury debt securities shrank slightly in PZU Życie SA's investment portfolio in 2006. Its proportion fell from 1.1% at the end of 2005 to 1% at the end of 2006. A similar, insignificant change was observed in the proportion made up of unlisted equities in PZU Życie SA's investment portfolio, which decreased from 3.5% at the end of 2005 to 3.3% at the end of 2006.

The proportion of term deposits (deposits and repos) grew: at the end of 2006, they represented 13.1% of the overall

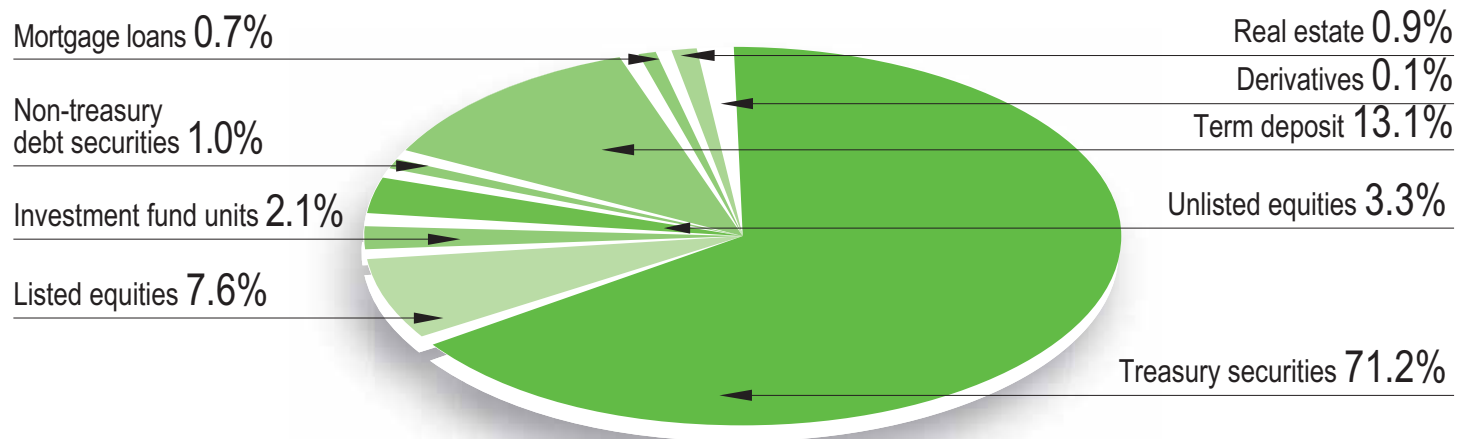
value of the investment portfolio of PZU Życie SA (compared to 3.9% in 2005). An increase was also reported for investment fund units (up from 1.9% in 2005 to 2.1% in 2006).

In 2006, PZU Życie SA achieved PLN 2,171.6 million in investment income, an improvement of 3.6% on 2005 (including investments at the risk and on account of the policyholder).



## Breakdown of PZU Życie SA investment portfolio as of 31 December 2006.

Source: PZU Życie SA

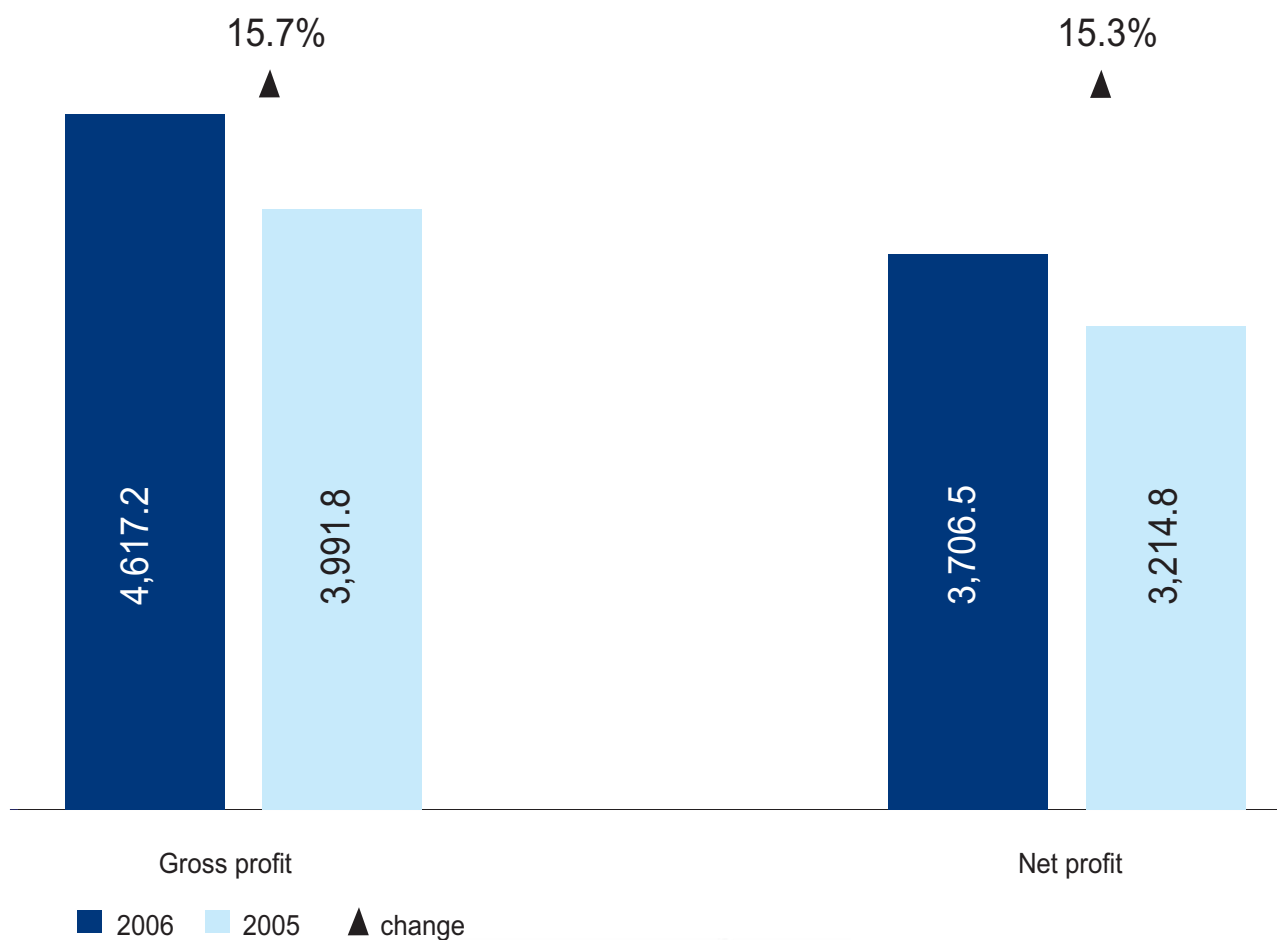


## 13.6 Financial result

In 2006, the PZU Group achieved PLN 4,617.2 million in consolidated gross profit, a significant growth of 15.7% as compared to 2005. Net profit at the end of the period discussed herein amounted to PLN 3,706.5 million.

### Financial results of PZU Group (in PLN million)

Source: The PZU Group consolidated financial statement

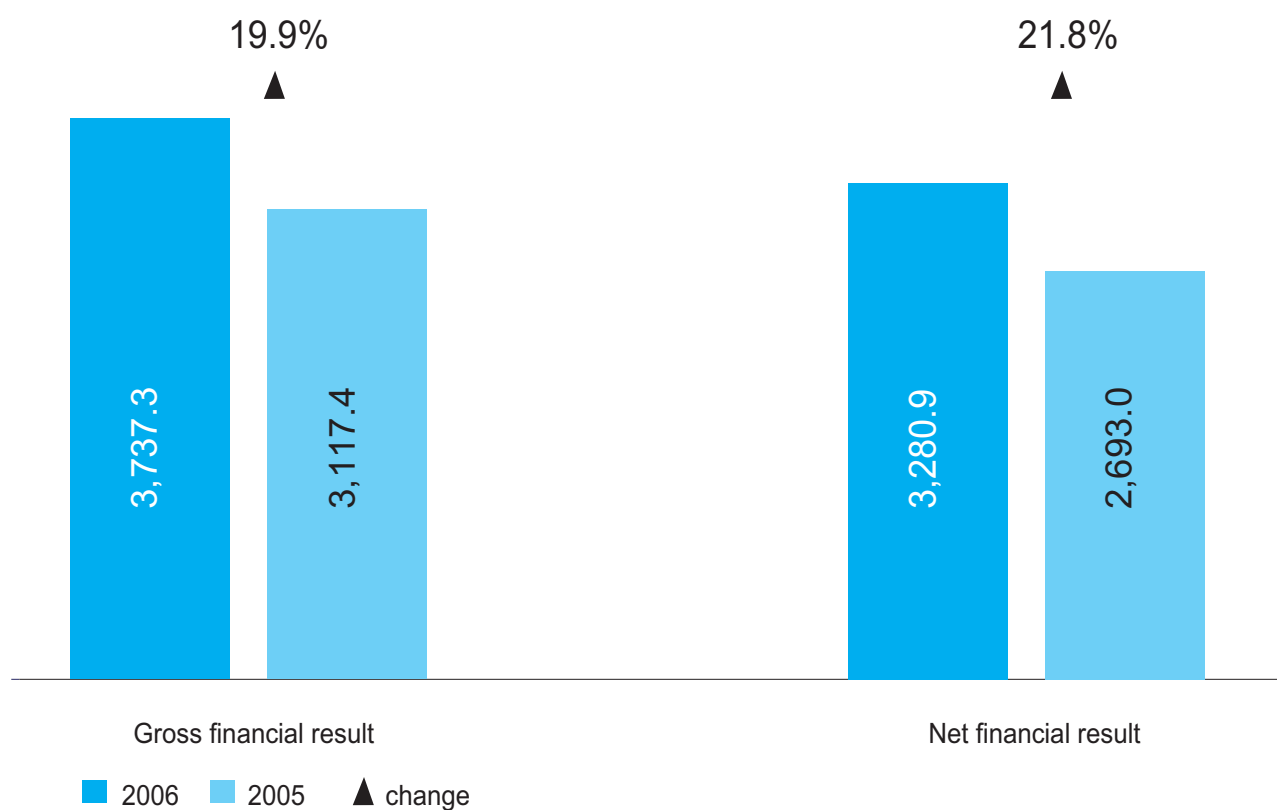


PZU SA generated PLN 3,280.9 million of net profit in 2006, 21.8% more than a year earlier. A significant part of this result was the dividend (of PLN 1,405.2 million) paid out of the profit of PZU Życie SA for 2005. The net profit of PZU SA excluding the dividend of PZU Życie SA amounted to PLN

1,875.7 million at the end of this period: an increase of 8% on 2005. The two main drivers of such a significant improvement in the financial result of the Company were soaring underwriting results and the exceptionally good result on investment activities.

## Financial results of PZU SA (in PLN million)

Source: PZU SA financial statement

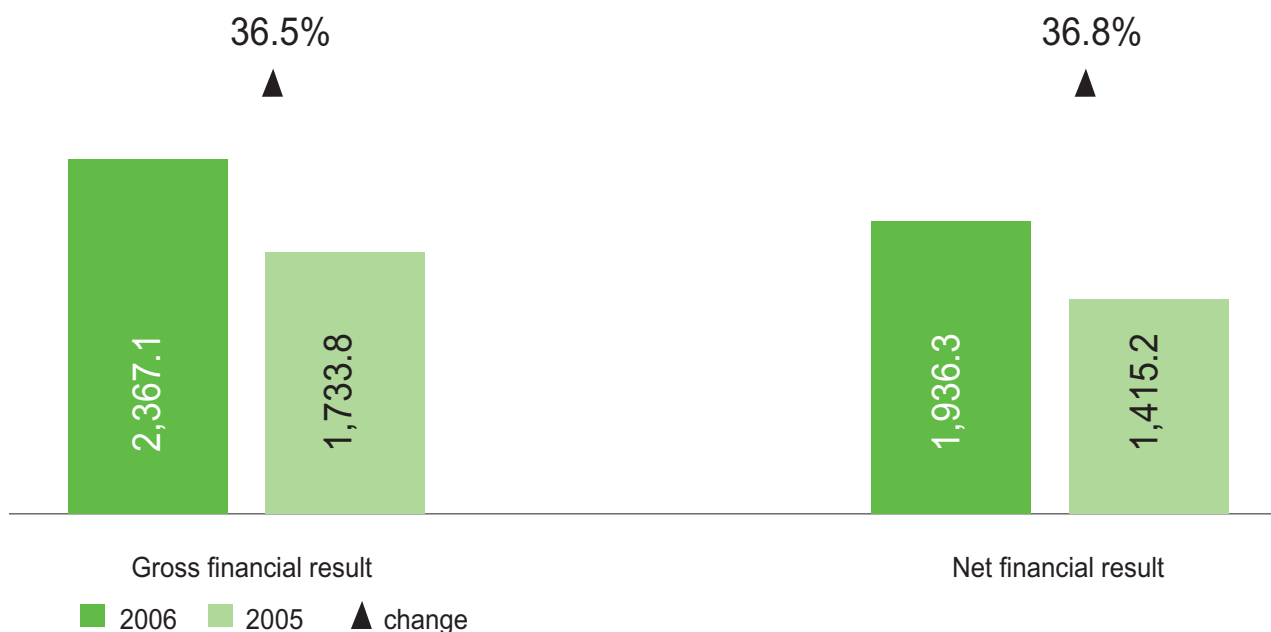


Net profit achieved by PZU Życie SA at the end of 2006 amounted to PLN 1,936.3 million, 36.8% more than in 2005.

Such a marked improvement in financial results was mainly due to the significant growth in the Company's underwriting results.

## Financial results of PZU Życie SA (in PLN million)

Source: PZU Życie SA financial statement



PTE PZU SA also reported growing profits. At the end of 2006, the net profit of the Company amounted to PLN 83.9 million, 25.7% more than in the previous year.

The improvement in PTE PZU SA's profit was due to the higher results on operations and other activities.





## 13.7 Technical reserves

The PZU Group's balance of gross technical reserves at the end of 2006, including estimated recourses and recoveries, amounted to PLN 33,549.7 million (PLN 32,342.6 million net of the reinsurers' share). This corresponds to a 7.1% growth of the reserves set up compared to 2005 (a growth of 7.9% net of reinsurers' share).

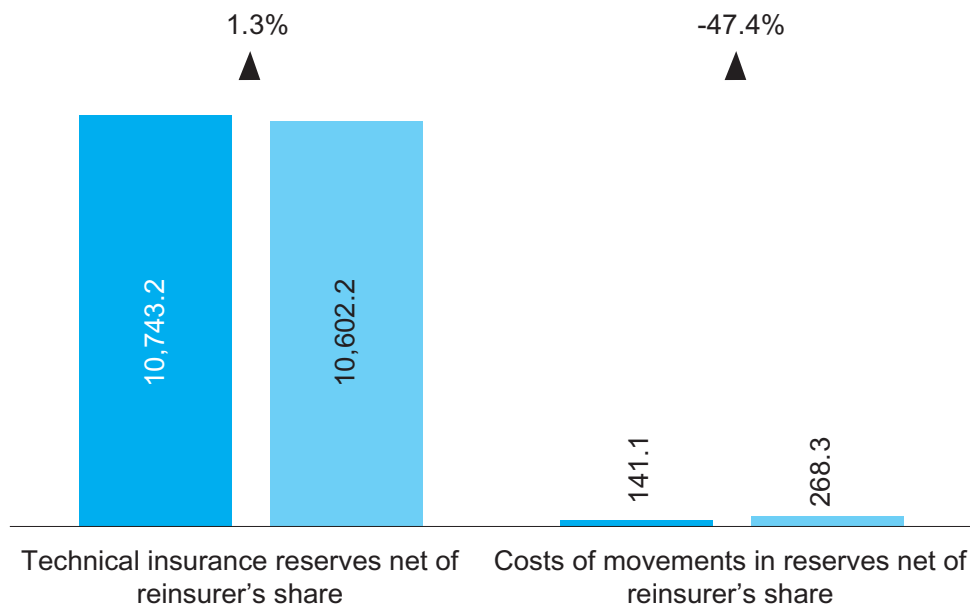
The balance of gross technical reserves of PZU SA, including estimated recourses and recoveries, amounting to PLN 11,906.6 million (or PLN 10,743.2 million net of the reinsurers' share) guarantees the complete financial security both of the Company and its customers. Compared to 2005, the balance of gross technical reserves of PZU SA dropped by 0.4%.

PZU SA's policy of setting up technical reserves is characterized by a conservative approach, taking into account foreseeable events that may contribute to an increase in liabilities (including the development of insurance awareness as well as future economic and legal changes). The reserves set up meet the requirements of Polish law and regulations for ensuring full coverage of current and future liabilities that may arise under insurance contracts entered into.

The balance of all technical reserves of PZU SA changed by PLN -46.6 million (PLN 141.1 million net of the reinsurers' share). The balance of reserves was among other things driven in 2006 by factors related to the introduction in the year of an algorithm allowing catastrophic provisions being exhausted faster and a reduction of the surcharge planned for future costs of pension service from 4% to 3%.

### Technical reserves net of the reinsurers' share and cost of movements in PZU SA reserves (in PLN million)

Source: PZU SA financial statement



■ 2006

■ 2005

▲ change

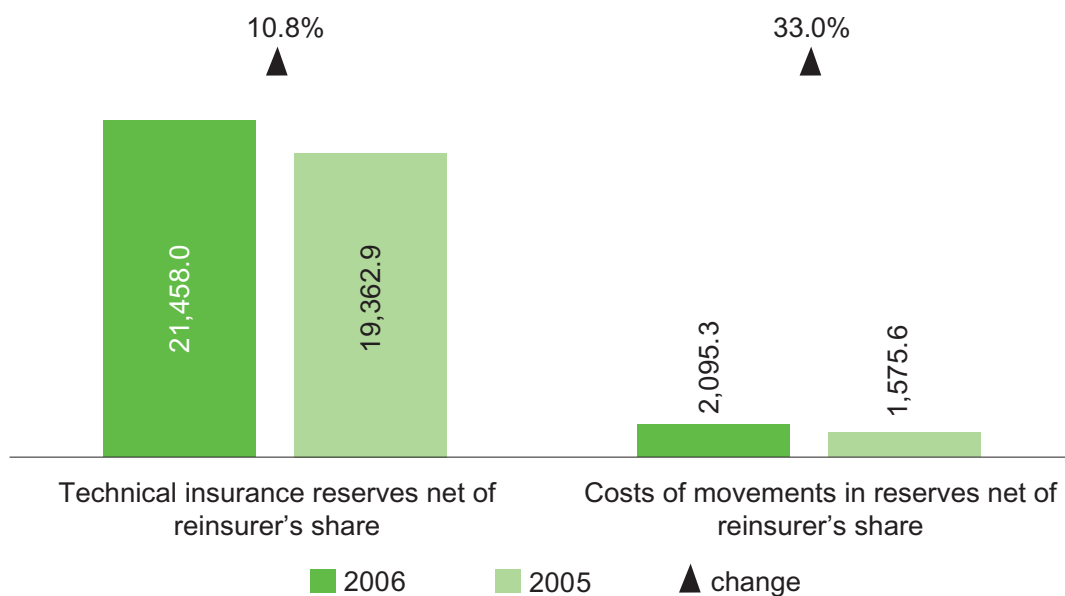


The balance of gross technical reserves of PZU Życie SA amounted to PLN 21,458 million, the amount net of the reinsurers' share being equal. As of the end of 2005, it amounted to PLN 19,362.9million, which is growth of PLN 2,095.1 million in 2006. In percentage terms, the Company's technical reserves grew by 10.8% in 2006.

The cost of changing the balance of PZU Życie SA gross reserves in 2006 amounted to PLN 2,095.2 million and PLN 2,095.3 million net of the reinsurers' share.

## Technical reserves net of the reinsurers' share and cost of movements in PZU Życie SA reserves (in PLN million)

Source: PZU Życie SA financial statement



## 13.8 Profitability, financial security and efficiency ratios

### Profitability ratios

Source: The PZU Group

Ratio	2006	2005	Change
Return on equity (ROE) (%) (net profit/average equity balance) x 100%	30.6	33.4	-2.8 points
Return on assets (ROA) (%) (net profit/average assets) x 100%	8.0	7.8	0.2 points
Profitability of investment activities (%) (income on investment activities/balance of investments)	7.5	8.9	-1.4 points
Profitability of technical activities (%) (underwriting result/premium earned net of reinsurer's share) x 100%	23.7	19.9	3.8 points
Return on sales (ROS) (%) (financial result/gross premiums written) x 100%	24.0	23.4	0.6 points

The growing ROA of the entire PZU Group bears witness to high and constantly increasing assets, among all group assets, which are working towards generating profit per unit of assets.

The mean ROE, higher than the market average, indicates that the capital entrusted to the PZU Group is managed very effectively.

The high profitability of investment activities maintained by the PZU Group proves the effective policy for investing assets, which cover technical reserves. Particularly good results were achieved by investing in bonds and shares.



## Solvency and liquidity ratios – financial security ratios

Source: The PZU Group

Ratio	2006	2005	Change
Solvency margin in property and casualty insurance (in PLN million)	1,169.5	1,182.2	-1.07%
Solvency margin in life insurance (in PLN million)	1,492.9	1,467.9	1.7%
Own funds to cover solvency margin in property and casualty insurance (in PLN million)	11,744.0	9,248.4	26.9%
Own funds to cover the solvency margin in life insurance (in PLN million)	4,435.9	3,908.2	13.5%
Coverage ratio of the solvency margin with own funds in property and casualty insurance (%)	1,004.1	782.3	221.8 points
Coverage ratio of the solvency margin with own funds in life insurance (%)	297.1	266.3	30.8 points
Guarantee capital in property and casualty insurance (in PLN million)	389.8	394.1	-1.1%
Guarantee capital in life insurance (in PLN million)	497.6	489.3	1.7%
Coverage ratio of guarantee capital with own funds in property and casualty insurance (%)	3,012.4	2,346.9	665.5 points
Coverage ratio of guarantee capital with own funds in life insurance (%)	891.4	798.8	92.6 points
Coverage ratio of technical reserves with assets in property and casualty insurance (%) (assets for covering reserves/balance of technical reserves) x 100%	169.0	147.3	21.7 points
Coverage ratio of technical reserves with assets in life insurance (%) (assets for covering reserves/balance of technical reserves) x 100%	121.4	116.0	5.4 points

The equity and the solvency margins are the main solvency measures, and the legal requirement for covering the solvency margin is absolute.

The above ratios show that capital requirements are covered several times over and that there is a large surplus of own funds, which paints a splendid financial security picture for the main PZU Group companies.



## Efficiency ratios

Source: The PZU Group

Ratio	2006	2005	Change
Gross loss ratio (simple) (%) (gross claims and benefits/gross premiums written)	56.78	60.1	-3.32 points
Net loss ratio (%) (claims and benefits/premium earned net of the reinsurers' share)	57.17	62.1	-4.9 points
Insurance activities costs ratio (%) (insurance activities costs/premium earned net of reinsurer's share)	19.55	20.4	-0.85 points
Combined ratio (%) (ratio of claims and benefits net of the reinsurers' share + ratio of insurance operation costs)	76.7	82.5	-5.8 points
Administrative expenses ratio (%) (administrative expenses/premium earned net of the reinsurers' share)	10.9	11.6	-0.7 points

The drop in the ratio of insurance operation costs was due to cutting current administrative expenses while the earned premium went up.

The clear fall in the combined ratio bears witness to an improvement in the general efficiency of the PZU Group and is mainly the result of improving loss ratios (lower costs of changing the balances of reserves and claims paid, while earned and written premiums increased).



## I. Introduction to the consolidated financial statements

### 1. Composition of the Capital Group of Powszechny Zakład Ubezpieczeń S.A., scope and method of consolidation

The Capital Group of Powszechny Zakład Ubezpieczeń SA ("PZU Capital Group", "the PZU Group") includes:

- Powszechny Zakład Ubezpieczeń SA ("PZU SA", "the parent company") as the parent company,
- Powszechny Zakład Ubezpieczeń na Życie SA ("PZU Życie SA") as a subsidiary subject to consolidation under the full method,
- Powszechne Towarzystwo Emerytalne PZU SA ("PTE PZU SA") as a subsidiary subject to consolidation under the full method,
- PZU Tower Sp. z o.o. ("PZU Tower") as a subsidiary subject to consolidation under the full method,
- Centrum Informatyki Grupy PZU SA ("CIG PZU SA") as a subsidiary subject to consolidation under the full method,
- UAB DK PZU Lietuva ("PZU Lietuva") as a subsidiary subject to consolidation under the full method as of 1 January 2006,
- OJSC IC PZU Ukraine ("PZU Ukraine") as a subsidiary subject to consolidation under the full method as of 1 January 2006.

Other entities have been excluded from consolidation due to the fact that their financial data are insignificant in relation to the financial data of the PZU Group, according to the criteria set out in Article 4 items 1 and 4 of the Accounting Act of 29 September 1994 (Journal of Laws No. 76/2002, item 694, as amended, hereinafter referred to as the "Accounting Act").

#### 1.1 Powszechny Zakład Ubezpieczeń SA

PZU SA is a joint stock company with its registered office in Warsaw, al. Jana Pawła II 24. It was formed through transformation of the Państwowy Zakład Ubezpieczeń state-owned enterprise into a joint-stock company of the State Treasury pursuant to Article 97 of the Insurance Activities Act of 28 July 1990 (uniform text in Journal of Laws No. 11/1996 item 62, as amended), hereinafter the Insurance Activities Act of 28 July 1990.

On 30 April 2001, PZU SA was registered in the National Court Register kept by the District Court for the capital city of Warsaw, 19th Commercial Division of the National Court Register, entry into the Register of Entrepreneurs No. KRS 0000009831.

According to the Statistical Classification of Economic Activities in the European Community (NACE), the main area of the Company's activities is property and casualty insurance (NACE 66.03).

#### 1.2 Powszechny Zakład Ubezpieczeń na Życie SA

PZU Życie SA is a joint stock company with its registered office in Warsaw, al. Jana Pawła II 24, incorporated on 18 December 1991 and entered in the Commercial Register kept by the Registry Court for the capital city of Warsaw, Commercial Court, 16th Commercial-Registry Department, section B, entry No. RHB 30260, on 20 December 1991.

On 26 July 2001, PZU Życie SA was entered in the Register of Entrepreneurs of the National Court Register under no. KRS 0000030211 on the basis of the decision issued by the District Court for the capital city of Warsaw, 19th Commercial Division.

According to the Statistical Classification of Economic Activities in the European Community (NACE), the main area of PZU Życie SA activities is life insurance (NACE 66.01).





### 1.3 Powszechnie Towarzystwo Emerytalne PZU SA

PTE PZU SA was incorporated on the basis of the Notarial Deed of 6 August 1998 to manage Otwarty Fundusz Emerytalny "Złota Jesień" ["Golden Autumn" Open-End Pension Fund] ("OFE PZU").

PTE PZU SA is a joint stock company with its registered office in Warsaw, al. Jana Pawła II 24, incorporated on 6 August 1998 and entered into the Register of Entrepreneurs of the National Court Register kept by the District Court for the capital city of Warsaw, 19th Commercial Division of the National Court Register, entry No. KRS 0000040724.

According to the Statistical Classification of Economic Activities in the European Community (NACE), the main area of PTE PZU SA activities are activities auxiliary to insurance and pension funding (NACE 67.20).

### 1.4 PZU Tower Sp. z o.o.

PZU Tower with its registered office in Warsaw, ul. Ogrodowa 58, was incorporated on 25 August 1998, and entered into the Register of Entrepreneurs of the National Court Register kept by the District Court for the capital city of Warsaw, 19th Commercial Division of the National Court Register, entry No. KRS 0000021844.

According to the Statistical Classification of Economic Activities in the European Community (NACE), the main area of PZU Tower activities is development and selling of property (NACE 70.11), including purchase and selling of property, intermediation in property trading as well as administration of property.

### 1.5 Centrum Informatyki Grupy PZU SA

CIG PZU SA with its registered office in Warsaw, ul. Matuszewska 14, was incorporated on 29 June 1998. On 26 September 2001, CIG PZU SA was entered in the National Court Register kept by the District Court for the capital city of Warsaw, 20th Division of the National Court Register, entry No. KRS 0000043026.

According to the Statistical Classification of Economic Activities in the European Community (NACE), CIG PZU SA business activities include activities auxiliary to insurance and pension funding (NACE 67.20).

### 1.6 UAB DK PZU Lietuva

PZU Lietuva with its registered office in Vilnius, Konstitucijos Ave. 7, was registered in the Register of Corporate Persons of the Republic of Lithuania on 2 November 2004, under No. 019084.

The main area of PZU Lietuva activities is property and casualty insurance.

### 1.7 OJSC IC PZU Ukraine

PZU Ukraine with its registered office in Kiev, ul. Degtyarevskaya 62, was incorporated in 1993 as Skide-West Close-End Joint-Stock Insurance Company. In 1999, it was transformed into an Open-End Joint-Stock Insurance Company.

PZU Ukraine has been using the name of OJSC IC PZU Ukraine since 28 February 2005.

The main area of PZU Ukraine activities is property and casualty insurance.

## 2. Sources of information for the preparation of the consolidated financial statements of the PZU Capital Group

The consolidated financial statements of the PZU Capital Group for 2006 ("consolidated financial statements") were prepared by the parent company based on data derived from consolidation documentation. The consolidation documentation is kept in accordance with the Accounting Act and the Ordinance on Special Rules of Accounting to be applied by Insurance Companies issued by the Minister of Finance on 8 December 2003 (Journal of Laws No. 218/2003 item 2144, hereinafter referred to as "Ordinance on Insurance Accounting").



For consolidation purposes, the financial data from standalone financial statements of PTE PZU SA, PZU Tower, CIG PZU SA, PZU Lietuva and PZU Ukraine were allocated to the relevant items of the financial statements of PZU SA. The format of the consolidated financial statements of the PZU Capital Group for 2006 included in this document and the scope of information disclosed is in compliance with:

- The Accounting Act; and
- The Ordinance on Insurance Accounting.

The financial year of the entities whose financial statements are subject to consolidation corresponds to the financial year of the parent company. The financial year covered by these consolidated financial statements commenced on 1 January 2006, and ended on 31 December 2006.

All the figures presented in these consolidated financial statements are shown in PLN thousands unless stated otherwise.

### 3. Going concern assumption

The present consolidated financial statements have been prepared on the assumption that the entities making up the PZU Capital Group and subject to consolidation will continue as going concerns in the foreseeable future, i.e. for a minimum period of 12 months from the balance sheet date, i.e. after 31 December 2006.

As of the date of signing of these consolidated financial statements, no facts or circumstances exist that would indicate the continued activity of PZU Group entities consolidated using the full method is threatened in the period of twelve months following the balance sheet date as a result of intended or forced discontinuance of their existing activities or significant limitation thereof.

#### 3.1 Business combinations

During the period covered by these consolidated financial statements, no business combinations took place involving PZU SA and other companies.

### 4. List of entities of the PZU Capital Group and their basic financial data

The following information has been presented below:

- A table presenting the percentage of ownership in the share capital and the percentage of voting rights held, directly or indirectly, by PZU SA in the individual entities making up the PZU Capital Group as of 31 December 2006 and 31 December 2005, as well as the information on the type of business activities conducted by those entities,
- A list of entities making up the PZU Capital Group as of 31 December 2006 and their basic financial data for 2006.



No.	Name of entity	Registered office	% of share capital directly or indirectly held by PZU SA	
			31.12.2006	31.12.2005
Subsidiaries consolidated using the full method as of 31 December 2006				
1	PZU Życie SA	Warsaw	100.00%	100.00%
2	PTE PZU SA	Warsaw	100.00%	100.00%
3	Centrum Informatyki Grupy PZU SA	Warsaw	100.00%	100.00%
4	PZU Tower Sp. z o.o.	Warsaw	100.00%	100.00%
5	OJSC IC PZU Ukraine	Kiev (Ukraine)	100.00%	100.00%
6	UAB DK PZU Lietuva	Vilnius (Lithuania)	99.72%	99.72%
Subsidiaries not consolidated as of 31 December 2006				
7	SYTA Development Sp. z o.o. in liquidation	Warsaw	100.00%	100.00%
8	TFI PZU SA	Warsaw	100.00%	100.00%
9	Sigma Investments Sp. z o.o.	Warsaw	100.00%	100.00%
10	PZU Asset Management SA	Warsaw	100.00%	100.00%
11	CERPO Sp. z o.o. in liquidation	Gliwice	0.00%	100.00%
12	Biuro Likwidacji i Obsługi Szkód Sp. z o.o.	Warsaw	100.00%	100.00%
13	Międzyzakładowe Pracownicze Towarzystwo Emerytalne PZU SA	Warsaw	100.00%	100.00%
14	PZU International Sp. z o.o.	Warsaw	100.00%	100.00%
15	OJSC IC PZU Ukraine Life Insurance	Kiev (Ukraine)	100.00%	100.00%
16	LLC SOS Services Ukraine	Kiev (Ukraine)	100.00%	100.00%
17	UAB PZU Lietuva Gyvybės Draudimas	Vilnius (Lithuania)	99.34%	99.34%
18	Company with Additional Liability Inter-Risk Ukraine	Kiev (Ukraine)	100.00%	100.00%
19	Krakowska Fabryka Armatur SA	Krakow	90.53%	90.53%



% of voting rights held, directly or indirectly, by PZU SA		Scope of activities
31.12.2006	31.12.2005	
100.00%	100.00%	Life insurance
100.00%	100.00%	Establishment and management of OFE PZU Złota Jesień
100.00%	100.00%	Activities auxiliary to insurance and pension funding
100.00%	100.00%	Property acquisition, use, lease and sale
100.00%	100.00%	Property insurance
99.72%	99.72%	Property insurance
100.00%	100.00%	Purchase and sale of property, intermediation in property trading, and property administration
100.00%	100.00%	Establishment, representation and management of investment funds
100.00%	100.00%	Investment activities. Purchase and sale of shares in listed companies, bonds and other securities admitted to public trading
100.00%	100.00%	Management of third-party investment portfolios
0.00%	100.00%	Provision of services in the scope of gathering and processing information on vehicle registration
100.00%	100.00%	Loss adjusting services on behalf of other insurers
100.00%	100.00%	Third pillar insurance
100.00%	100.00%	Capital investment
100.00%	100.00%	Life insurance
100.00%	100.00%	Provisions of assistance services
99.34%	99.34%	Life insurance
100.00%	100.00%	Legal services
90.53%	90.53%	Manufacture of bathroom and kitchen fixtures and fittings



No.	Name of entity	Registered office	% of share capital directly or indirectly held by PZU SA	
			31.12.2006	31.12.2005
20	ICH Center SA	Warsaw	56.00%	46.00%
Affiliates as of 31 December 2006				
21	VIS-Inwestycje SA	Warsaw	45.14%	45.14%
22	Kolej Gondolowa Jaworzyna Krynicka SA	Krynica	37.53%	37.83%
23	Nadwiślańska Agencja Ubezpieczeniowa SA	Tychy	30.00%	30.00%
24	Polskie Towarzystwo Reasekuracji SA	Warsaw	23.77%	23.77%
25	PPW Uniprom SA in bankruptcy	Warsaw	21.28%	21.28%



% of voting rights held, directly or indirectly, by PZU SA		Scope of activities
31.12.2006	31.12.2005	
56.00%	46.00%	Handling of claims from Green Card insurance
45.14%	45.14%	Manufacturing of tools, apparatus and spares
36.71%	36.85%	Operation of ski-lifts and tourist cable cars
30.00%	30.00%	Handling of claims
23.77%	23.77%	Organization and conduct of indirect insurance activities (reinsurance)
21.28%	21.28%	Publishing and printing related services; manufacturing of cardboard and paper packaging





No.	Company name	In PLN thousand	Net profit (loss)
Subsidiaries not consolidated as of 31 December 2006			(1,853)
1	SYTA Development Sp. z o.o. in liquidation /1		767
2	TFI PZU SA		1,667
3	Sigma Investments Sp. z o.o.		(3)
4	PZU Asset Management SA		2,072
5	Biuro Likwidacji i Obsługi Szkód Sp. z o.o. /1		(111)
6	Międzyzakładowe Pracownicze Towarzystwo Emerytalne PZU SA		-
7	PZU International Sp. z o.o. /1		(17)
8	OJSC IC PZU Ukraine Life Insurance /5		(4,881)
9	LLC SOS Services Ukraine /1 /5		176
10	UAB PZU Lietuva Gyvybės Draudimas /4		(4,362)
11	Company with Additional Liability Inter-Risk Ukraine /1 /5		1
12	Krakowska Fabryka Armatur SA		2,156
13	ICH Center SA		682
Associates not consolidated as of 31 December 2006			14,682
14	VIS-Inwestycje SA		(4,700)
15	Kolej Gondolowa Jaworzyna Krynicka SA		2,274
16	Nadwiślańska Agencja Ubezpieczeniowa SA		385
17	Polskie Towarzystwo Reasekuracji SA /2 /3		16,723
18	PPW Uniprom SA in bankruptcy /1 /6		-
TOTAL			12,829

1) Unaudited data

2) "Sales revenue" calculated as the sum total of the gross premium written and other technical income, net of reinsurers' share

3) "Financial income" calculated as the difference between "Investment income" and "Unrealized gains on investments" and "Cost of investing activities" and "Unrealized losses on investments".

4) Data according to the Lithuanian Accounting Standards, which do not significantly differ from Polish Accounting Standards

5) Data according to the Ukrainian Accounting Standards

6) Data as of 30 November 2004



Sales revenue and financial income	Total assets	Liabilities and provisions for liabilities	Shareholders' equity
202,038	251,355	114,122	111,909
4,639	12,174	17,979	(5,802)
19,543	37,789	8,560	29,229
1	69	-	69
22,286	17,553	10,198	7,355
-	33	8	26
165	648	148	500
1	24	5	19
7,919	15,720	1,205	8,500
1,202	512	223	290
11,494	35,671	1,406	14,952
43	13	4	8
131,153	128,234	73,956	54,278
3,592	2,915	430	2,485
254,099	527,040	224,203	80,414
6,524	29,258	31,724	(2,466)
12,330	38,289	6,825	31,464
1,974	3,290	392	2,897
231,249	404,127	30,930	150,775
2,022	52,076	154,332	(102,256)
456,137	778,395	338,325	192,323



## 5. Principal accounting policies

All the consolidated entities of the PZU Capital Group apply methods of measurement of assets and liabilities compliant with the provisions of the Accounting Act and the Ordinance on Specific Rules for Recognition, Measurement Methods, Scope of Disclosure and Method of Presentation of Financial Instruments issued by the Minister of Finance on 12 December 2001 (Journal of Laws No. 149/2001 item 1674, as amended, hereinafter the Ordinance on Financial Instruments), and in addition, in the case of PZU SA, PZU Życie SA, PZU Lietuva and PZU Ukraine, with the Ordinance on Insurance Accounting.

### 5.1 1.1 Basis of consolidation

In order to select the entities consolidated under the full method or equity method, the criterion of materiality has been applied which considers if the operating result and the net result (in absolute values) as well as the balance sheet total are material in relation to the relevant figures of the consolidated financial statements of the PZU Group, net of consolidation adjustments.

These consolidated financial statements comprise balances of the parent company and of its subsidiaries after elimination of inter-company transactions.

Assets and liabilities of foreign subsidiaries are converted into the Polish currency at the average National Bank of Poland (NBP) exchange rate obtaining at the balance sheet date for a given currency. Items of the profit and loss account are converted at the exchange rate representing the arithmetic mean of average exchange rates obtaining on the day ending each month of the financial year. The resulting foreign exchange differences are shown in the present consolidated financial statements in "Foreign exchange differences from conversion of subordinates". The following exchange rates have been adopted for the purposes of these consolidated financial statements:

Exchange rates used for foreign subordinates translation	LTL	UAH
Closing exchange rate as of 31 December 2006	1,1096	0,5760
Average exchange rate for the period from 1 January to 31 December 2006	1,1292	0,6129



To prepare these consolidated financial statements, the following consolidation adjustments were applied to the financial data of the companies consolidated under the full method:

- Carrying amount of the parent company's investments in each subsidiary,
- Share capital of subsidiaries,
- Other equity items of subsidiaries arising prior to 1 January 1995,
- Inter-company receivables and liabilities of the entities being subject to consolidation,
- Revenues and costs relating to operations executed between the entities being subject to consolidation,
- Unrealized, from the point of view of the PZU Capital Group, gains or losses on operations executed between the consolidated entities and included in the consolidated amounts,
- Dividends paid between the PZU Group companies consolidated on a full basis.

Both in the current and in the preceding financial year, revenues, costs and gains unrealized from the point of view of the PZU Group were taken to "Accumulated profits/(losses) from previous years", irrespective of whether such elimination related to companies posting losses or companies transferring gains to reserve capital.

## 5.2 Intangible assets

In particular, software, copyrights and licenses shall be included in intangible assets.

Intangible assets are recorded at acquisition cost or cost of production less accumulated amortization and impairment losses.

Intangible fixed assets are depreciated using the straight-line method over the anticipated period of their useful life.

Software, licenses and other property rights are depreciated over a period of up to 5 years.

Intangible assets of an initial cost not exceeding PLN 3,500.00 are redeemed in full when brought into use.

## 5.3 Goodwill on consolidation

Goodwill on consolidation represents the surplus of the cost of acquisition over the share of the acquiring entity in fair value of net assets of the acquired entity. Goodwill on consolidation is amortized to the consolidated General Profit and Loss Account over a period of five years, starting from the month following the month in which goodwill on consolidation is determined.



## 5.4 Investments

Investments are valued and presented in these consolidated financial statements as follows:

### 5.4.1 Investment property

Included in investment property are land, perpetual usufruct, buildings and constructions, cooperative freehold right to a residential or non-residential unit, investments in constructions and prepayments for those investments.

Freehold land is shown at cost or re-valued amount less any impairment losses. Under the provisions of the Accounting Act, freehold land is not depreciated.

Buildings and constructions are valued at cost or cost of production less accumulated depreciation and impairment losses.

Perpetual usufruct of land, cooperative freehold right to a residential unit and cooperative right to a non-residential unit as investment are recorded in the books of account at cost or cost of production less accumulated amortization and impairment losses.

Investments in constructions and prepayments for those investments are shown at cost or cost of production less impairment losses.

Investment property, except for freehold land and investments in constructions and prepayments for those investments are depreciated over their estimated useful lives.

The PZU Group companies apply the following annual depreciation and amortization rates to investment property subject to depreciation and amortization:

Category	Rate
Perpetual usufruct of land	Determined in proportion to the period of time over which the right is held by the PZU Group companies
Cooperative freehold right to a residential unit and cooperative freehold right to a non-residential unit	2.5%
Buildings and constructions	2.5 – 4.5%

Under the Polish regulatory framework, land, buildings and constructions are re-valued at the rates published by the President of the Central Statistical Office (CSO). The last revaluation took place on 1 January 1995.



## 5.4.2 Shares in related entities

Shares in related entities not covered by consolidation (except for insurance companies) are valued using the equity method as long as they comply with the significance criterion as defined in the accounting policies of the PZU Group.

Shares in the remaining related entities are shown at cost less impairment losses.

## 5.4.3 Financial instruments

Upon purchase, financial instruments are classified into one of the following categories:

- financial assets held for trading,
- financial assets held to maturity,
- financial assets available for sale, and
- loans and receivables.

### 5.4.3.1 Financial assets held for trading

Included under financial assets held for trading are assets acquired to obtain economic benefits resulting from short-term fluctuation of prices, fluctuation of other market factors or from the short term of the life of the acquired asset itself, as well as derivatives, unless they have been recognized as hedging instruments under the Ordinance on Financial Instruments.

Debt securities, shares and derivatives included in the portfolio of financial assets held for trading are valued at fair value or, when their fair value cannot be reliably determined, at cost less impairment losses.

Fair value of derivatives (forward rate agreements (FRAs) and interest rate swaps (IRSs)) is determined using the cost-to-close method, i.e. at closing cost of the given item in the market as of the balance sheet date.

Derivatives are recorded in the balance sheet under item C.III.7., "Other investments" on the assets' side or under item J.V.2., "Other liabilities" on the equity and liabilities' side of the balance sheet.



## 5.4.3.2 Financial assets held to maturity

Included in financial assets held to maturity are financial assets which have not been included under loans and receivables and whose contracts determine the nominal value maturity and the right to obtain economic benefits such as, for instance, interest, fixed or determinable, on predefined dates, which financial assets the company intends to and may hold until maturity. Financial assets held to maturity include, in particular, debt securities that the company intends to and may hold until maturity.

At the balance sheet date, financial assets held to maturity are valued at depreciated cost determined using the effective interest rate set in accordance with the Ordinance on Financial Instruments, less any impairment losses.

## 5.4.3.3 Financial assets available for sale

Included in financial assets available for sale are assets which have not been classified as financial assets held for trading or financial assets held to maturity and not classified as Loans and receivables. Financial assets available for sale are valued at fair value or, where their fair value cannot be reliably determined, at cost less impairment losses.

The difference between the fair value of financial assets available for sale and their adjusted acquisition cost (and for equity instruments – the purchase price) is set against revaluation reserve, while the effects of revaluation of debt instruments classified in that category to the adjusted acquisition cost are shown in investment income. In the case of assets taken into account when determining technical insurance reserves, the effects of measurement are set against the consolidated life insurance revenue account (for life insurance) or against the consolidated property and casualty insurance revenue account (for property and casualty insurance).

## 5.4.3.4 Loans and receivables

The item of Loans and receivables includes, irrespective of their maturity (payment date), financial assets resulting from direct issuance of cash to the counterparty.

Included in this category are also bonds and other debt financial instruments purchased in exchange for cash issued directly to the counterparty if the concluded contract stipulates explicitly that the seller does not lose control over financial instruments issued. In particular, this item includes buy-sell-back transactions.





Loans are stated in the amount due (adjusted acquisition cost) less any impairment losses.

Term deposits held with financial institutions are shown at par value. Term deposits in foreign currencies are valued as of the balance sheet date according to the average National Bank of Poland exchange rate obtaining on that day.

Interest on term deposits accrued by the balance sheet date is shown in the G.III. item of assets, "Accrued interest and rental charges".

#### 5.4.3.5 Deposits with cedants

Deposits with cedants include claims and premium deposits retained by insurers for which PZU SA provides reinsurance coverage. They represent a part of the premium payable to PZU SA but retained as collateral for future claims.

Deposits with cedants are measured at the amount due determined in accordance with the provisions of the reinsurance contract incorporating – whenever the deposit constitutes a financial instrument – also the measurement of such instrument and impairment losses, if any.

#### 5.4.3.6 Net life insurance assets where the policyholder bears the investment risk

"Net life insurance assets where the policyholder bears the investment risk" show net assets of insurance capital funds that comprise investments of life insurance funds at the risk of policyholder as well as cash, receivables and liabilities associated with the aforementioned investments.

Investments whose risk is carried by the policyholder are valued at fair value.

### 5.5 Receivables

Receivables are recognized at the amount determined at the moment they arise. As of the balance sheet date, receivables are stated in the amount due determined using the principle of prudence. Receivables are shown at the value adjusted for impairment losses. The companies of the PZU Group create provisions for bad or doubtful debt on the basis of analysis of the debtors' financial condition, analysis of the ageing structure of their receivables and debt collection history, thus evaluating the likelihood of payment.



## 5.5.1 Direct insurance receivables

Direct insurance receivables comprise accounts receivable from policyholders arising from premiums paid in instalments and from overdue premiums, as well as receivables due from insurance intermediaries, i.e. insurance brokers and agents.

Impairment losses updating the value of direct insurance receivables are classified as other technical expenses.

## 5.5.2 Reinsurance receivables

Reinsurance related receivables include balances receivable in respect of settlements with cedants, reinsurers and reinsurance brokers arising from reinsurance inwards and outwards as well as retrocession. These receivables refer in particular to reinsurers' share in claims and benefits paid by the insurer, reinsurance commissions and shares in reinsurers' profits.

Write-downs against receivables from reinsurers are included in "Other technical expense".

## 5.5.3 Non-insurance receivables

Other receivables include in particular receivables due from the Budget and receivables arising from loss-adjusting services rendered.

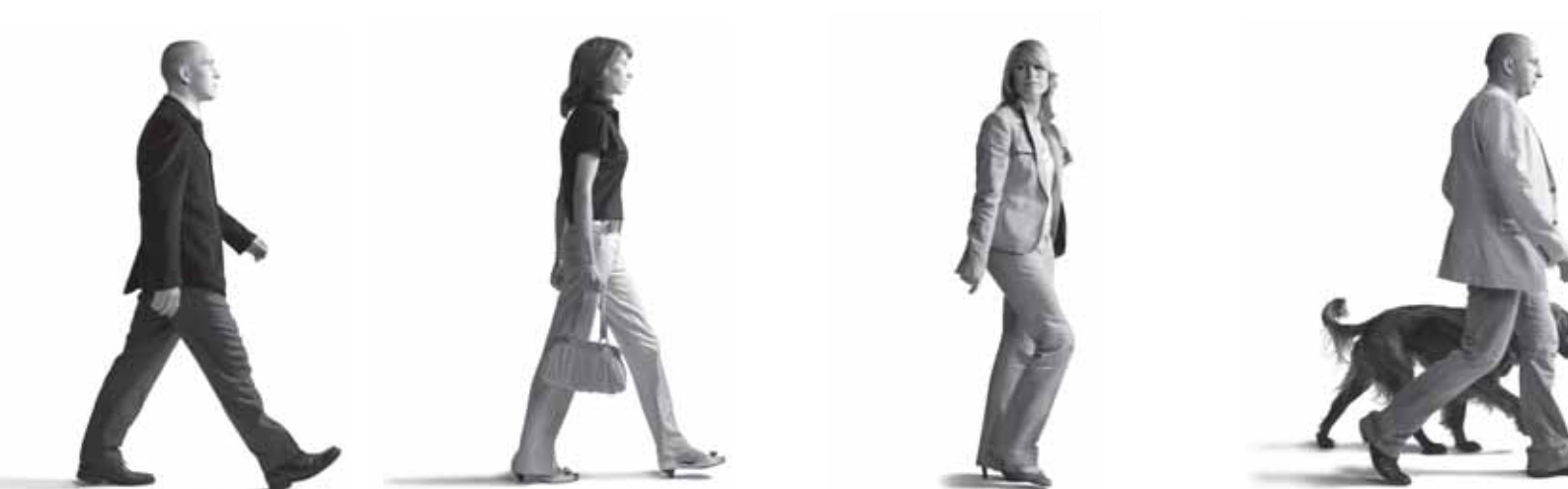
Impairment losses on non-insurance receivables are recorded under other operating expenses.

## 5.6 Property, plant and equipment

Property, plant and equipment include tangible fixed assets and their equivalents with the expected useful lives of more than one year that are completed and ready for use by the PZU Group companies.

Tangible fixed assets are stated at acquisition cost or cost of production or re-valued amount (from appraisal), less accumulated depreciation and impairment losses. Assets are re-valued in accordance with separate provisions. The last revaluation took place on 1 January 1995. The effects of the revaluation are taken to revaluation reserve. Once a fixed asset has been sold or liquidated, the amount remaining in revaluation reserve is transferred to reserve capital.

Tangible fixed assets are depreciated using the straight-line method over their expected useful lives.



The examples of annual depreciation rates used by the companies of the PZU Group are as follows:

Category	Rate
Plant and machinery	8.5% – 40%
Motor vehicles	10% – 20%
Other tangible fixed assets	5% – 40%

Assets with an initial cost below PLN 3,500.00 are expensed in full when brought into use, only once.

Included in property, plant and equipment is also construction in progress. Construction in progress is stated in the amount of aggregate costs directly attributable to their acquisition or production less revaluation losses. Construction in progress also includes investment materials. Construction in progress is not depreciated until completed and brought into use.

For tax purposes, entities with their registered offices in Poland adopt depreciation rates stemming from the Act on Corporate Income Tax of 15 February 1992 (Journal of Laws No. 54/2000 item 654, as amended, hereinafter the Act on Corporate Income Tax). The rates derived from the Ordinance on Depreciation and Amortization of Fixed Assets and Intangible Assets issued by the Minister of Finance on 17 January 1997 apply to fixed assets acquired and entered in the books of account before 1 January 2000.

## 5.7 Cash

Cash are shown in the consolidated financial statements at par value. Cash expressed in foreign currencies are stated as of the balance sheet date at the average National Bank of Poland exchange rate obtaining on that day.

## 5.8 Prepaid and accrued expenses and deferred income

The PZU Group companies account for prepaid and accrued expenses to ensure that they are allocated to the appropriate reporting period.

The Company recognizes prepayments if the costs incurred relate to future reporting periods. Among others, prepayments include deferred acquisition costs.

In the case of property and casualty insurance, direct and indirect costs of acquisition are deferred. In the case of full employment, direct and indirect costs of acquisition are deferred together Social Security surcharges.



As far as life insurance (insurance from Group 1 and 2 of Section I) is concerned, acquisition costs relating directly or indirectly to the sale of insurance policies as well as commission expenses paid on the due annualized premium income for individual insurance and unit-linked insurance are subject to deferral.

Additionally, the PZU Group companies recognize accruals and deferred income to ensure that they are allocated to the appropriate reporting period.

Accrued income includes, among other things, receivables from accrued revenues from fixed term deposits and rental charges.

Deferred income includes, among other things, deferred reinsurance commissions and premiums paid in respect of insurance policies with the insurance coverage period commencing after the balance sheet date.

At the level of the PZU Capital Group, the commission paid to sales agents for the acquisition carried out for OFE PZU is spread over a two-year period beginning in the month of conclusion of the OFE PZU membership agreement. Deferred acquisition costs are presented under the "Other prepayments" caption. As of the balance sheet date, the portion of deferred acquisition costs relating to the agreements that will not generate income for the PZU Capital Group in the future is covered by an impairment loss.

Accruals comprise costs of the current reporting period that will be incurred in the subsequent period, including in particular the costs of reinsurance outwards.

Reinsurance accruals comprise accrued income and costs arising from economic events occurring until the balance sheet date and relating to the portfolio of risks subject to reinsurance coverage whose settlement with reinsurance companies – as per the terms of contract – will take place in the future.

## 5.9 Equity

Equity is recognized in the books of account at par value by type and in accordance with binding legal regulations and provisions of the parent company's articles of association.

Equity captions of subsidiaries, other than share capital, were added to respective captions of equity of the parent company proportionately to the percentage of the parent company's ownership of the subsidiary.

The effects of "Revaluation of financial assets" classified as financial assets available for sale, buildings and constructions as well as fixed assets are recognized in revaluation reserve under separate provisions.



## 5.10 Minority interests' equity

Minority interests' equity is the part of net assets of the subsidiaries consolidated using the full method that represents the interests held by the shareholders from outside of the PZU Capital Group.

The result of the subsidiaries consolidated using the full method proportional to the interests of the shareholders from outside of the PZU Capital Group constitutes the result (profit or loss) of minority shareholders.

## 5.11 Technical and insurance reserves

Technical and insurance reserves are created to cover current and future claims and costs that may arise from concluded insurance contracts. The reserves are established using the prudence principle, in accordance with Article 7 of the Accounting Act.

Technical and insurance reserves have been created in compliance with applicable articles of association of insurance companies making up the PZU Capital Group, the Insurance Activities Act, the Ordinance on Insurance Accounting and internal regulations for creating technical and insurance reserves.

### 5.11.1 Unearned premium reserve

#### *Property and casualty insurance*

The unearned premium reserve is created in the amount of premiums written allocated to future reporting periods, in proportion to the insurance coverage period for which a given premium has been written.

The unearned premium reserve is created to cover liabilities that may arise after the end of the reporting period and resulting from insurance contracts under which the coverage period expires after the balance sheet date.

The unearned premium reserve is valued at the end of each reporting period using the individual method, to the nearest day.

For insurance policies with uneven spread of risk over the insurance coverage period, the unearned premium reserve is established in the amount dependent on distribution of risk during the insurance coverage period.

The reinsurers' share in the unearned premium reserve is calculated in accordance with the terms and conditions of applicable reinsurance agreements, in the amount proportionate to the reinsurance coverage allocated to the periods after the end of a given reporting period.

#### *Life insurance*

The unearned premium reserve is created in the amount representing a part of premiums written allocated to future reporting periods, in proportion to the insurance coverage period for which the premium is written.



## 5.11.2 Life insurance reserve

Life insurance reserves are created using actuarial methods in the following way:

- group employee insurance and individually continued insurance reserves are based on the actuarial prospective method under which a life insurance reserve is established separately for each insurance policy based on certain statistical data regarding the insured;
- unit-linked life insurance in aggregate as a percentage of the fund's value to cover the death risk, in accordance with the general terms and conditions of such insurance;
- other types of insurance using the prospective actuarial method, individually for each policy.

For the portfolio of individual insurance policies and annuities taken over from PZU SA, the life insurance reserve also includes the effects of valorisation of such policies by PZU Życie SA.

## 5.11.3 Outstanding losses and benefits reserves

### *Property and casualty insurance*

#### 5.11.3.1 Outstanding losses and benefits reserve

The outstanding claims and benefits reserve comprises the reserve for claims and benefits for loss and accidents incurred and reported, reserve for loss and accidents incurred but not reported, loss adjustment expenses reserve and the annuities reserve.

##### ***Reserve for losses reported and unadjusted***

The reserve for losses reported and not adjusted (hereinafter "Reserve I") is determined in the amount of average loss for losses not assessed by the loss adjuster or in the amount specified by loss adjusting units. The reserve balance takes into account the deductible of the insured and the anticipated increase in prices of goods and repair services, and may not exceed the sum insured or guaranteed.

The reserve balance is updated immediately after the information affecting its balance has been obtained, using the individual claims and benefits assessment method.

##### ***Reserve for losses and accidents incurred but not reported***

The reserve for losses and accidents incurred but not reported (hereinafter "IBNR" or "Reserve II") is created for losses and benefits that have been incurred but have not been reported by the date of creation of the reserve, using the triangulation methods such as Chain Ladder, Cape Code and Bornhuetter-Ferguson method, broken down by year of loss.



**Loss adjustment expenses reserve**

The loss adjustment expenses reserve is determined at the end of each reporting period as the sum of the reserve for direct and indirect costs of loss adjustment.

The reserve for direct costs of loss adjustment is established both for losses already reported (individual method) and for not reported losses (lump sum method – share in the IBNR reserve).

The reserve for indirect costs of loss adjustment is established as a percentage of the sum of the reserve for losses incurred and not adjusted, reserve for incurred but not reported losses and of the reserve for direct costs of loss adjustment.

**Estimates of recourses and recoveries for technical and insurance reserves**

In determining the balance of future claims and benefits payments, PZU SA makes assessments of anticipated reimbursements of costs incurred by PZU SA as a result of assumption of claims against third parties (recourses) and of ownership rights in the assets insured (recoveries). The assessed balance of recourses and recoveries includes the costs of their enforcement.

**Reinsurers' share in technical and insurance reserves**

The reinsurers' share in the balance of outstanding claims and benefits reserve is calculated in accordance with the terms and conditions of applicable reinsurance contracts.

**5.11.3.2 Capitalized value of annuities from third parties liability insurance**

The reserve for capitalized value of annuities is calculated individually for each beneficiary as the present value of annuity (lifelong or periodical), payable in advance.

At the end of each reporting period, an annuities reserve is also created for the losses that occurred after 31 December 1990, and were not recorded as annuities until the balance sheet date (the "Annuity IBNR Reserve").

At the end of each reporting period, an additional reserve is created to cover liabilities arising from the increase in the value of annuities included in the so-called "old portfolio". The additional reserve applies to the annuitants for whom an analogous reserve was calculated at the end of 1997 but whose annuities did not reach the satisfactory level at the end of the reporting period. The satisfactory level of annuities has been adopted as a percentage of the average present value of salaries in the years 1960–1990. The annuities reserve is calculated for the difference between the satisfactory and actual annuity level, in accordance with applicable regulations.





## Life insurance

### 5.11.3.3 Outstanding claims reserve, including annuities reserve

The outstanding claims and benefits reserve is created independently to cover benefits that:

- have been reported but not paid; or
- have been incurred but not reported.

The reserve for benefits reported but not paid is created for benefits reported and not adjusted by the last day of the reporting period. The reserve for benefits reported but not paid is created individually or for high volumes of benefits when it is not possible to estimate the value of individual benefits, using the average value of individual benefit paid in the last quarter preceding the reporting period.

The reserve for benefits incurred but not reported by the balance sheet date is created for each type of benefits using the lump sum method, as a percentage of benefits paid during the last twelve months. The outstanding claims and benefits reserve also includes the loss adjustment expenses reserve.

### 5.11.4 Other technical and insurance reserves in property and casualty insurance

#### 5.11.4.1 Unexpired risk reserve

The unexpired risk reserve is created as a supplement to the unearned premium reserve to cover future claims, benefits and expenses arising from insurance contracts that do not expire on the last day of the reporting period.

The unexpired risk reserve is created for all groups (types) of insurance with the loss ratio for a given financial year exceeding 100% as the difference between the product of the unearned premium reserve and the loss ratio for a given financial year and the unearned premium reserve, both relating to the same period of insurance.

The reinsurers' share in the unexpired risk reserve is calculated in accordance with the terms and conditions of applicable reinsurance contracts.

#### 5.11.4.2 Loss (risk) equalization reserve

The loss (risk) equalization reserve is created in the amount that is expected to ensure equalization of any future fluctuations in the loss ratio, net of the reinsurers' share, in accordance with the Ordinance on Insurance Accounting.



## 5.11.4.3 Catastrophe and exceptional risk reserve

The catastrophe and exceptional risk reserve is created to cover losses incurred as a result of catastrophic or large-scale events and exceptional risk losses.

As of 1 July 2004, PZU SA has ceased to increase the level of the catastrophe and exceptional risk reserve.

If claims are paid for losses arising from catastrophic or exceptional risk events, the reserve is decreased by such payments, net of the reinsurers' share.

## 5.11.5 Other reserves in life insurance

### 5.11.5.1 Technical and insurance reserves for life insurances where investment risk is borne by policyholder

The life insurance reserves under which investment risk is borne by the policyholder are created in the amount of the sum of the participation units in the investment fund held in the insureds' accounts valued at fair value as of the balance sheet date.

### 5.11.5.2 Other technical and insurance reserves defined in the Articles of Association of PZU Życie SA

Other technical and insurance reserves defined in the articles of association of PZU Życie SA include:

- reserve for the valorisation of benefits under individual life policies and annuities taken over from Państwowy Zakład Ubezpieczeń (the so-called "old portfolio"),
- reserve for litigations and benefits in relation with court decisions and settlements issued on the basis of Article 3581 §3 of the Polish Civil Code of 23 April 1964 (Journal of Laws No. 16/1964 item 93, as amended, hereinafter the "Civil Code") regarding changes to the amount or manner of payment of a cash benefit.

The reserve for litigations is created in the amount of anticipated additional benefits resulting from litigations and is based on the information held by PZU Życie SA on the trends in concluded settlements and completed court cases.

- Reserve for low interest rates relating to revenue from insurance investment fund for policies with a guaranteed rate of return.



The low interest reserve relating to an anticipated decrease in the insurance fund investment returns in the case of individual life insurance, individual insurance with a rising sum insured and insurance premium, the “Firm” group insurance and annuity insurance is created using the actuarial method on a case-by-case basis for each insurance policy in the amount corresponding to the difference between the balance of mathematical reserves created using appropriate mathematical formulas and modified technical rates to reflect a potential decrease in the future and the balance of mathematical reserves created in accordance with applicable regulations for establishing reserves, with the original technical rate applied when assigning tariffs for these products.

#### 5.11.5.3 Reserves for bonuses and rebates for the insured

This reserve corresponds to anticipated shares in the earnings of the insurer posted at the balance sheet date that will be awarded after the conclusion of the settlement period.

### 5.12 Other reserves and special funds

In the item of “Other reserves and special funds” includes reserves for certain or very likely future liabilities arising from past events, the amount and date of payment of which – although not certain – can be determined in a reliable manner. In particular, other reserves and special funds include reserves for jubilee bonuses, reserve for retirement benefits, reserve for unused leave, reserve for losses from pending business transactions, reserve for sureties and guarantees granted, and reserve for losses from pending court cases and third party claims.

Reserve for deferred tax liability is also shown in other reserves and special funds.

The costs of creation of reserves are included, respectively, in other technical costs, net of the reinsurers’ share, other operating expenses, other financial expenses or administrative expenses, depending on the type of the future liability.

#### 5.12.1 Reserve for jubilee bonuses and retirement benefits

In accordance with the Remuneration Regulations applicable to the PZU Group companies with registered offices in Poland, employees are entitled to jubilee bonuses after a specified number of years in service and to retirement benefits upon retirement. The amount of the bonus or retirement benefit depends on the number of years in service and on the amount of average monthly remuneration.

The Company’s expenses associated with jubilee bonuses and retirement benefits assessed by means of actuarial methods are recognized on an accrual basis using the projected unit credit method.

Actuarial profits and losses are recognized in full in the period in which they occurred.



In the case of jubilee bonuses, the costs of past service – within the meaning of IAS 19 – are immediately recognized in the profit and loss account.

Reserves for retirement benefits are valued at fair value of future benefits that may be allocated to the previous period of service, after adjustment for not recognized costs of past service.

## 5.12.2 Reserve for untaken leave

The value of the reserve for unused leave is calculated as the difference between the number of annual leave days actually taken and the number of annual leave days that would apply if the annual leave was used in proportion to the passage of time in the period for which the employees are entitled to annual leave, in accordance with binding provisions.

## 5.12.3 Reserve for posthumous and post-employment benefits

Under the provisions of the Polish Labour Code of 26 June 1974 (uniform text in Journal of Laws No. 21/1998 item 94, as amended, hereinafter the “Labour Code”), in the case of the employee’s demise during the course of employment or during the period for which sickness benefit is collected, the family of the deceased employee is entitled to a posthumous benefit from the employer, the amount of which depends on the period of service with the employer and constitutes the equivalent of 1 to 6-month remuneration.

Pursuant to the provisions of the Social Fund Act of 4 March 1994 (Journal of Laws No. 43/1994 item 163, as amended) and to the Regulations of the PZU SA Social Fund, entitled to the benefits and services financed from the fund are, among other persons, the retired employees and pensioners of PZU SA (former employees) and their families. According to the assumptions adopted at the PZU Group companies with registered offices in Poland, the annual amount of such benefits represents on average 6.25% of the mean monthly remuneration per retiree or pensioner.

Reserves for posthumous and post-employment benefits are valued at fair value of future benefits that may be allocated to the employee’s previous period of service.

## 5.12.4 Special funds

The item “Special funds” includes balances of the Company Social Benefit Fund and of the Prevention Fund. The Company Social Benefit Fund is created in accordance with appropriate provisions governing operation of a company social benefit fund and it is charged against costs and the net profit pursuant to the resolutions of the General Meeting.

The Prevention Fund is charged against costs in accordance with the provisions of the Act on Insurance Activities. The balance of special funds is increased by gains from investments made by those funds.



## 5.13 Liabilities

Liabilities are stated in the amount due and payable.

## 5.14 Revenues and costs from investment activities

### 5.14.1 Revenues from interest on deposits with financial institutions

Income from interest on deposits with financial institutions is recognized by the PZU Group companies on an accrual basis, whereby the total interest due to the PZU Group companies for a given reporting period is recorded in the books of account, irrespective of the date of its receipt. If a deposit matures after the balance sheet date, interest is accrued proportionately to passage of time from the date of placement of the deposit until the balance sheet date inclusive.

### 5.14.2 Debt securities' revenue and expenses

The result of measurement of debt securities at depreciated cost is taken to revenues from debt securities.

The difference between fair value as of the balance sheet date and depreciated cost is recognized as follows:

- For debt securities classified as available-for-sale (not included in the calculation of technical and insurance reserves, bonuses and rebates) – under "Revaluation reserve",
- For debt securities classified as held-for-trading (not included in the calculation of technical and insurance reserves) – under "Unrealized profits or unrealized losses on investments".

Realized profits/losses on sale/surrender of debt securities are recognized under Profits/Losses on realization of investments.

Investment revenues covering reserves are shown in the property and casualty insurance revenue account as well as in the life insurance technical account, net of any related costs.

The above rules do not apply to investment revenues whereby investment risk is borne by policyholder for whom revenues and costs are shown in the life revenue account.



## 5.14.3 Revenue from property and cost of property maintenance

Revenue from property includes rental fees received, lease rentals and other charges relating to property management.

Revenue from property constituting investments is shown under revenue from property in the general profit and loss account (for property and casualty insurance) or in the life revenue account (for life insurance).

The costs of maintenance of property earmarked for investment purposes are shown under “Costs of property maintenance” in the life insurance technical account or in the general profit and loss account.

The costs of maintenance of property used for own purposes by the PZU Group companies are shown in the consolidated property and casualty insurance revenue account and in the consolidated life revenue account under “Administrative expenses”.

The costs of maintenance of the PZU SA headquarters comprising, among other things, operating expenses of PZU Tower and, in particular, depreciation and amortization of the building, external services as well as materials and energy, are recorded in consolidated property and casualty insurance revenue account and life revenue account, and in the consolidated general profit and loss account in the proportions derived from the area occupied by a given PZU Group company.

## 5.14.4 Share-related profits and losses

Included in unrealized profits/losses on investments are profits and losses on measurement of shares classified as held-for-trading in the amount of the difference between fair value and acquisition cost or, in the case of shares acquired in previous years – between fair value and the carrying amount as of the end of the previous financial year.

Profits and losses on revaluation of shares classified as available-for-sale (not included in the calculation of technical and insurance reserves) are recognized in revaluation reserve.

Profits/losses on sale of shares are recorded under “Profits/Losses on realization of investments”.

Included in “Losses on investment revaluation” are investments’ impairment losses for the reporting period, while profits on reversal of impairment losses made in previous reporting periods are shown under ‘gains on investment revaluation’.

Revenues from dividends are recorded in the gross amount.

Profits on investments covering life insurance reserves are recognized in the consolidated life revenue account and subsequently allocated to the technical and general parts. The method of allocation has been presented in Item of these consolidated financial statements.



## 5.14.5 Presentation of investment revenues in life insurance

PZU Życie SA presents both realized and unrealized investment revenues (excluding revenues and costs taken to revaluation) and costs of investing activities in the consolidated life revenue account. Revenues on investments of own funds, less costs of investment activities relating to such revenues, are transferred from the consolidated life revenue account to the consolidated general profit and loss account and included under "Net gains on investments allocated from the consolidated life revenue account, less costs".

## 5.15 Revenues from sale of insurance services in property and casualty insurance and life insurance

Revenue from premiums written is recorded by premium maturity. For direct insurance, premium maturity date is the first day of coverage as defined in the insurance contract (policy), however not earlier than the date of premium payment if the insurer's liability has been rendered conditional on payment of the premium in the insurance contract. The premium paid by the last day of the reporting period (inclusive) which relates to the policies with insurance coverage running from the first or any subsequent day of the following month is recorded under deferred income as of the balance sheet date.

The reinsurers' share in the premium has been calculated for those groups of insurance with reinsurance coverage in the amount equal to the amount assignable to the reinsurers, as stipulated in relevant reinsurance contracts in force during a given insurance period.

## 5.16 Net investment revenues allocated from the consolidated general profit and loss account, less costs

### *Property and casualty insurance*

The value of the annuities reserve under third-party liability policies has been increased by the amount of revenues from investments representing coverage for that reserve. Due to the fact that the Company's own funds and funds from the insurance fund are invested jointly and that no separation of such investments is made, the amount of investment income to be allocated from the consolidated general profit and loss account to the consolidated property and casualty insurance revenue account is calculated as the product of the balance of the annuities reserve at the beginning of the month and of profitability for that month of held-to-maturity State Treasury bonds, inclusive of relevant costs of investment activities.





## 5.17 Costs of claims and benefits paid

### 5.17.1 Property and casualty insurance

Included in the costs of the reporting period are all the costs of paid claims and benefits arising from concluded insurance contracts, along with direct and indirect costs of loss adjusting activities and movements in the outstanding claims and benefits reserve (OCR). The costs of claims and benefits reduce the balance of all recourses and recoveries made and the balance of movements in estimated recourses and recoveries.

The value of claims and benefits represents all payments and charges made in the reporting period in connection with claims and benefits for losses and accidents that occurred in the current and previous reporting periods, jointly with all the costs of loss adjusting and recourse-collection activities, less any returns, recourses and recoveries.

The reinsurers' share in the claims and benefits was calculated for the insurance groups with reinsurance coverage in the amount equal to the amount due to reinsurers under reinsurance treaties binding in a given insurance period.

### 5.17.2 Life insurance

Benefits paid include all payments and charges (compensated with receivables) incurred in the reporting period with regard to claims and benefits relating to losses and accidents that occurred in the current and previous reporting periods (including annuities and surrenders), along with all direct and indirect, external and internal costs of loss adjusting activities. Costs of loss adjusting activities comprise also the costs of litigations.

The value of claims and benefits paid is recognized in the amounts actually paid less returns and refunds (except for refunds from reinsurance outwards), increased by movements in the OCR reserve, net of reinsurers' share, at the end and beginning of the reporting period and less the reinsurers' share in benefits paid and in reserves.

Loss adjusting costs comprise direct and indirect costs relating to the activities aimed at examining and adjusting losses reported or to the activities supporting the above.



## 5.18 Insurance activity costs

### 5.18.1 Property and casualty insurance

Acquisition expenses include the costs of conclusion and renewal of insurance contracts. Direct acquisition costs include, among others, insurance agent commissions, payroll costs of employees engaged in policy conclusion, costs of certification, expert opinions and research relating to the risk insured. Indirect acquisition costs include costs of advertising and promotion of insurance products as well as general costs of assessment of insurance applications and issuance of policies.

In order to match the PZU S.A. revenues (from the premium written) and acquisition costs, the commission on the premium written during the current reporting period – accrued but not payable – is taken to the acquisition costs, while the non-payable commission recorded in the previous reporting period is settled and the acquisition costs incurred and accrued relating to future reporting periods are deferred.

Administrative expenses comprise the costs of insurance activities not classified as acquisition costs or costs of claims and benefits or costs of investing activities, relating to premium collection, management of the portfolio of insurance contracts, reinsurance contracts and to the general management of the insurance company.

Costs of insurance activities are adjusted for the value of reinsurance commissions and shares in the profits of reinsurers and retrocessionaries received from brokers and reinsurers under reinsurance outwards and retrocession. The value of reinsurance commissions received or receivable is adjusted for the amount of deferred reinsurance commissions in the portion relating to future reporting periods.

### 5.18.2 Life insurance

Acquisition costs include direct and indirect costs relating to conclusion of insurance contracts, in particular costs of the activities which:

- are aimed at signing and incorporating in the portfolio of new insurance contracts, which relates to writing of new premium, or
- are aimed at changing the scope of insurance coverage or renewal of insurance contracts and incorporation of those changes in the insurance portfolio, which entails writing of new premium.

Commission costs are recognized in the same period in which the corresponding premium written is due. Acquisition costs are adjusted for movements in the balance of deferred acquisition costs.



Administrative expenses comprise the costs of insurance activities not classified as acquisition costs or costs of claims and benefits or costs of investment activities, relating to premium collection, management of the portfolio of insurance contracts, reinsurance agreements and to the general management of the insurance company.

In particular, PZU Życie SA recognizes as administrative expenses all the costs of services rendered by third parties handling group employee insurance policies.

### 5.19 Revenue and costs relating to activities of pension fund management company

Costs incurred in connection with acquisition of members for OFE PZU are settled over a period of two years from the date of the contract conclusion and are recorded in "Other operating expenses" in the consolidated general profit and loss account. Deferred acquisition costs are presented in the consolidated balance sheet under "Other prepayments and deferred costs". All the other expenses and revenues relating to the PTE PZU SA activities are shown in the consolidated general profit and loss account under 'Other operating costs and 'Other operating revenues.

#### 5.19.1 OFE PZU management fee

PTE PZU SA receives a management fee from OFE PZU in the amount stated in the Articles of Association of OFE PZU, including the limits set forth in the Act on Organization and Functioning of Pension Funds of 28 August 1997 (Journal of Laws No. 159/2004 item 1667, as amended, hereinafter the Pension Funds Act).

#### 5.19.2 Handling fees

PTE PZU SA charges handling fees on contributions transferred by the Social Security Fund ("ZUS") to OFE PZU in the amount stated in the Articles of Association of OFE PZU, including the limits set forth in the Pension Funds Act.

The handling fee is recognized as revenue of PTE PZU SA in the month the relevant contribution is transferred to OFE PZU.

#### 5.19.3 Transfer-out fees in PTE PZU SA

Transfer-out fees are charged in accordance with the Articles of Association of OFE PZU and shown in the months in which transfer payments are to be settled.

#### 5.19.4 Contributions to the primary part of the Guarantee Fund

PTE PZU SA is obliged to make contributions to the primary part of the Guarantee Fund in the amount of 0.1% of the value of net assets of OFE PZU. Payments due are calculated taking into account all earlier payments and revenues on earlier deposits less remuneration owed to the National Depository for Securities ("KDPW") being the administration fee for managing the primary part of the Guarantee Fund.



In the case of insufficient contributions, payments are made from the primary part of the Guarantee Fund to the open-end fund in which the shortage is reported to the extent in which the funds of the additional part of the Guarantee Fund are inadequate to cover such shortage. Also, the Guarantee Fund is required to cover losses for which the fund management company is not liable.

#### 5.19.5 Payments to the additional part of Guarantee Fund

According to the Pension Funds Act, PTE PZU SA is obliged to make contributions to the additional part of the Guarantee Fund constituting a portion of OFE PZU assets. The minimum funds kept in the additional part of the Guarantee Fund range from 0.3% to 0.4% of the net assets of OFE PZU. The payments to the additional part of the Guarantee Fund are classified in full as other operating costs.

The shortage in the open-end fund is covered from the funds kept in the additional part of the Guarantee Fund when the moneys accumulated in the reserve account are insufficient to cover the said shortage. The shortage in the open-end fund occurs when the rate of return on that fund's assets for a period of 36 months falls below the minimum required rate of return.

#### 5.19.6 Payments to premium account/reserve account

According to the Pension Funds Act, funds accumulated in the premium account – to which PTE PZU SA has become entitled – should be immediately transferred to the reserve account. The funds in the reserve account constitute a portion of OFE PZU assets and are converted into settlement units. PTE PZU SA may withdraw the funds accumulated in the reserve account on the last working day of April or October on the condition that the rate of return is obtained on the funds managed in accordance with the rules set forth in the Pension Funds Act.

#### 5.19.7 KDPW charges

PTE PZU SA is obliged to make payments to the National Depository for Securities in lieu of all costs incurred in connection with processing of transfers-out.

The fee for every transfer-out amounts to 1% of the minimum remuneration, defined by separate regulations.

#### 5.19.8 ZUS contributions

PTE PZU SA is obliged to make payments to ZUS as a recharge of incurred costs of premium collection and recovery. The amount of ZUS fee is specified every year in the State Budget Law. In the years 2005-2006, the fees charged by ZUS amounted to 0.8% of all the premiums transferred.



PTE PZU SA is also obliged to pay a fee to ZUS as a refund of the costs of execution of operations relating to members' subscription to the open-end fund in the amount of 1% of the minimum remuneration as defined under separate provisions, on each registered OFE PZU membership contract.

## 5.20 Foreign currency transactions

As of the balance sheet date, foreign currency assets and liabilities are converted at the average NBP exchange rate obtaining on that day.

Foreign currency purchase or sale transactions as well as discharging of liabilities or collection of receivables denominated in foreign currencies are recorded in the books of account at the buying or selling rate applied by the bank employed by PZU Group companies.

For the remaining operations, the PZU Group companies apply the average NBP exchange rate for a given currency obtaining at the transaction date unless another exchange rate has been defined in the customs declaration or another binding document.

## 5.21 Taxation

Corporate income tax shown in the profit and loss account consists of current tax liability and deferred tax.  
Current tax liability

During the financial year, PZU SA and PZU Życie SA have taken advantage of the simplified form of prepayments for corporate income tax as envisaged by Article 25 para. 6 of the Act on Corporate Income Tax. In these consolidated financial statements, a liability towards the Tax Office was recognized and a tax charge on the gross profit in the amount derived from calculation of corporate income tax on general principles.

Deferred tax

In connection with temporary differences between the carrying amount of assets and liabilities shown in the books of account and their tax base and tax losses deductible in the future, the PZU Group companies recognize deferred tax assets and deferred tax liabilities, of which they are payers.

The tax base of assets is the amount that will be deductible for tax purposes against any taxable direct and indirect economic benefits that will flow to an entity. If those economic benefits are not taxable, the tax base of the assets is their carrying amount. The tax base of liabilities is their carrying amount less any amount deductible for tax purposes with respect to these liabilities in the future.



The PZU Group companies recognize deferred tax assets in the amount deductible in the future from corporate income tax in connection with negative temporary differences that will reduce taxable income and deductible tax loss as determined using the principle of prudence.

The PZU Group companies establish the reserve for deferred tax assets in the amount of corporate income tax payable in the future in connection with occurrence of positive temporary differences, i.e. differences that result in the increase of taxable income in the future.

The levels of the reserve and of deferred tax assets are determined using the corporate income tax rates applicable in the year in which the tax obligation arises.

Deferred tax assets and deferred tax liabilities resulting from business transactions with the use of equity items are settled against equity.

## 6. Changes in accounting policies and in the manner of preparation of the consolidated financial statements

In 2006, the PZU Group companies did not make any changes in the accounting policies or valuation methods of assets or liabilities that could have an effect on the consolidated financial statements.

Below the changes in the method of preparation of the consolidated financial statements are presented.

### 6.1 Presentation of the buy-sell-back transactions

In 2006, changes were made to the method of presentation of the buy-sell-back transactions.

Previously, liabilities arising from the said transactions were presented in off-balance sheet items under "Contingent liabilities". In connection with the position adopted by the supervisory body regarding presentation in the financial statements of contracts on conditional purchase or sale of debt securities, recognition of the aforementioned transactions in Off-balance sheet items was discontinued.

The financial data recognized as of the end of 2005 were restated for comparability purposes.



## 6.2 Presentation of assets pledged as securities and litigations

In order to ensure transparent presentation of off-balance sheet items, security established on assets and litigations not recognized by PZU SA and pursued by creditors in court were presented under "Other off-balance sheet items" in the figures cited at the end of 2006 and 2005.

## 6.3 Presentation of assets earmarked for liquidation

In order to ensure transparent presentation of off-balance sheet items, the value of fixed assets put into liquidation due to their tear and wear, loss or sale was presented under "Other off-balance sheet items", and not as previously shown in Item 5 "Third party assets not included in the PZU Group assets".

The data as of 31 December 2005 have been adjusted to preserve their comparability.

## 6.4 Presentation of accrued reinsurance revenues and costs

In order to ensure a transparent presentation of the off-balance sheet items, in 2006 a change was made in the method of presentation of accrued revenues and costs of outwards and inwards reinsurance. Currently, these items are presented separately i.e. under item G.IV. "Other prepayments and deferred costs" on the assets side, and under item K.1 "Accruals and deferred income – Accrued expenses" on the equity and liabilities side.

Prior to that, those items were presented in the netted-off amount under item K.1 on the equity and liabilities side.

As a result of that change, comparable data presented herein were adjusted, which led to an increase in the balance sheet total as of 31 December 2005 by PLN 94,505 thousand with respect to the data presented in the consolidated financial statements for 2005.

## 7. Significant events of the financial year with a material effect on the structure of balance sheet items and of the financial result

### 7.1 First-time consolidation of PZU Ukraine and PZU Lietuva since 1 January 2006

The financial data of PZU Ukraine and PZU Lietuva is subject to consolidation using the full method since 1 January 2006. The prior year financial data of those entities was not subject to consolidation due to its immateriality from the PZU Group perspective.





Net assets as of 31 December 2005	In thousand zloty	PZU Ukraine	PZU Lietuva
Intangible assets		907	2,275
Fixed assets		7,983	4,012
Investments		40,214	82,565
Receivables		16,545	32,918
Other assets		2,089	12,703
Cash		3,440	1,613
Technical reserves (gross)		(50,794)	(122,645)
Reinsurers' share in technical reserves		18,354	36,184
Other liabilities		(19,336)	(24,234)
Net assets		19,402	25,391

An increase of PLN 5,053 thousand in cash as a result of inclusion of PZU Ukraine and PZU Lietuva under consolidation has been presented under other inflow from investing activities.

Valuation as of 31 December 2005	In thousand zloty	PZU Ukraine	PZU Lietuva
Net carrying amount of shares (valued at cost)		60,199	90,443
Share of PZU in the entity's net assets as of the date of purchase or taking up shares		41,508	53,165
Goodwill on consolidation of subordinated entities (gross)		18,691	37,278
Impairment losses of goodwill on consolidation of subordinated entities		(3,115)	(26,080)
Goodwill on consolidation of subordinated entities (net)		15,576	11,198



The difference between the net carrying amount of investments in the shares of these entities as of 31 December 2005 and PZU Group's share in net assets of the entities and goodwill on consolidation (PLN 25,221 thousand for PZU Ukraine and PLN 53,854 thousand for PZU Lietuva) was taken to the 2006 financial result.

Additionally, net consolidated result for 2006 was affected by the performance of PZU Ukraine (a loss of PLN 70,736 thousand) and of PZU Lietuva (a loss of PLN 33,004 thousand).

The 2005 financial data was not restated for comparability.

## 8. Significant prior year events reflected in the current year consolidated financial statements

Until the date of preparation of these consolidated financial statements, no significant prior year events occurred that should have but were not included in the 2006 consolidated financial statements.

In 2005 and in previous years, no errors that would require adjustments in the 2006 books of account were made in the PZU Group.

## 9. Significant post-balance sheet events not reflected in the current year consolidated financial statements

Until the date of preparation of these consolidated financial statements, no significant post-balance sheet events occurred that should have but were not included in the 2006 consolidated financial statements.

## 10. Discontinued activities

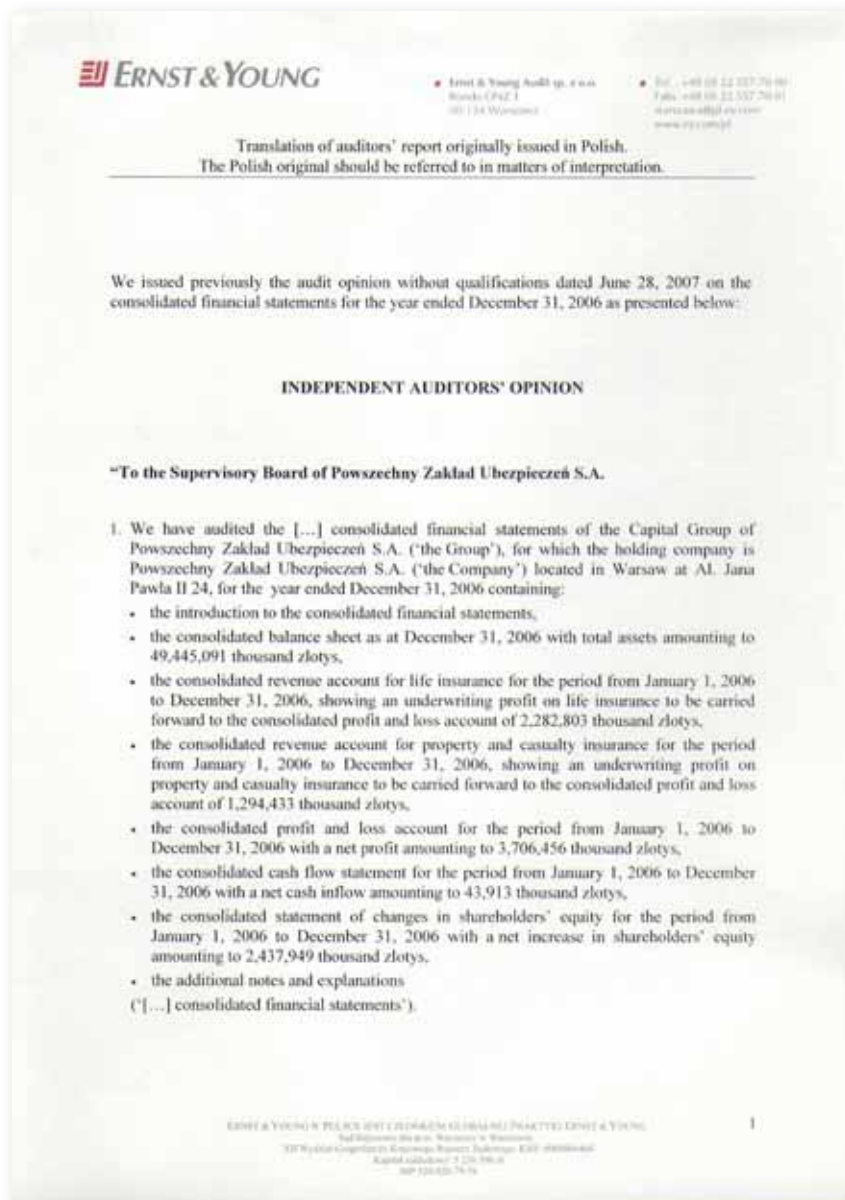
During 2006, the PZU Group companies covered by these consolidated financial statements did not discontinue any type of business activity.

## 11. Comparability of the 2006 opening and 2005 closing balances

The 2006 opening balances are comparable with the 2005 closing balances.



## II. Consolidated financial statements – the PZU Group



Translation of auditors' report originally issued in Polish.  
The Polish original should be referred to in matters of interpretation.

2. The truth and fairness<sup>1</sup> of the [...] consolidated financial statements and the proper maintenance of the consolidation documentation are the responsibility of the Company's Management Board. Our responsibility was to audit the [...] consolidated financial statements and to express an opinion whether, based on our audit, these financial statements are, in all material respects, true and fair<sup>2</sup>.
3. We conducted our audit of the [...] consolidated financial statements in accordance with the following regulations being in force in Poland:
- chapter 7 of the Accounting Act, dated September 29, 1994 ('the Accounting Act'),
  - the auditing standards issued by the National Chamber of Auditors,
- in order to obtain reasonable assurance whether the [...] consolidated financial statements are free of material misstatement. In particular, the audit included examining, to a large extent on a test basis, documentation supporting the amounts and disclosures in the [...] consolidated financial statements. The audit also included assessing the accounting principles adopted and used and significant estimates made by the Group, as well as evaluating the overall presentation of the [...] consolidated financial statements. We believe our audit has provided a reasonable basis to express our opinion on the [...] consolidated financial statements treated as a whole.
4. In our opinion, the [...] consolidated financial statements, in all material respects:
- present truly and fairly all information material for the assessment of the results of the Group's operations for the period from January 1, 2006 to December 31, 2006, as well as its financial position<sup>3</sup> as at December 31, 2006;
  - have been prepared in accordance with the accounting principles specified in the Accounting Act and regulations issued based on that Act;
  - are in accordance with the Accounting Act and regulations issued based on that Act and the provisions of the Company's statute.
5. We have read the Directors' Report for the period from January 1, 2006 to December 31, 2006 ('the Directors' Report') and concluded that the information derived from the [...] consolidated financial statements reconciles with these financial statements. The information included in the Directors' Report corresponds with article 49 paragraph 2 of the Accounting Act and the Appendix 5 to the Decree of the Minister of Finance of December 8, 2003 on specific accounting principles for insurance companies."

<sup>1</sup> Translation of the following expression in Polish: "prawidłowości, rzetelność i jasność"

<sup>2</sup> Translation of the following expression in Polish: "prawidłowe, rzetelne i jasne"

<sup>3</sup> Translation of the following expression in Polish: "sytuacja majątkowa i finansowa"





Translation of auditors' report originally issued in Polish.  
The Polish original should be referred to in matters of interpretation.

In our opinion the information presented in the published, condensed financial statements on pages 103 to 164 of this annual report is in all material respects fairly stated in relation to the consolidated financial statements from which it has been derived. The consolidated financial statements that were audited by us include notes that were not fully presented in the attached condensed consolidated financial statements. In order for the reader to obtain a true and fair view of the state of affairs of the Group as at December 31, 2006 and the results of its operations for the period from January 1, 2006 to December 31, 2006, the reader must review the full financial statements in their entirety including supporting schedules and statutory disclosures as required by the Accounting Act and the regulations based thereof.

On behalf of  
Ernst & Young Audit Sp. z o.o.  
Rondo ONZ 1, 00-124 Warszawa  
Reg. No. 130

Marcin Dymek  
Certified Auditor Nr 9899/7370

Dominik Januszewski  
Certified Auditor No. 9707/7255

Warsaw, October 31, 2007

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## Consolidated balance sheet

Assets,	In PLN thousand	31 December 2006	31 December 2005
A. Intangible assets		101,592	92,822
1. Goodwill		-	-
2. Other intangible assets and advances for intangible assets		101,592	92,822
B. Goodwill of related entities		18,992	1,733
C. Investments		43,453,060	38,726,522
I. Property		1,104,537	1,114,205
1. Freehold land, including perpetual usufruct		156,024	156,636
2. Buildings and constructions and cooperative freehold right		922,113	920,351
3. Construction in progress and advances for construction in progress		26,400	37,218
II. Investments in related entities,		216,487	313,779
1. Shares in related entities		183,922	297,384
2. Loans granted to related entities and debt securities issued by those entities		32,565	16,295
3. Other		-	100
III. Other financial investments		42,123,392	37,290,862
1. Shares and other variable income securities, participation units and investment certificates in investment funds		4,167,248	3,891,843
2. Debt securities and other fixed income securities		32,323,580	30,637,913
3. Shares in joint ventures		-	-
4. Mortgage loans		58	-
5. Other loans		4,274,332	1,919,366





Assets,	In PLN thousand	31 December 2006	31 December 2005
6. Term deposits with financial institutions		1,328,680	841,740
7. Other investments		29,494	-
IV. Deposits due from cedants		8,644	7,676
D. Net life insurance where the policyholder bears the investment risk		3,161,650	1,778,839
E. Receivables		1,470,600	1,377,908
I. Receivables from direct insurance		1,077,608	1,075,509
1. Receivables from policyholders		1,036,483	1,055,650
1.1. From related entities		19	43
1.2. From other entities		1,036,464	1,055,607
2. Receivables from insurance intermediaries (agents):		30,557	19,177
2.1. From related entities		-	761
2.2. From other entities		30,557	18,416
3. Other receivables		10,568	682
3.1. From related entities		80	110
3.2. From other entities		10,488	572
II. Reinsurance receivables		37,171	60,014
1. From related entities		44	2,522
2. From other entities		37,127	57,492
III. Other receivables		355,821	242,385
1. Receivables from the State Budget		92,142	101,502
2. Other receivables		263,679	140,883
2.1. From related entities		9,263	13,580
2.2. From other entities		254,416	127,303





Assets	In PLN thousand	31 December 2006	31 December 2005
F. Other assets		616,410	619,418
I. Tangible assets		252,058	300,151
II. Cash and cash equivalents		361,737	317,824
III. Other		2,615	1,443
G. Prepayments and deferred costs		622,787	538,941
I. Deferred tax assets		9,832	9,421
II. Deferred acquisition costs		408,053	388,278
III. Accrued interest and rental charges		11,077	4,048
IV. Other prepayments and deferred costs		193,825	137,194
Assets, total		49,445,091	43,136,183

Equity and liabilities	In PLN thousand	31 December 2006	31 December 2005
A. Equity		13,330,887	10,892,938
I. Share capital		86,352	86,352
II. Unpaid share capital (negative value)		-	-
III. Treasury shares (negative value)		-	-
IV. Reserve capital		7,869,693	6,536,323
V. Revaluation reserve		301,411	192,650
VI. Other reserves		-	-
VII. Foreign exchange differences on related entities		145	-
1. Foreign exchange gains		145	-
2. Foreign exchange losses		-	-



Equity and liabilities	In PLN thousand	31 December 2006	31 December 2005
VIII. Accumulated profits/ (losses) from previous years		1,366,830	862,821
IX. Net profit/(loss)		3,706,456	3,214,792
X. Deductions from net profit (loss) for the financial year (negative value)		-	-
B. Negative goodwill of related entities		-	-
C. Minority capital		136	-
D. Subordinated liabilities		-	-
E. Technical reserves		33,602,247	31,379,811
I. Unearned premium reserve and unexpired risk reserve		3,708,048	3,590,531
II. Life insurance reserves		16,775,480	16,102,416
III. Outstanding claims reserve		8,002,217	7,830,358
IV. Reserve for bonuses and rebates for the insured		2,581	1,729
V. Risk equalization reserve		575,387	560,955
VI. Other technical reserves as defined in Articles of Association		1,376,884	1,516,509
VII. Life technical reserves where the investment risk is borne by policyholders		3,161,650	1,777,313
F. Reinsurers' share in technical reserves (negative value)		(1,208,065)	(1,351,297)
I. Reinsurers' share in unearned premium reserve and unexpired risk reserve		(34,109)	(160,341)
II. Reinsurers' share in life insurance reserve		-	(39)
III. Reinsurers' share in outstanding claims reserve		(1,173,956)	(1,190,917)
IV. Reinsurers' share in reserve for bonuses and rebates for the insured		-	-
V. Reinsurers' share in other technical reserves		-	-
VI. Reinsurers' share in life insurance technical reserves where the investment risk is borne by policyholders		-	-



Equity and liabilities	In PLN thousand	31 December 2006	31 December 2005
G. Estimated salvages and subrogations (negative value)		(51,558)	(64,210)
I. Estimated salvages and subrogations, gross		(52,567)	(64,895)
II. Reinsurers' share in estimated salvages and subrogations		1,009	685
H. Other reserves		648,430	674,111
I. Reserve for retirement benefits and similar obligations		284,029	270,988
II. Deferred tax liability		342,779	380,438
III. Other provisions		21,622	22,685
I. Liabilities from reinsurance deposits		34	66
J. Other liabilities and special funds		2,512,687	843,823
I. Direct insurance liabilities		378,593	253,368
1. Liabilities to the policyholders		199,932	155,763
1.1. To related entities		1	-
1.2. To other entities		199,931	155,763
2. Liabilities to insurance intermediaries (agents)		66,048	60,310
2.1. To related entities		-	30
2.2. To other entities		66,048	60,280
3. Other insurance liabilities, of which:		112,613	37,295
3.1. To related entities		779	798
3.2. To other entities		111,834	36,497
II. Reinsurance liabilities		55,003	63,917
1. To related entities		28	4,534
2. To other entities		54,975	59,383
III. Liabilities from issuance of own debt securities and loans taken out		-	-



Equity and liabilities	In PLN thousand	31 December 2006	31 December 2005
1. Liabilities convertible to insurer's shares		-	-
2. Other		-	-
IV. Liabilities to financial institutions		72	10
V. Other liabilities		1,871,085	333,036
1. Liabilities to the State Budget		367,648	106,620
2. Other liabilities		1,503,437	226,416
2.1. To related entities		16,474	16,083
2.2. To other entities		1,486,963	210,333
VI. Special funds		207,934	193,492
K. Accruals and deferred income		610,293	760,941
I. Accrued expenses		500,039	603,997
II. Negative goodwill		-	-
III. Deferred income		110,254	156,944
Total equity and liabilities		49,445,091	43,136,183

	In PLN thousand	31 December 2006	31 December 2005
Book value		13,330,887	10,892,938
Number of shares		86,352,300	86,352,300
Book value per share (in PLN)		154,38	126,15
Diluted number of shares		86,352,300	86,352,300
Diluted book value per share (in PLN)		154,38	126,15



Off-balance sheet items	In PLN thousand	31 December 2006	31 December 2005
1. Contingent receivables, of which:		3,186,142	2,320,197
1.1. Guarantees received		4,342	2,776
1.2. Other		3,181,800	2,317,421
2. Contingent liabilities, of which:		88,863	114,291
2.1. Guarantees issued		10,916	10,390
2.2. Bills of exchange accepted and endorsed		-	-
2.3. Buy and sell back assets		-	-
2.4. Other liabilities		-	-
3. Reinsurance guarantees made to the insurer		-	-
4. Reinsurance guarantees made by the insurer to cedants		-	-
5. Third party assets not included in the insurer's assets		215,342	118,302
6. Other off-balance sheet items, of which:		62,638	64,809
– security established on the insurer's assets		62,638	63,760
– Other off-balance sheet items		-	1,049

Information on solvency of the parent company	In PLN thousand	31 December 2006	31 December 2005
Own funds		11,743,970	9,248,377
Solvency margin		1,169,545	1,182,191
Surplus (shortage) of own funds to cover solvency margin		10,574,425	8,066,186
Technical reserves		11,906,162	11,952,737
Assets to cover technical reserves		20,117,019	17,606,334
Surplus (shortage) of assets to cover technical reserves		8,210,857	5,653,597



## Consolidated life insurance revenue account

Consolidated life insurance revenue account	In PLN thousand	1 January – 31 December 2006	1 January – 31 December 2005
I. Premiums		7,579,467	6,085,888
1. Gross premium written		7,589,821	6,096,054
2. Reinsurers' share in gross premium written		8,402	8,645
3. Movements in unearned premium reserve and unexpired risk reserve, gross		1,952	1,521
4. Reinsurers' share in movements in unearned premium reserve		-	-
II. Investment income		1,762,772	1,689,929
1. Income from property		424	490
2. Income from investments in related entities		1,174	2,376
2.1. from shares		103	134
2.2. from loans and debt securities		1,071	2,242
2.3. from other investments		-	-
3. Income from other financial investments		1,200,230	1,270,192
3.1. from shares and other variable income securities, participation units and investment certificates in investment funds		62,773	49,437
3.2. debt securities and other fixed income securities		1,104,444	1,199,728
3.3. term deposits with financial institutions		29,448	21,027
3.4. other deposits		3,565	-
4. Gain on impairment of investments		35,091	20,343
5. Gain on realization of investments		525,853	396,528
III. Unrealized gains on investments		574,769	487,934
IV. Other technical income, net of reinsurers' share		19,550	27,785
V. Claims and benefits		4,297,860	3,909,135



Consolidated life insurance revenue account	In PLN thousand	1 January – 31 December 2006	1 January – 31 December 2005
1. Claims and benefits paid out, net of reinsurers' share		4,274,330	3,978,236
1.1. Claims and benefits paid out, gross		4,274,330	3,979,592
1.2. Reinsurers' share in claims and benefits paid out		-	1,356
2. Movements in outstanding claims reserve, net of reinsurers' share		23,530	(69,101)
2.1. Movement in outstanding claims reserve, gross		23,530	(69,101)
2.2. Reinsurers' share in movement in outstanding claims reserve		-	-
VI. Movements in other technical reserves, net of reinsurers' share		2,069,801	1,643,135
1. Movements in life insurance reserves, net of reinsurers' share		673,103	1,046,071
1.1. Movement in life insurance reserves, gross		673,064	1,045,989
1.2. Reinsurers' share in movement in life insurance reserves		(39)	(82)
2. Movements in life insurance technical reserves, net of reinsurers' share, where the investment risk is borne by policyholders		1,384,336	479,968
2.1. Movement in life insurance reserves, gross		1,384,336	479,968
2.2. Reinsurers' share in movement in life insurance reserves		-	-
3. Movements in other reserves defined in Articles of Association, net of reinsurers' share		12,362	117,096
3.1. Movement in other reserves defined in the Articles of Association, gross		12,362	117,096
3.2. Reinsurers' share in movement in other reserves defined in the Articles of Association		-	-
VII. Bonuses and rebates form the insured, net of reinsurers' share		1,704	1,830





Consolidated life insurance revenue account	In PLN thousand	1 January – 31 December 2006	1 January – 31 December 2005
VIII. Insurance activities		895,624	865,786
1. Acquisition expenses		365,259	313,294
– Movements in deferred acquisition costs		13,071	17,125
2. Administrative expenses		532,911	553,947
3. Reinsurance commission and share in reinsurers' profits		2,546	1,455
IX. Costs of investing activities		190,196	136,885
1. Costs of property maintenance		1,347	1,389
2. Other costs of investing activities		34,748	21,460
3. Loss on impairment of investments		4,692	10,275
4. Loss on realization of investments		149,409	103,761
X. Unrealized losses on investments		101,184	56,422
XI. Other technical costs, net of reinsurers' share		74,794	44,090
XII. Net investment income transferred to the consolidated general profit and loss account		22,592	23,512
<b>XIII. Life underwriting result, of which:</b>		<b>2,282,803</b>	<b>1,610,741</b>
– Life underwriting result of related entities		2,282,803	1,610,741



## Consolidated property and casualty insurance revenue account

Consolidated property and casualty insurance revenue account	In PLN thousand	1 January – 31 December 2006	1 January – 31 December 2005
I. Premiums		7,518,997	7,124,261
1. Gross premium written		7,864,287	7,651,536
2. Reinsurers' share in gross premium written		158,640	399,231
3. Movements in unearned premium reserve and unexpired risk reserve, gross		38,265	114,457
4. Reinsurers' share in movements in unearned premium reserve		(148,385)	(13,587)
II. Net investment income transferred from consolidated general profit and loss account		220,581	205,224
III. Other technical income, net of reinsurers' share		32,313	91,435
IV. Claims and benefits		4,335,068	4,297,999
1. Claims and benefits paid out, net of reinsurers' share		4,208,741	4,072,068
1.1. Claims and benefits paid out, gross		4,501,032	4,295,776
1.2. Reinsurers' share in claims and benefits paid out		292,291	223,708
2. Movements in outstanding claims reserve, net of reinsurers' share		126,327	225,931
2.1. Movements in outstanding claims reserve, gross		79,582	159,344
2.2. Reinsurers' share in movements in outstanding claims reserve		(46,745)	(66,587)
V. Movements in other technical reserves, net of reinsurers' share		(151,987)	(60,448)
1. Movements in other technical reserves, gross		(151,987)	(60,448)
2. Reinsurers' share in movements in other technical reserves		-	-



Consolidated property and casualty insurance revenue account	In PLN thousand	1 January – 31 December 2006	1 January – 31 December 2005
VI. Bonuses and rebates for the insured, net of reinsurers' share, including movement in reserve for bonuses and rebates		1,022	-
VII. Insurance activities expenses		2,057,300	1,829,758
1. Acquisition expenses		1,048,147	941,780
– Movements in deferred acquisition costs		(22,378)	5,706
2. Administrative expenses		1,110,286	976,832
3. Reinsurance commission and share in reinsurers' profits		101,133	88,854
VIII. Other technical costs, net of reinsurers' share		223,588	330,910
IX. Movements in risk equalization reserve		12,467	2,047
X. Property and casualty underwriting result, of which:		1,294,433	1,020,654
– Property and casualty underwriting result of related entities		(106,638)	–



## Consolidated general profit and loss account

Consolidated general profit and loss account	In PLN thousand	1 January – 31 December 2006	1 January – 31 December 2005
I. Property and casualty and life underwriting result		3,577,236	2,631,395
II. Investment income		1,363,915	1,276,382
1. Income from property		21,194	20,703
2. Income from investments in related entities		466	793
2.1. shares		466	542
2.2. loans and debt securities		-	251
2.3. other investments		-	-
3. Income from other financial investments		980,410	1,003,218
3.1. shares, other variable income securities, participation units and investment certificates in investment funds		66,195	99,025
3.2. debt securities and other fixed income securities		839,720	870,566
3.3. term deposits with financial institutions		15,491	14,336
3.4. other investments		59,004	19,291
4. Gain on impairment of investments		8,626	30,642
5. Gain on realization of investments		353,219	221,026
III. Unrealized gains on investments		222,455	280,721
IV. Net investment income transferred from the consolidated life insurance technical account		22,592	23,512



Consolidated general profit and loss account	In PLN thousand	1 January – 31 December 2006	1 January – 31 December 2005
V. Costs of investing activities		196,922	74,653
1. Costs of property maintenance		13,410	13,333
2. Other costs of investing activities		13,953	13,753
3. Loss on impairment of investments		705	7,341
4. Loss on realization of investments		168,854	40,226
VI. Unrealized losses on investments		149,316	34,522
VII. Net investment income transferred to the consolidated property and casualty insurance revenue account		220,581	205,224
VIII. Other operating income		288,781	274,488
IX. Other operating expenses		281,490	178,400
X. Operating profit (loss)		4,626,670	3,993,699
XI. Extraordinary gains		102	64
XII. Extraordinary losses		20	45
XIII. Amortization of goodwill of related entities		9,515	1,871
XIV. Amortization of negative goodwill of related entities		-	-
XV. Gross profit (loss)		4,617,237	3,991,847
XVI. Corporate income tax		910,874	777,055
a) Current tax		973,565	723,876
b) Deferred tax		(62,691)	53,179
XVII. Other obligatory decreases of profit / increases of loss		-	-
XVIII. Share in net profits (losses) of related entities valued using equity method		-	-
XIX. (Profit) loss of minority shareholders		93	-
XX. Net profit (loss)		3,706,456	3,214,75



Consolidated general profit and loss account	In PLN thousand	1 January – 31 December 2006	1 January – 31 December 2005
Annualized net profit/(loss)		3,706,456	3,214,792
Weighted average of ordinary share		86,352,300	86,352,300
Profit (loss) per ordinary share (in PLN)		42,92	37,23
Diluted weighted average of ordinary shares		86,352,300	86,352,300
Diluted profit/loss per ordinary share (in PLN)		42,92	37,23



## Consolidated cash flow statement

Consolidated cash flow statement	In PLN thousand	1 January – 31 December 2006	1 January – 31 December 2005
A. Net cash flow from operating activities		-	-
I. Inflows		18,895,850	16,879,356
1. Cash inflows from direct insurance and reinsurance inwards		15,783,983	13,883,038
1.1. gross premium written		15,588,998	13,715,054
1.2. Salvages and subrogations		131,896	130,628
1.3. Other		63,089	37,356
2. Cash inflows from reinsurance outwards		246,084	437,653
2.1. Cash inflows from reinsurers due to share in claims paid		211,642	291,009
2.2. Cash inflows from reinsurance commission and share in reinsurers' profits		29,973	137,844
2.3. Other cash inflows from reinsurance outwards		4,469	8,800
3. Cash inflows from other operating activities		2,865,783	2,558,665
3.1. Cash inflows from loss adjusting services rendered		43,492	43,639
3.2. Sale of intangible assets and tangible fixed assets other than investments		3,910	3,775
3.3. Other cash inflows		2,818,381	2,511,251
II. Cash outflows		16,010,291	15,506,191
1. Cash outflows from direct insurance and reinsurance inwards		11,944,523	11,171,514
1.1. Gross premium returns		135,731	129,946
1.2. Claims and benefits paid out, gross		8,296,497	7,949,539
1.3. Acquisition costs		1,110,451	985,581
1.4. Administrative expenses		1,940,982	1,797,950
1.5. Costs of loss adjusting and subrogation collection		298,249	244,819





Consolidated cash flow statement	In PLN thousand	1 January – 31 December 2006	1 January – 31 December 2005
1.6. Commissions paid out and shares in profits from reinsurance inwards		3,062	1,899
1.7. Other outflows		159,551	61,780
2. Cash outflows from reinsurance outwards		268,792	581,811
2.1. Premiums paid in respect of reinsurance outwards		239,282	543,818
2.2. Other outwards reinsurance expenses		29,510	37,993
3. Other operating expenses		3,796,976	3,752,866
3.1. Expenses relating to loss adjusting services rendered		32,171	41,425
3.2. Purchase of intangible assets and tangible fixed assets other than investments		124,388	220,112
3.3. Other		3,640,417	3,491,329
III. Net cash flows from operating activities (I – II)		2,885,559	1,373,165
B. Net cash flow from investing activities		-	-
I. Inflows		557,717,351	274,346,211
1. Sale of property		-	894
2. Sale of shares in related entities		-	48
3. Sale of shares in other entities, participation units and investment certificates in investment funds		4,962,566	2,249,747
4. Sale of debt securities issued by related entities and loans repaid by those entities		20,957	36,792
5. Sale of debt securities issued by other entities		25,396,365	18,194,598
6. Withdrawal of term deposits with financial institutions		215,541,835	144,904,989
7. Sale of other investments		310,595,167	107,755,218



Consolidated cash flow statement	In PLN thousand	1 January – 31 December 2006	1 January – 31 December 2005
8. Cash inflows from property		24,735	25,570
9. Interest received		1,061,028	1,054,397
10. Dividends received		104,680	120,538
11. Other investment inflows		10,018	3,420
II. Cash outflows		559,214,497	274,973,253
1. Purchase of property		3,974	4,711
2. Purchase of shares in related entities		10,301	116,865
3. Purchase of shares in other entities, participation units and investment certificates in investment funds		4,863,804	2,101,406
4. Purchase of debt securities issued by related entities and loans granted to those entities		19,219	2,241
5. Purchase of debt securities issued by other entities		25,767,097	18,813,454
6. Creation of creation of term deposits with financial institutions		216,031,178	145,191,376
7. Acquisition of other investments		312,412,028	108,641,482
8. Cash outflows for property maintenance		49,814	62,467
9. Other investments and outflows		57,082	39,251
III. Net cash flows from investing activities (I – II)		(1,497,146)	(627,042)
C. Cash flow from financing activities		-	-
I. Inflows		7,463	-
1. Net inflow from issuance of shares and additional payments to share capital		-	-
2. Loans and credits, and issuance of debt securities		6,538	-
3. Other		925	-



Consolidated cash flow statement	In PLN thousand	1 January – 31 December 2006	1 January – 31 December 2005
II. Outflows		1,349,776	707,119
1. Dividends paid		1,342,468	707,119
2. Cash outflows due to appropriation of profit other than payments to shareholders		-	-
3. Re-acquisition of own shares		-	-
4. Repayment of loans and credits, and redemption of own debt securities		6,542	-
5. Interest on loans and credits and debt securities issued		-	-
6. Other cash outflows from financing activities		766	-
III. Net cash flow from financing activities (I – II)		(1,342,313)	(707,119)
D. Total net cash flow (A.III +/- B.III +/- C.III)		46,100	39,004
E. Balance sheet change in cash and cash equivalents, of which:		43,913	38,941
– Change in cash and cash equivalents due to foreign exchange differences		(2,187)	(63)
F. Cash and cash equivalents at the beginning of period		317,824	278,883
G. Cash and cash equivalents at the end of period (F +/- D),		361,737	317,824
– of restricted use		142,921	163,128



## Consolidated statement of changes in equity

Consolidated statement of changes in equity	In PLN thousand	1 January – 31 December 2006	1 January – 31 December 2005
I. Shareholders' equity at the beginning of the period		10,892,938	8,365,504
a) changes in accounting policies		-	-
b) adjustments due to errors		-	-
I. a. Shareholders' equity at the beginning of the period, after adjustments		10,892,938	8,365,504
1. Share capital at the beginning of the period		86,352	86,352
1.1. Changes in share capital		-	-
a) increases		-	-
b) decreases		-	-
1.2. Share capital at the end of the period		86,352	86,352
2. Unpaid share capital at the beginning of the period		-	-
2.1. Changes in unpaid share capital		-	-
a) increases		-	-
b) decreases		-	-
2.2. Unpaid share capital at the end of the period		-	-
3. Treasury shares at the beginning of the period		-	-
3.1. Changes in treasury shares		-	-
a) increases		-	-
b) decreases		-	-
3.2. Treasury shares at the end of the period		-	-
4. Reserve capital at the beginning of period		6,536,323	5,810,652
a) changes in accounting policies		-	-
b) adjustments due to errors		-	-



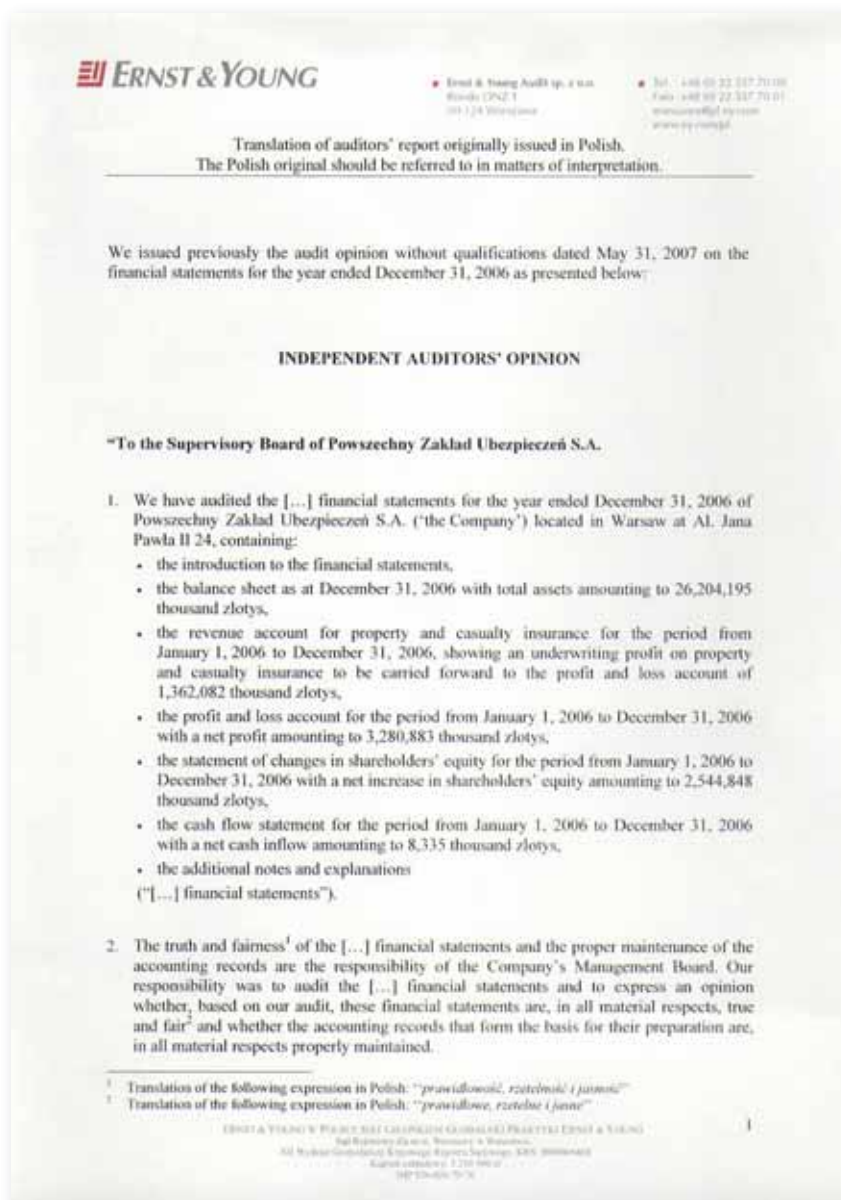
Consolidated statement of changes in equity	In PLN thousand	1 January – 31 December 2006	1 January – 31 December 2005
4.1. Reserve capital at the beginning of the period, after adjustments		6,536,323	5,810,652
4.2. Changes in reserve capital		1,333,370	725,671
a) increases		1,333,370	725,678
– dividends paid out (in excess of legal requirements)		1,333,287	725,158
– from revaluation reserve		83	520
b) decreases		-	7
– other		-	7
4.3. Reserve capital at the end of the period		7,869,693	6,536,323
5. Revaluation reserve at the beginning of the period		192,650	149,982
a) changes in accounting policies		-	(7,406)
b) adjustments due to errors		-	-
5.1. Revaluation reserve at the beginning of period, after adjustments		192,650	142,576
5.2. Revaluation reserve		108,761	50,074
a) increases (due to)		250,558	119,455
– valuation of financial investments		250,558	119,455
b) decreases (due to)		141,797	69,381
– disposal and liquidation of fixed assets		83	520
– valuation of financial investments		141,714	68,861
5.3. Revaluation reserve at the end of the period		301,411	192,650
6. Other reserves at the beginning of the period		-	-



Consolidated statement of changes in equity	In PLN thousand	1 January – 31 December 2006	1 January – 31 December 2005
6.1. Changes in other reserves		-	-
a) increases (due to)		-	-
b) decreases (due to)		-	-
6.2. Other reserves at the end of the period		-	-
7. Foreign exchange differences of subordinated entities		145	-
8. Accumulated profits/(losses) from previous years at the beginning of period		4,077,613	2,318,518
8.1. Accumulated profits/(losses) from previous years at the beginning of the period		4,077,613	2,318,518
a) changes in accounting policies		-	7,406
b) adjustments due to errors		-	-
8.2. Accumulated profits/(losses) from previous years at the beginning of period, after adjustments		4,077,613	2,325,924
a) increases		-	-
b) decreases (due to)		2,710,783	1,463,103
– dividends paid		1,347,096	708,088
– transfer to reserve capital		1,333,287	725,158
– contribution to social fund		30,400	29,857
8.3. Accumulated profits/(losses) from previous years at the end of the period		1,366,830	862,821
9. Net result		3,706,456	3,214,792
a) net profit		3,706,456	3,214,792
b) net loss		-	-
c) deductions from net profit		-	-
II. Shareholders' equity at the end of the period		13,330,887	10,892,938
III. Shareholders' equity after proposed appropriation of profits/ (absorption of losses)		13,300,737	9,525,842



## III. Financial statements – PZU SA







Translation of auditors' report originally issued in Polish.  
The Polish original should be referred to in matters of interpretation.

3. We conducted our audit of the [...] financial statements in accordance with the following regulations being in force in Poland:

- chapter 7 of the Accounting Act, dated September 29, 1994 ("the Accounting Act"),
- the auditing standards issued by the National Chamber of Auditors,

in order to obtain reasonable assurance whether these financial statements are free of material misstatement. In particular, the audit included examining, to a large extent on a test basis, documentation supporting the amounts and disclosures in the [...] financial statements. The audit also included assessing the accounting principles adopted and used and significant estimates made by Management Board, as well as evaluating the overall presentation of the [...] financial statements. We believe our audit has provided a reasonable basis to express our opinion on the [...] financial statements treated as a whole.

4. In our opinion, the [...] financial statements, in all material respects:

- present truly and fairly all information material for the assessment of the results of the Company's operations for the period from January 1, 2006 to December 31, 2006, as well as its financial position<sup>1</sup> as at December 31, 2006;
- have been prepared in accordance with the accounting principles specified in the Accounting Act and regulations issued based on that Act and based on properly maintained accounting records;
- are in accordance with the Accounting Act and regulations issued based on that Act and the provisions of the Company's statute that affect their content.

5. We have read the Directors' Report for the period from January 1, 2006 to December 31, 2006 ("the Directors' Report") and concluded that the information derived from the [...] financial statements reconciles with these financial statements. The information included in the Directors' Report corresponds with art. 49 of the Accounting Act and the Appendix 5 to the Decree of the Minister of Finance of December 8, 2003 on specific accounting principles for insurance companies.

6. The financial statements are accompanied by the actuary's opinion on creation of technical reserves, calculated using methods applied in insurance mathematics."

<sup>1</sup> Translation of the following expression in Polish: "sytuacji majątkowa i finansowa"





Translation of auditors' report originally issued in Polish.  
The Polish original should be referred to in matters of interpretation.

In our opinion the information presented in the published, condensed financial statements on pages 168 to 185 of this annual report is in all material respects fairly stated in relation to the consolidated financial statements from which it has been derived. The financial statements that were audited by us include notes that were not fully presented in the attached condensed financial statements. In order for the reader to obtain a true and fair view of the state of affairs of the Company as at December 31, 2006 and the results of its operations for the period from January 1, 2006 to December 31, 2006, the reader must review the full financial statements in their entirety including supporting schedules and statutory disclosures as required by the Accounting Act and the regulations based thereof.

On behalf of  
Ernst & Young Audit Sp. z o.o.  
Rondo ONZ 1, 00-124 Warszawa  
Reg. No. 130

Marcin Dyrnek  
Certified Auditor No. 9899/7370

Dominik Januszczyński  
Certified Auditor No. 9707/7255

Warsaw, October 31, 2007

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## Balance sheet of PZU SA

Assets	In PLN thousand	31 December 2006	31 December 2005
<b>A. Intangible assets</b>		<b>25,808</b>	<b>18,203</b>
1. Goodwill		-	-
2. Other intangible assets and advances for intangible assets		25,808	18,203
<b>B. Investments</b>		<b>24,050,156</b>	<b>21,042,659</b>
<b>I. Property</b>		<b>341,827</b>	<b>352,181</b>
1. Freehold land, including perpetual usufruct		40,698	41,027
2. Buildings and constructions, and cooperative freehold right		287,452	283,356
3. Construction in progress and advances for construction in progress		13,677	27,798
<b>II. Investments in related entities</b>		<b>4,778,943</b>	<b>4,237,063</b>
1. Shares in related entities		4,728,378	4,173,286
2. Loans granted to related entities and debt securities issued by related entities		50,565	63,677
3. Other		-	100
<b>III. Other financial investments</b>		<b>18,920,742</b>	<b>16,445,739</b>
1. Shares and other variable income securities, participation units and investment certificates in investment funds		1,807,914	1,598,659
2. Debt securities and other fixed income securities		14,779,786	13,036,325
3. Shares in joint venture investments		-	-
4. Mortgage loans		-	-
5. Other loans		1,969,433	1,565,523
6. Term deposits with financial institutions		358,361	245,232
7. Other investments		5,248	-



Assets	In PLN thousand	31 December 2006	31 December 2005
IV. Deposits due from cedants		8,644	7,676
C. Net life insurance where the policyholder bears the investment risk		-	-
D. Receivables		1,206,748	1,228,506
I. Receivables from direct insurance		953,138	987,512
1. Receivables from policyholders		916,940	968,613
1.1. From related entities		37	43
1.2. From other entities		916,903	968,570
2. Receivables from insurance intermediaries		28,469	18,221
2.1. From related entities		-	761
2.2. From other entities		28,469	17,460
3. Other receivables		7,729	678
3.1. From related entities		80	110
3.2. From other entities		7,649	568
II. Receivables from reinsurance		27,107	60,014
1. From related entities		372	2,522
2. From other entities		26,735	57,492
III. Other receivables		226,503	180,980
1. Receivables from the State Budget		90,457	101,061
2. Other receivables		136,046	79,919
2.1. From related entities		17,593	21,941
2.2. From other entities		118,453	57,978

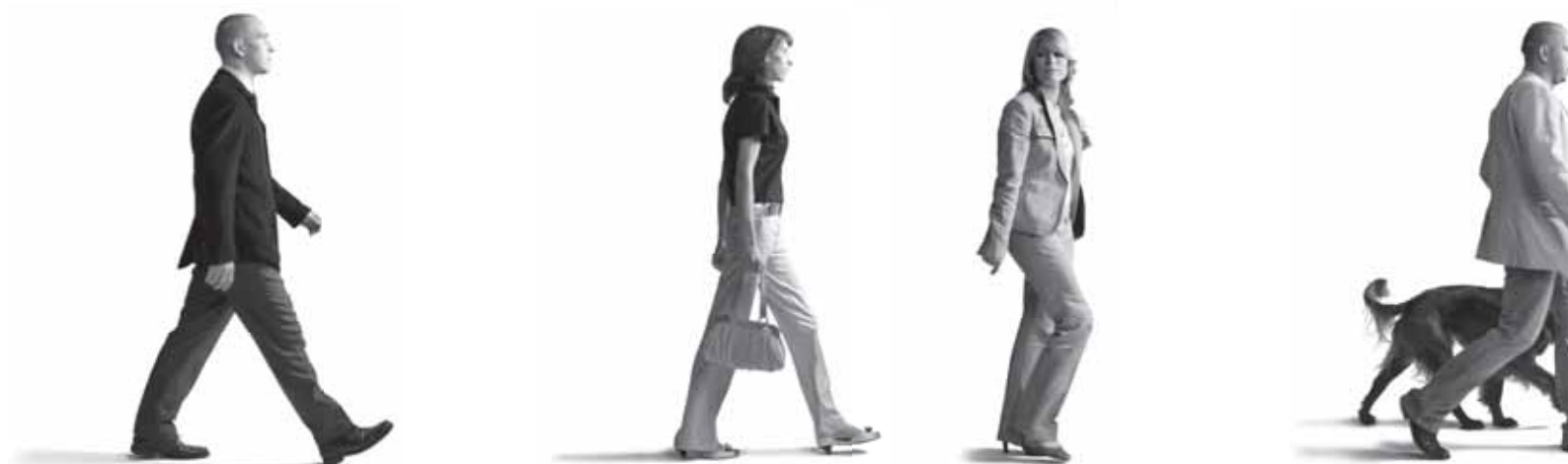


Assets	In PLN thousand	31 December 2006	31 December 2005
E. Other assets		393,005	431,304
I. Tangible assets		184,997	231,631
II. Cash and cash equivalents		208,008	199,673
III. Other		-	-
F. Prepayments and deferred costs		528,478	393,802
I. Deferred tax assets		-	-
II. Deferred acquisition costs		304,472	270,812
III. Accrued interest and rental charges		142	177
IV. Other prepayments and deferred costs		223,864	122,813
Assets, total		26,204,195	23,114,474

Equity and liabilities	In PLN thousand	31 December 2006	31 December 2005
A. Equity		13,448,705	10,903,857
I. Share capital		86,352	86,352
II. Unpaid share capital (negative value)		-	-
III. Treasury shares (negative value)		-	-
IV. Reserve capital		5,564,534	4,231,167
V. Revaluation reserve		4,516,936	3,885,956
VI. Other reserves		-	-
VII. Accumulated profits/(losses) from previous years		-	7,406
VIII. Net profit/(loss)		3,280,883	2,692,976
B. Subordinated liabilities		-	-
C. Technical reserves		11,955,358	12,017,632



Equity and liabilities	In PLN thousand	31 December 2006	31 December 2005
I. Unearned premium reserve and unexpired risk reserve		3,551,334	3,519,196
II. Life insurance reserves		-	-
III. Outstanding claims reserve		7,450,508	7,404,779
IV. Reserve for bonuses and rebates for the insured		-	-
V. Risk equalization reserve		572,801	560,955
VI. Reserve for premium returns for policyholders		-	-
VII. Other technical reserves as defined in Articles of Association		380,715	532,702
VIII. Life insurance technical reserve where investment risk is borne by policyholders		-	-
D. Reinsurers' share in technical reserves (negative value)		(1,163,304)	(1,351,258)
I. Reinsurers' share in unearned premium reserve and unexpired risk reserve		(23,901)	(160,341)
II. Reinsurers' share in life insurance reserve		-	-
III. Reinsurers' share in outstanding claims reserve		(1,139,403)	(1,190,917)
IV. Reinsurers' share in reserve for bonuses and rebates for the insured		-	-
V. Reinsurers' share in other technical reserves defined in Articles of Association		-	-
VI. Reinsurers' share in life insurance technical reserve where investment risk is borne by policyholders		-	-
E. Estimated salvages and subrogations (negative value)		(48,805)	(64,210)
1. Estimated salvages and subrogations, gross		(49,196)	(64,895)
2. Reinsurers' share in estimated salvages and subrogations		391	685
F. Other provisions		389,575	384,410
I. Provision for retirement benefits and similar obligations		214,263	220,355



Equity and liabilities	In PLN thousand	31 December 2006	31 December 2005
II. Deferred tax liability		153,861	142,850
III. Other		21,451	21,205
G. Liabilities from reinsurance deposits		34	66
H. Other liabilities and special funds		1,109,068	526,549
I. Direct insurance liabilities		198,865	112,558
1. Liabilities to policyholders		40,762	20,648
1.1. To related entities		1	-
1.2. To other entities		40,761	20,648
2. Liabilities to insurance intermediaries		63,748	60,138
2.1. To related entities		-	30
2.2. To other entities		63,748	60,108
3. Other insurance liabilities		94,355	31,772
3.1. To related entities		779	798
3.2. To other entities		93,576	30,974
II. Reinsurance liabilities		31,396	59,842
1. To related entities		372	4,534
2. To other entities		31,024	55,308
III. Liabilities from issuance of own debt securities and loans taken out		-	-
1. Liabilities convertible to INSURER'S shares		-	-
2. Other		-	-
IV. Liabilities to financial institutions		2	10
V. Other liabilities		735,829	214,972
1. Liabilities to the State Budget		20,944	21,512
2. Other		714,885	193,460





Equity and liabilities	In PLN thousand	31 December 2006	31 December 2005
2.1. To related entities		29,454	27,473
2.2. To other entities		685,431	165,987
VI. Special funds		142,976	139,167
I. Accruals and deferred income		513,564	697,428
1. Accrued expenses		406,955	543,261
2. Negative goodwill		-	-
3. Deferred income		106,609	154,167
Total equity and liabilities		26,204,195	23,114,474

Off-balance sheet items	In PLN thousand	31 December 2006	31 December 2005
1. Contingent receivables,		3,186,142	2,320,197
1.1. Guarantees received		4,342	2,776
1.2. Other		3,181,800	2,317,421
2. Contingent liabilities,		57,448	66,801
2.1. Guarantees issued		10,916	10,390
2.2. Bills of exchange accepted and endorsed		-	-
2.3. Buy and sell back assets		-	-
2.4. Other liabilities		-	-
2.5. Disputed claims nor recognized by Company and pursued by creditors in court		45,929	55,604
3. Reinsurance guarantees made to Company		-	-



Off-balance sheet items	In PLN thousand	31 December 2006	31 December 2005
4. Reinsurance guarantees made by Company to cedants		-	-
5. Third party assets not included in Company assets		680,977	583,937
6. Other off-balance sheet items,		62,638	64,809
6.1. Security established on Company assets		62,638	63,760
6.2. Other off-balance sheet items		-	1,049
Own funds		11,743,970	9,248,377
Solvency margin		1,169,545	1,182,191
Surplus (shortage) of own funds to cover solvency margin		10,574,425	8,066,186
Technical reserves, gross*		11,906,162	11,952,737
Assets to cover technical reserves		20,117,019	17,606,334
Surplus (shortage) of assets to cover technical reserves		8,210,857	5,653,597

\* Following deduction of estimated gross recourses and recoveries



## Property and casualty insurance revenue account of PZU SA

Revenue account of property and casualty insurance	In PLN thousand	1 January – 31 December 2006	1 January – 31 December 2005
I. Premiums (1 – 2 +/- 3 +/- 4)		7,383,274	7,126,391
1. Gross premiums written in the accounting year		7,677,355	7,653,607
2. Reinsurers' share in the gross premium written		125,503	399,231
3. Movement in unearned premium reserve and unexpired risk reserve, gross		32,138	114,398
4. Reinsurers' share in movement in unearned premium reserve		(136,440)	(13,587)
II. Net investment incomes taking account of costs, carried over from the general profit and loss account		214,684	205,224
III. Other technical income, net of reinsurers' share		30,660	91,435
IV. Claims and benefits (1 +/- 2)		4,215,061	4,299,534
1. Claims and benefits paid out, net of reinsurers' share		4,102,413	4,073,603
1.1. Claims and benefits paid out, gross		4,368,448	4,297,311
1.2. Reinsurers' share of claims and benefits paid out		266,035	223,708
2. Movement in outstanding claims reserve, net of reinsurers' share		112,648	225,931
2.1. Movement in outstanding claims reserve, gross		61,428	159,344
2.2. Reinsurers' share in movement in outstanding claims reserve		(51,220)	(66,587)
V. Movement in other technical reserves, net of reinsurers' share		(151,987)	(60,448)
1. Movement in other technical reserves, gross		(151,987)	(60,448)
2. Reinsurers' share in movement in life insurance reserves		-	-



Revenue account of property and casualty insurance	In PLN thousand	1 January – 31 December 2006	1 January – 31 December 2005
VI. Bonuses and rebates for the insured net of reinsurers' share		-	-
VII. Insurance activities expenses(1 + 2 – 3)		1,974,327	1,868,845
1. Acquisition expenses:		1,004,348	950,108
1.1. movement in deferred acquisition costs		(33,660)	5,706
2. Administrative expenses		1,066,050	1,007,591
3. Reinsurance commissions and shares in reinsurers' profits		96,071	88,854
VIII. Other technical expenses, net of reinsurers' share		217,289	330,910
IX. Movement in risk equalization reserve		11,846	2,047
IX. Underwriting result on property and casualty insurance and life insurance		1,362,082	982,162



## General profit and loss account of PZU SA

General profit and loss account	In PLN thousand	1 January – 31 December 2006	1 January – 31 December 2005
I. Underwriting result on property and casualty insurance		1,362,082	982,162
II. Investment incomes (1 + 2 + 3 + 4 + 5)		2,730,906	2,193,085
1. Income from property		5,256	8,307
2. Income from investments in related entities		1,408,746	961,524
2.1. shares		1,405,674	956,665
2.2. loans and debt securities		3,072	4,859
2.3. other investments		-	-
3. Income from other financial investments		963,838	994,469
3.1. shares, variable income securities, participation units and certificates in investment funds		65,294	98,866
3.2. debt securities and other fixed income securities		832,380	866,781
3.3. term deposits with financial institutions		7,532	9,531
3.4. other investments		58,632	19,291
4. Gains on impairment of investments		1,910	7,759
5. Gains on realization of investments		351,156	221,026
III. Unrealized gains on investments		194,586	285,484
IV. Net investment income less costs, carried over from life revenues account		-	-
V. Cost of investing activities (1 + 2 + 3 + 4)		182,095	63,422
1. Costs of property maintenance		353	2,102
2. Other costs of investing activities		13,711	13,753



General profit and loss account	In PLN thousand	1 January – 31 December 2006	1 January – 31 December 2005
3. Loss on impairment of investments		705	7,341
4. Loss on realization of investments		167,326	40,226
VI. Unrealized losses on investments		159,605	103,947
VII. Net investment income less costs, carried over to revenue account of property and casualty insurance and life		214,684	205,224
VIII. Other operating income		38,137	71,081
IX. Other operating expenses		32,122	41,867
X. Operating profit/ (loss)		3,737,205	3,117,352
XI. Extraordinary gains		102	79
XII. Extraordinary losses		7	32
XIII. Gross profit (loss)		3,737,300	3,117,399
XIV. Income tax		456,417	424,423
XV. Other obligatory decreases of profit/ increases of loss		-	-
XVI. Net profit (loss)		3,280,883	2,692,976



## Cash flow statement of PZU SA

Cash flow statement	In PLN thousand	1 January – 31 December 2006	1 January – 31 December 2005
<b>A. Net cash flow from operating activities</b>		<b>845,666</b>	<b>595,923</b>
<b>I. Inflows</b>		<b>10,757,319</b>	<b>10,538,292</b>
1. Cash inflows from direct insurance and reinsurance inwards		7,899,902	7,743,549
1.1. Gross premium written		7,728,433	7,604,098
1.2. Salvages and subrogations		127,417	130,628
1.3. Other		44,052	8,823
2. Cash inflows from reinsurance outwards		234,285	434,842
2.1. Cash inflows from reinsurers' share in claims paid		202,389	289,653
2.2. Cash inflows from reinsurance commission and the share in reinsurers' profits		27,427	136,389
2.3. Other		4,469	8,800
3. Cash inflows from other operating activities		2,623,132	2,359,901
3.1. Proceeds from loss adjusting services rendered		41,733	43,639
3.2. Sales of intangible assets and tangible fixed assets other than investments		2,113	2,260
3.3. Other inflows		2,579,286	2,314,002
<b>II. Outflows</b>		<b>9,911,653</b>	<b>9,942,369</b>
1. Cash outflows from direct insurance and reinsurance inwards		6,669,227	6,459,955
1.1. Gross premiums returns		134,221	129,946
1.2. Claims and benefits paid out, gross		4,022,861	4,096,645
1.3. Acquisition expenses		727,020	665,559
1.4. Administrative expenses		1,490,916	1,416,832





Cash flow statement	In PLN thousand	1 January – 31 December 2006	1 January – 31 December 2005
1.5. Costs of loss adjusting services and subrogation collection		150,271	115,616
1.6. Commissions paid out and the share in profits from reinsurance inwards		3,062	1,899
1.7. Other outflows		140,876	33,458
2. Cash outflows from reinsurance outwards		229,625	573,166
2.1. Premiums paid in respect of reinsurance outwards		200,280	535,173
2.2. Other outwards reinsurance expenses		29,345	37,993
3. Other operating expenses		3,012,801	2,909,248
3.1. Expenses relating to loss adjusting services rendered		32,171	41,425
3.2. Purchase of intangible assets and tangible fixed assets other than investments		79,999	170,708
3.3. Other		2,900,631	2,697,115
<b>B. Net cash flow from investing activity</b>		<b>505,141</b>	<b>134,436</b>
I. Inflows		267,800,360	117,410,609
1. Sale of property		-	894
2. Sale of shares in related entities		-	-
3. Sale of shares in other entities, participation units and investment certificates in investment funds		1,514,252	569,864
4. Sale of debt securities issued by related entities and loans repaid by those entities		7,107	17,104
5. Sale of debt securities issued by other entities		16,426,294	8,874,260
6. Withdrawal of term deposits from financial institutions		79,595,749	45,916,177
7. Sale of other investments		169,035,504	61,149,499
8. Inflows from property		5,923	9,876
9. Interest received		23,087	15,166
10. Dividends received		1,191,452	854,900



Cash flow statement	In PLN thousand	1 January – 31 December 2006	1 January – 31 December 2005
11. Other inflows		992	2,869
II. Outflows		267,295,219	117,276,173
1. Purchase of property		-	61
2. Purchase of shares in related entities		116,240	116,865
3. Purchase of shares in other entities, participation units and investment certificates in investment funds		1,205,430	340,560
4. Purchase of debt securities issued by related entities and loans granted to those entities		-	2,241
5. Purchase of debt securities issued by other entities		17,319,464	8,780,710
6. Creation of term deposits with financial institutions		79,715,267	45,908,544
7. Acquisition of other investments		168,907,688	62,082,559
8. Outflows for property maintenance		16,395	27,430
9. Other investment outflows		14,735	17,203
C. Net cash flow from financing activities		(1,342,472)	(707,119)
I. Inflows		6,538	-
1. Net inflow from issuance of shares and additional payments to share capital		-	-
2. Loans and credits and issuance of debt securities		6,538	-
3. Other		-	-
II. Outflows		1,349,010	707,119
1. Dividends paid		1,342,468	707,119
2. Outflows due to appropriation of profit other than payments to shareholders		-	-
3. Re-acquisition of own shares		-	-
4. Repayment of loans and credits and redemption of debt securities		6,542	-



Cash flow statement	In PLN thousand	1 January – 31 December 2006	1 January – 31 December 2005
5. Interest on loans and credits and debt securities issued		-	-
6. Other outflows from financing activities		-	-
D. Total net cash flow		8,335	23,240
E. Balance sheet change in cash, and cash equivalents, of which:		8,335	23,240
1. change in cash and cash equivalents due to foreign exchange differences		(17)	(63)
F. Cash and cash equivalents at the beginning of the period		199,673	176,433
G. Cash and cash equivalents at the end of the period:		208,008	199,673
1. – of restricted use		89,491	112,464



## Statement of changes in equity of PZU SA

Statement of changes in equity	In PLN thousand	1 January – 31 December 2006	1 January – 31 December 2005
I. Shareholders' equity at the beginning of the period		10,903,857	8,440,374
a) changes in accounting policies		-	-
b) adjustment due to errors		-	-
I. a. Shareholders' equity at the beginning of the period, after adjustments		10,903,857	8,440,374
1. Share capital at the beginning of the period		86,352	86,352
1.1. Changes in share capital		-	-
a) increase		-	-
b) decrease		-	-
1.2. Share capital at the end of the period		86,352	86,352
2. Unpaid share capital at the beginning of the period		-	-
2.1. Changes in unpaid share capital		-	-
a) increase		-	-
b) decrease		-	-
2.2. Unpaid share capital at the end of the period		-	-
3. Treasury shares at the beginning of the period		-	-
3.1. Changes in treasury shares		-	-
a) increase		-	-
b) decrease		-	-
3.2. Treasury shares at the end of the period		-	-
4. Reserve capital at the beginning of the period		4,231,167	3,510,902
4.1. Changes in reserve capital		1,333,367	720,265
a) increases:		1,333,367	720,272



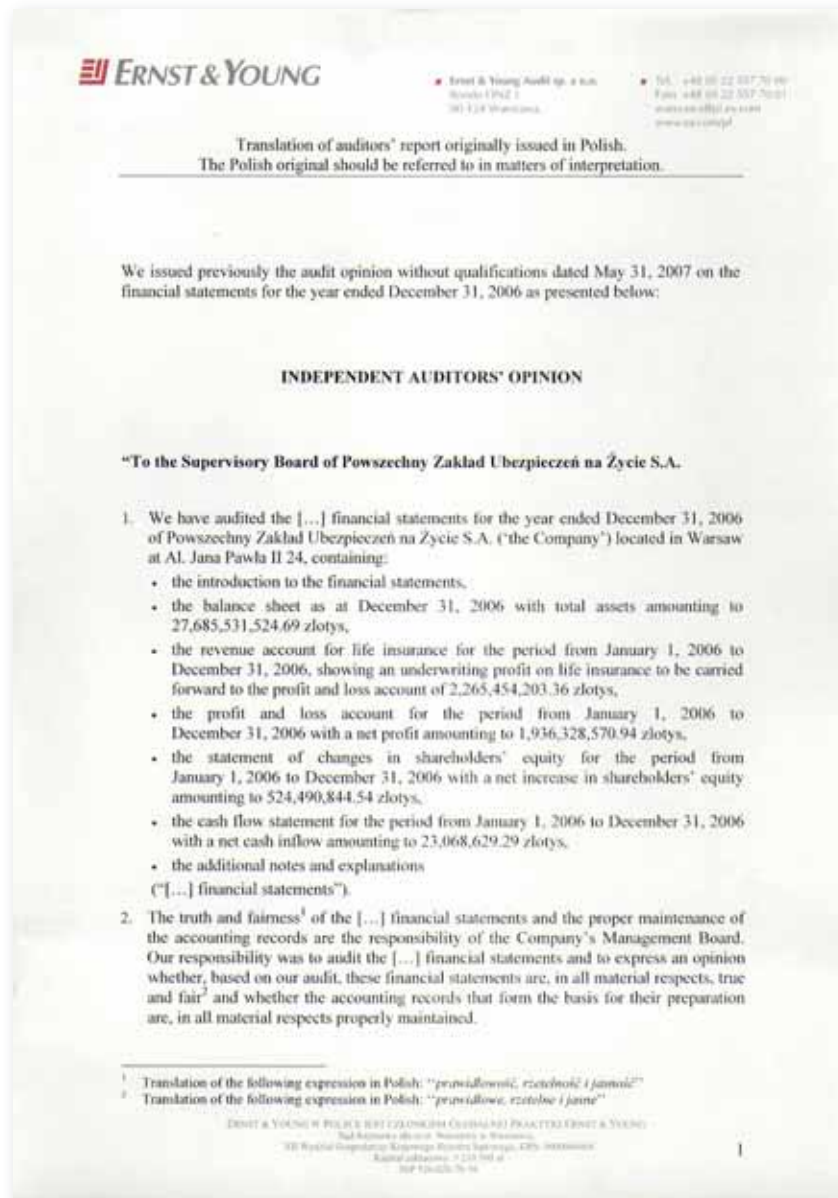
Statement of changes in equity	In PLN thousand	1 January – 31 December 2006	1 January – 31 December 2005
– share issues in excess of par		-	-
– dividends paid out (statutory)		-	-
– dividends paid out (in excess of legal requirements)		1,333,286	719,809
– from revaluation reserve		81	463
b) decreases:		-	7
– loss coverage		-	-
– other decrease		-	7
4.2. Reserve capital at the end of the period		5,564,534	4,231,167
5. Revaluation reserve at the beginning of the period		3,885,956	3,395,223
a) changes in accounting policies		-	(7,406)
b) adjustments due to errors		-	-
5a. Revaluation reserve at the beginning of the period, after adjustments		3,885,956	3,387,817
5.1. Revaluation reserve		630,980	498,139
a) increases (due to):		771,695	567,463
– valuation of financial investments		771,695	567,463
b) decreases (due to):		140,715	69,324
– valuation of long-term financial investments		140,634	68,861
– valuation of property		-	-
– disposal and liquidation of fixed assets		81	463
5.2. Revaluation reserve at the end of the period		4,516,936	3,885,956
6. Other reserves at the beginning of the period		-	-
6.1. Changes of other reserves		-	-
6.2. Other reserves at the end of the period		-	-
7. Accumulated profits/(losses) from previous years at the beginning of the period		2,700,382	1,447,897



Statement of changes in equity	In PLN thousand	1 January – 31 December 2006	1 January – 31 December 2005
7.1. Accumulated profits/(losses) from previous years at the beginning of the period		2,700,382	1,447,897
a) changes in accounting policies		-	7,406
b) adjustments due to errors		-	-
7.2. Accumulated profits/(losses) from previous years at the beginning of the period, after adjustments		2,700,382	1,455,303
a) increases		-	-
b) decreases (due to):		2,700,382	1,447,897
– dividends paid out		1,347,096	708,088
– transfer to reserve capital		1,333,286	719,809
– transfer to social fund		20,000	20,000
7.3. Closing balance of profit from previous years		-	7,406
7.4. Closing balance of loss from previous years		-	-
a) changes in accounting policies		-	-
7.5. Closing balance of loss brought forward, after adjustments		-	-
7.6. Closing balance of loss brought forward		-	-
7.7. Closing balance of accumulated profit (loss) from previous years		-	7,406
8. Net result		3,280,883	2,692,976
a) net profit		3,280,883	2,692,976
b) net loss		-	-
II. Shareholders' equity at the end of the period		13,448,705	10,903,857
III. Shareholders' after proposed appropriation of profits / absorption of losses		13,428,705	9,536,761



## IV. Financial statements – PZU Życie SA





Translation of auditors' report originally issued in Polish.  
The Polish original should be referred to in matters of interpretation.

3. We conducted our audit of the [...] financial statements in accordance with the following regulations being in force in Poland:

- chapter 7 of the Accounting Act, dated September 29, 1994 ("the Accounting Act"),
- the auditing standards issued by the National Chamber of Auditors,

in order to obtain reasonable assurance whether these financial statements are free of material misstatement. In particular, the audit included examining, to a large extent on a test basis, documentation supporting the amounts and disclosures in the [...] financial statements. The audit also included assessing the accounting principles adopted and used and significant estimates made by Management Board, as well as evaluating the overall presentation of the [...] financial statements. We believe our audit has provided a reasonable basis to express our opinion on the [...] financial statements treated as a whole.

4. In our opinion, the [...] financial statements, in all material respects:

- present truly and fairly all information material for the assessment of the results of the Company's operations for the period from January 1, 2006 to December 31, 2006, as well as its financial position<sup>1</sup> as at December 31, 2006;
- have been prepared in accordance with the accounting principles specified in the Accounting Act and regulations issued based on that Act and based on properly maintained accounting records;
- are in accordance with the Accounting Act and regulations issued based on that Act and the provisions of the Company's statute that affect their content.

5. We have read the Directors' Report for the period from January 1, 2006 to December 31, 2006 ("the Directors' Report") and concluded that the information derived from the [...] financial statements reconciles with these financial statements. The information included in the Directors' Report corresponds with art. 49 of the Accounting Act and the Appendix 5 to the Decree of the Minister of Finance of December 8, 2003 on specific accounting principles for insurance companies."

<sup>1</sup> Translation of the following expression in Polish: "sytuacja majątkowa i finansowa"





Translation of auditors' report originally issued in Polish.  
The Polish original should be referred to in matters of interpretation.

In our opinion the information presented in the published, condensed financial statements on pages 189 to 208 of this annual report is in all material respects fairly stated in relation to the consolidated financial statements from which it has been derived. The financial statements that were audited by us include notes that were not fully presented in the attached condensed financial statements. In order for the reader to obtain a true and fair view of the state of affairs of the Company as at December 31, 2006 and the results of its operations for the period from January 1, 2006 to December 31, 2006, the reader must review the full financial statements in their entirety including supporting schedules and statutory disclosures as required by the Accounting Act and the regulations based thereof.

On behalf of  
Ernst & Young Audit Sp. z o.o.  
Rondo ONZ 1, 00-124 Warszawa  
Reg. No. 130

Adam Fornalik  
Certified Auditor No. 9916/7376

Dominik Janaszewski  
Certified Auditor No. 9707/7255

Warsaw, October 31, 2007

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## Balance sheet of PZU Życie SA

Assets	In PLN thousand	31 December 2006	31 December 2005
A. Intangible assets		68,596	71,761
1. Goodwill		-	-
2. Other intangible assets and advances for intangible assets		68,596	71,761
B. Investments		23,889,628	21,661,663
I. Property		219,383	217,037
1. Freehold land, including perpetual usufruct		70,555	70,838
2. Buildings and constructions, and cooperative freehold right		136,105	136,779
3. Construction in progress and advances for construction in progress		12,723	9,420
II. Investments in related entities, of which:		948,698	920,446
1. Shares in related entities		782,577	730,986
2. Loans granted to related entities and debt securities issued by those entities		166,121	189,460
3. Other investments		-	-
III. Other financial investments		22,721,547	20,524,180
1. Shares and other variable income securities, participation units and investment certificates in investment funds		2,326,379	2,295,834
2. Debt securities and other fixed income securities		17,246,819	17,375,854
3. Shares in joint ventures		-	-
4. Mortgage loans		-	-
5. Other loans		2,304,898	353,843



Assets	In PLN thousand	31 December 2006	31 December 2005
6. Term deposits with financial institutions		821,516	498,649
7. Other investments		21,935	-
IV. Deposits due from cedants		-	-
C. Net life insurance assets where the policyholder bears the investment risk		3,161,650	1,778,839
D. Receivables		214,331	157,508
I. Receivables from direct insurance		85,940	87,997
1. Receivables from policyholders		82,734	87,037
1.1. from related entities		-	-
1.2. from other entities		82,734	87,037
2. Other receivables		377	956
2.1. from related entities		-	-
2.2. from other entities		377	956
3. Other receivables, including:		2,829	4
3.1. from related entities		-	-
3.2. from other entities		2,829	4
II. Receivables from reinsurance, including:		-	-
1. from related entities		-	-
2. from other entities		-	-
III. Other receivables, including:		128,391	69,511
1. Receivables from the State Budget		654	40
2. Other receivables, including:		127,737	69,471
2.1. from related entities		1,864	4,786
2.2. from other entities		125,873	64,685



Assets	In PLN thousand	31 December 2006	31 December 2005
E. Other assets		183,504	172,165
I. Tangible assets		42,750	54,900
II. Cash and cash equivalents		139,852	116,783
III. Other		902	482
F. Prepayments and deferred costs		167,823	173,427
I. Deferred tax assets		-	-
II. Deferred acquisition costs		104,395	117,466
III. Accrued interest and rental charge		8,856	3,871
IV. Other prepayments and deferred costs		54,572	52,090
Assets, total		27,685,532	24,015,363

Equity and liabilities	In PLN thousand	31 December 2006	31 December 2005
A. Equity		4,517,269	3,992,778
I. Share capital		295,000	295,000
II. Unpaid share capital (negative value)		-	-
III. Treasury shares (negative value)		-	-
IV. Reserves		2,279,488	2,279,485
V. Revaluation reserve		6,452	3,085
VI. Other reserves		-	-
VII. Accumulated profit (loss) from previous years		-	-
VIII. Net profit (loss)		1,936,329	1,415,208
B. Subordinated liabilities		-	-



Equity and liabilities	In PLN thousand	31 December 2006	31 December 2005
<b>C. Technical reserves</b>		<b>21,458,005</b>	<b>19,362,912</b>
I. Unearned premium reserve and unexpired risk reserve		74,020	72,068
II. Life insurance reserves		16,775,480	16,102,416
III. Outstanding claims reserve		449,109	425,579
IV. Reserve for bonuses and rebates for the insured		1,577	1,728
V. Risk equalization reserve		-	-
VI. Reserves for reimbursing premiums to members		-	-
VII. Other technical reserves, as defined in Articles of Association		996,169	983,807
VIII. Life technical reserves, where the investment risk is borne by policyholders		3,161,650	1,777,314
<b>D. Reinsurers' share in technical reserves (negative value)</b>		<b>-</b>	<b>39</b>
I. Reinsurers' share in unearned premium reserve and unexpired risk reserve		-	-
II. Reinsurers' share in life insurance reserve		-	39
III. Reinsurers' share in outstanding claims reserve		-	-
IV. Reinsurers' share in reserve for bonuses and rebates for the insured		-	-
V. Reinsurers' share in other technical reserves as defined in Articles of Association		-	-
VI. Reinsurers' share in life technical reserves where the investment risk is borne by policyholders		-	-
<b>E. Estimated salvages and subrogations (negative value)</b>		<b>-</b>	<b>-</b>
I. Estimated salvages and subrogations, gross		-	-
II. Reinsurers' share in estimated salvages and subrogations		-	-
<b>F. Other provisions</b>		<b>249,425</b>	<b>283,502</b>



Equity and liabilities	In PLN thousand	31 December 2006	31 December 2005
I. Provision for retirement benefits and similar obligations to employees		63,374	48,370
II. Deferred tax provision		186,051	233,984
III. Other provisions		-	1,148
G. Liabilities from reinsurance deposits		-	-
H. Other liabilities and special funds		1,352,982	319,210
I. Direct insurance liabilities		158,601	140,810
1. Liabilities to policyholders		150,754	135,115
1.1. To related entities		-	-
1.2. To other entities		150,754	135,115
2. Liabilities to insurance intermediaries (agents)		206	172
2.1. To related entities		-	-
2.2. To other entities		206	172
3. Other insurance liabilities, including:		7,641	5,523
3.1. To related entities		-	-
3.2. To other entities		7,641	5,523
II. Reinsurance liabilities, including:		4,229	4,075
1. To related entities		-	-
2. To other entities		4,229	4,075
III. Liabilities from the issuance of own debt securities and loans taken out		-	-
1. Liabilities convertible to INSURER'S shares		-	-
2. Other		-	-
IV. Liabilities to financial institutions		21,596	14,741
V. Other liabilities		1,104,785	106,059





Off-balance items	In PLN thousand	31 December 2006	31 December 2005
1. Liabilities to the State Budget		342,721	83,210
2. Other liabilities		762,064	22,849
2.1. To related entities		1,063	201
2.2. To other entities		761,001	22,648
VI. Special funds		63,771	53,525
I. Accruals and deferred income		107,851	57,000
1. Accrued expenses		105,280	54,214
2. Negative goodwill		-	-
3. Deferred income		2,571	2,786
Total equity and liabilities		27,685,532	24,015,363

Off-balance items	In PLN thousand	31 December 2006	31 December 2005
1. Contingent receivables,:		-	-
1.1. Guarantees received		-	-
1.2. Other		-	-
2. Contingent liabilities, of which:		2,336,314	401,333
2.1. Guarantees issued		-	-
2.2. Bills of exchange accepted and endorsed		-	-
2.3. Buy and sell back assets		2,304,899	353,843
2.4. Other liabilities		-	-
3. Reinsurance guarantees made to the Company		-	-



Off-balance items	In PLN thousand	31 December 2006	31 December 2005
4. Reinsurance guarantees made by the insurer on behalf of cedants		-	-
5. Third party assets not included in the assets		-	-
Off-balance items, total		2,336,314	401,333
Own funds		4,435,864	3,908,208
Solvency margin		1,492,885	1,467,852
Surplus (shortage) of own funds to cover solvency margin		2,942,979	2,440,356
Technical reserves		21,458,005	19,362,912
Assets to cover technical reserves		26,041,975	22,458,689
Surplus (shortage) of assets to cover technical reserves		4,583,970	3,095,777



## Life insurance revenue account of PZU Życie SA

Life insurance revenue account	In PLN thousand	1 January – 31 December 2006	1 January – 31 December 2005
I. Premiums		7,579,467	6,085,888
1. Gross premiums written		7,589,821	6,096,054
2. Reinsurers' share of premium written		8,402	8,645
3. Movement in unearned premium reserve and unexpired risk reserve, gross		1,952	1,521
4. Reinsurers' share in movement in unearned premium reserve		-	-
II. Investment income		1,833,572	1,694,035
1. Income from property		424	490
2. Income from investments in related entities		79,400	13,439
2.1. from shares		70,335	134
2.2. from loans and debt securities		9,065	13,305
2.3. from other investments		-	-
3. Income from other financial investments		1,200,231	1,270,193
3.1. from shares, other variable income securities, participation units and investment certificates in investment funds		62,773	49,437
3.2. debt securities and other fixed income securities		1,104,444	1,199,728
3.3. term deposits with financial institutions		29,448	21,028
3.4. other deposits		3,566	-
4. Gain on impairment of investments		27,664	13,385
5. Gain on realization of investments		525,853	396,528
III. Unrealized gains on investments		632,724	596,584
IV. Other technical income, net of reinsurers' share		19,550	27,784



Life insurance revenue account	In PLN thousand	1 January – 31 December 2006	1 January – 31 December 2005
V. Claims and benefits		4,299,580	3,911,598
1. Claims and benefits paid out, net of reinsurers' share		4,276,050	3,980,699
1.1. Claims and benefits paid out, gross		4,276,050	3,982,056
1.2. Reinsurers' share of claims and benefits paid out		-	1,357
2. Movement in outstanding claims reserve, net of reinsurers' share		23,530	(69,101)
2.1. Movement in outstanding claims reserve, gross		23,530	(69,101)
2.2. Reinsurers' share in movement in outstanding claims reserve		-	-
VI. Movement in other technical reserves, net of reinsurers' share		2,069,801	1,643,135
1. Movement in life insurance reserves, net of reinsurers' share		673,103	1,046,071
1.1. Movement in life insurance reserves, gross		673,064	1,046,989
1.2. Reinsurers' share in movement in life insurance reserves		(39)	(82)
2. Movement in life insurance reserves, net of reinsurers' share where the investment risk is borne by policyholders		1,384,336	479,968
2.1. Movement in life insurance reserves, gross		1,384,336	479,968
2.2. Reinsurers' share in movement in life insurance reserves		-	-
3. Movement in other reserves defined in the Articles of Association, net of reinsurers' share		12,362	117,096
3.1. Movement in other reserves defined in the Articles of Association, gross		12,362	117,096
3.2. Reinsurers' share in movement in other reserves defined in the Articles of Association		-	-
VII. Bonuses and rebates for the insured net of reinsurers' share		1,704	1,830
VIII. Insurance activities		919,076	894,308



Life insurance revenue account	In PLN thousand	1 January – 31 December 2006	1 January – 31 December 2005
1. Acquisition expenses		370,759	313,641
2. Administrative expenses		550,863	582,122
3. Reinsurance commission and share in reinsurers' profits		2,546	1,455
IX. Cost of investing activities		187,172	128,409
1. Cost of property maintenance		1,347	1,389
2. Other costs of investing activities		34,920	22,044
3. Loss on impairment of investments		1,496	1,215
4. Loss on realization of investments		149,409	103,761
X. Unrealized losses on investments		107,562	65,482
XI. Other technical costs, net of reinsurers' share		74,794	44,091
XII. Net investment income transferred to the consolidated general profit and loss account		140,170	129,957
XIII. Life underwriting result		2,265,454	1,585,481



## General profit and loss account of PZU Życie SA

General profit and loss account	In PLN thousand	1 January – 31 December 2006	1 January – 31 December 2005
I. Property and casualty and life insurance underwriting result		2,265,454	1,585,481
II. Investment income		-	-
1. Income from property		-	-
2. Income from investments in related entities		-	-
2.1. from shares		-	-
2.2. from loans and debt securities		-	-
2.3. from other investments		-	-
3. Income from other financial investments		-	-
3.1. shares, variable income securities, participation units and certificates in investment funds		-	-
3.2. from debt securities and other fixed income securities		-	-
3.3. from term deposits with financial institutions		-	-
3.4. from other investments		-	-
4. Gains on impairment of investments		-	-
5. Gains on realization of investments		-	-
III. Unrealized gains on investments		-	-
IV. Net investment income less costs transferred from life revenue account		140,170	129,957
V. Cost of investing activities		-	-
1. Cost of property maintenance		-	-



General profit and loss account	In PLN thousand	1 January – 31 December 2006	1 January – 31 December 2005
2. Other costs of investing activities		-	-
3. Loss on impairment of investments		-	-
4. Loss on realization of investments		-	-
VI. Unrealized losses on investments		-	-
VII. Net investment income less costs transferred from revenue account of property and casualty insurance and life insurance		-	-
VIII. Other operating income		70,265	55,180
IX. Other operating expenses		108,743	36,768
X. Operating profit/(loss)		2,367,146	1,733,850
XI. Extraordinary gains		-	1
XII. Extraordinary losses		-	2
XIII. Gross profit (loss)		2,367,146	1,733,849
XIV. Income tax		430,817	318,641
XV. Other obligatory decreases of profit / increases of loss		-	-
XVI. Net profit (loss)		1,936,329	1,415,208





## Cash flow statement of PZU Życie SA

Cash flow statement	In PLN thousand	1 January – 31 December 2006	1 January – 31 December 2005
<b>A. Net cash flow from operating activities</b>			
I. Inflows		7,681,186	6,190,514
1. Cash inflows from direct insurance and reinsurance inwards		7,626,801	6,141,560
1.1. Gross premium written		7,607,764	6,113,027
1.2. Salvages and subrogations		-	-
1.3. Other		19,037	28,533
2. Cash inflows from reinsurance outwards		2,546	2,811
2.1. Cash inflows from reinsurers' share in claims paid		-	1,356
2.2. Cash inflows from reinsurance commission and the share in reinsurers' profits		2,546	1,455
2.3. Other		-	-
3. Cash inflows from other operating activities		51,839	46,143
3.1. Proceeds from loss adjusting services rendered		-	-
3.2. Sale of intangible assets and tangible fixed assets other than investments		1,453	1,343
3.3. Other inflows		50,386	44,800
II. Outflows		5,456,958	5,375,556
1. Cash outflows from direct insurance and reinsurance inwards		5,133,402	4,831,528
1.1. Gross premiums returns		-	-
1.2. Claims and benefits paid out, gross		4,136,913	3,852,894
1.3. Acquisition expenses		344,618	320,022
1.4. Administrative expenses		494,061	501,087



Cash flow statement	In PLN thousand	1 January – 31 December 2006	1 January – 31 December 2005
1.5. Costs of loss adjusting services and subrogation collection		139,137	129,202
1.6. Commissions paid out and the share in profits from reinsurance inwards		-	-
1.7. Other outflows		18,673	28,323
2. Cash outflows from reinsurance outwards		8,402	8,645
2.1. Premiums paid in respect of reinsurance outwards		8,402	8,645
2.2. Other outwards reinsurance expenses		-	-
3. Other operating expenses		315,154	535,383
3.1. Expenses relating to loss adjusting services rendered		-	-
3.2. Purchase of intangible assets and tangible fixed assets other than investments		32,430	43,394
3.3. Other		282,724	491,989
III. Net cash flow from operating activities (I – II)		2,224,228	814,958
<b>B. Net cash flow from investing activities</b>			
I. Inflows		273,844,841	137,371,679
1. Sale of property		-	-
2. Sale of shares in related entities		-	48
3. Sale of shares in other entities, participation units and investment certificates in investment funds		3,413,795	1,679,883
4. Sale of debt securities issued by related entities and loans repaid by those entities		51,248	45,416
5. Sale of debt securities issued by other entities		8,836,352	9,218,268
6. Withdrawal of term deposits with financial institutions		118,818,884	78,716,647
7. Sale of other investments		141,559,663	46,605,720
8. Inflows from property		424	490



Cash flow statement	In PLN thousand	1 January – 31 December 2006	1 January – 31 December 2005
9. Interest received		1,053,019	1,065,109
10. Dividends received		107,891	40,098
11. Other inflows		3,565	-
II. Outflows		274,640,792	137,214,737
1. Purchase of property		-	-
2. Purchase of shares in related entities		-	-
3. Purchase of shares in other entities, participation units and investment certificates in investment funds		3,612,487	1,760,846
4. Purchase of debt securities issued by related entities and loans granted to those entities		-	-
5. Purchase of debt securities issued by other entities		8,320,578	9,853,685
6. Creation of term deposits with financial institutions		119,173,120	79,027,850
7. Acquisition of other investments		143,498,340	46,548,923
8. Outflows for property maintenance		1,347	1,389
9. Other investment outflows		34,920	22,044
III. Net cash flow from investing activities (I – II)		(795,951)	156,942
C. Cash flow from financing activities			
I. Inflows		-	-
1. Net inflow from issuance of shares and additional payments to share capital		-	-
2. Loans and credits and issuance of debt securities		-	-
3. Other		-	-
II. Outflows		1,405,208	956,123
1. Dividends paid		1,405,208	956,123
2. Outflows due to appropriation of profit other than payments to shareholders		-	-
3. Re-acquisition of own shares		-	-



Cash flow statement	In PLN thousand	1 January – 31 December 2006	1 January – 31 December 2005
4. Repayment of loans and credits and redemption of debt securities		-	-
5. Interest on loans and credits and debt securities issued		-	-
6. Other outflows from financing activities		-	-
III. Net cash flow on financing activities (I – II)		(1,405,208)	(956,123)
D. Total net cash flow (A.III +/- B.III +/- C.III)		23,069	15,777
E. Balance sheet change in cash and cash equivalents, of which:		23,069	15,777
– change in cash and cash equivalents due to foreign exchange differences		-	-
F. Cash and cash equivalents at the beginning of the period		116,783	101,006
G. Cash and cash equivalents at the end of the period (F+/-D), of which:		139,852	116,783
– of restricted use		52,976	50,523

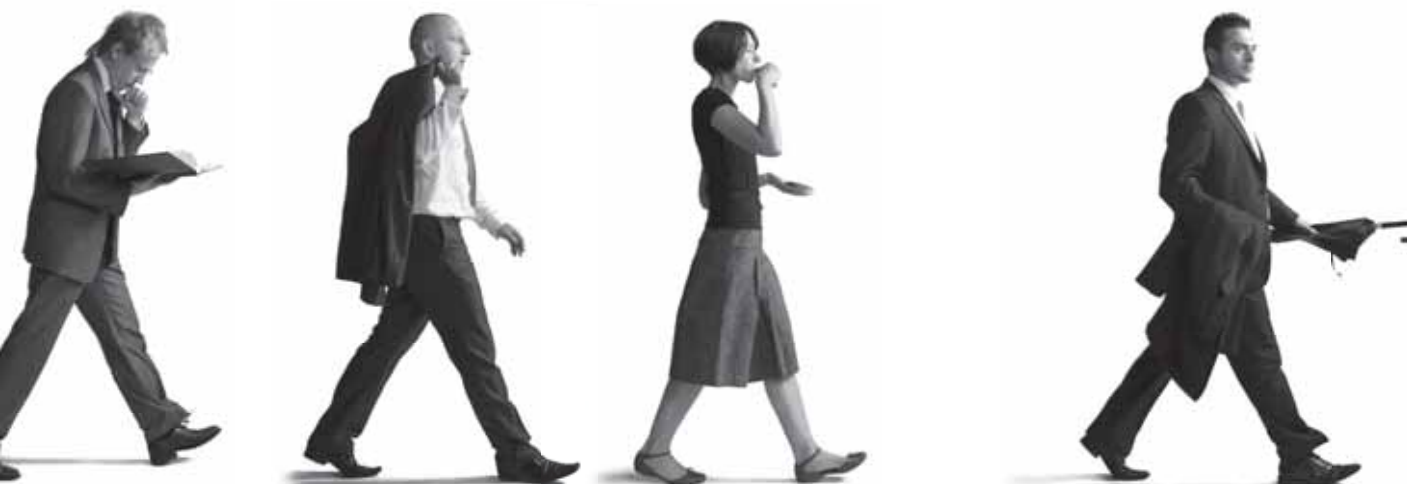


## Statement of changes in equity of PZU Życie SA

Statement of changes in equity	In PLN thousand	1 January – 31 December 2006	1 January – 31 December 2005
I. Shareholders' equity at the beginning of the period		3,992,778	3,543,333
a) changes in accounting policies		-	-
b) adjustments due to errors		-	-
I. a. Shareholders' equity at the beginning of the period, after adjustments		3,992,778	3,543,333
1. Share capital at the beginning of the period		295,000	295,000
1.1. Changes in share capital		-	-
a) increases		-	-
– share issue		-	-
b) decreases:		-	-
– share redemption		-	-
1.2. Share capital at the end of the period		295,000	295,000
2. Unpaid share capital at the beginning of the period		-	-
2.1. Changes in unpaid share capital		-	-
a) increases		-	-
b) decreases		-	-
2.2. Unpaid share capital at the end of the period		-	-
3. Treasury shares at the beginning of the period		-	-
3.1. Changes in treasury shares		-	-
a) increases		-	-
b) decreases		-	-
3.2. Treasury shares at the end of the period		-	-



Statement of changes in equity	In PLN thousand	1 January – 31 December 2006	1 January – 31 December 2005
4. Reserve capital at the beginning of the period		2,279,485	2,279,428
4.1. Changes in reserve capital		4	57
a) increases		4	57
– share issues in excess of par		-	-
– dividend paid out (statutory)		-	-
– dividend paid out (in excess of the statutory minimum value)		-	-
– from revaluation reserve		4	57
b) decreases		-	-
4.2. Reserve capital at the end of the period		2,279,489	2,279,485
5. Opening balance of revaluation reserve		3,085	3,124
a) changes in accounting policies		-	-
b) adjustments of errors		-	-
5a. Revaluation reserve at the beginning of the period		3,085	3,124
5.1. Revaluation reserve		3,366	(39)
a) increases (due to):		4,396	18
– disposal and liquidation of fixed assets		-	-
– revaluation		4,396	18
b) decreases (due to):		1,030	57
– disposal and liquidation of fixed assets		4	57
– valuation of financial investments		1,026	-
5.2. Revaluation reserve at the end of the period		6,451	3,085
6. Other reserves at the beginning of the period		-	-
6.1. Changes of other reserves		-	-
a) increases (due to)		-	-



Statement of changes in equity	In PLN thousand	1 January – 31 December 2006	1 January – 31 December 2005
b) decreases (due to)		-	-
6.2. Other reserves at the end of the period		-	-
7. Accumulated profits/(losses) from previous years at the beginning of the period		1,415,208	965,781
7.1. Accumulated profits/(losses) from previous years at the beginning of the period		1,415,208	965,781
a) changes in accounting policies		-	-
b) adjustments due to errors		-	-
7.2. Accumulated profits/(losses) from previous years at the beginning of the period, after adjustments		1,415,208	965,781
a) increases (due to):		-	-
– profit distribution of previous years		-	-
b) decreases (due to):		1,415,208	965,781
– dividend paid		1,405,208	956,123
– transfer to reserve capital		-	-
– transfer to social fund		10,000	9,658
7.3. Accumulated profits from previous years at the end of the period		-	-
7.4. Accumulated losses from previous years at the end of the period		-	-
a) changes in accounting policies		-	-
b) adjustments due to errors		-	-
7.5. Accumulated losses from previous years after adjustments		-	-
a) increases (due to):		-	-
– loss coverage		-	-
b) decreases (due to):		-	-
– loss coverage		-	-
7.6. Closing balance of loss of previous years		-	-



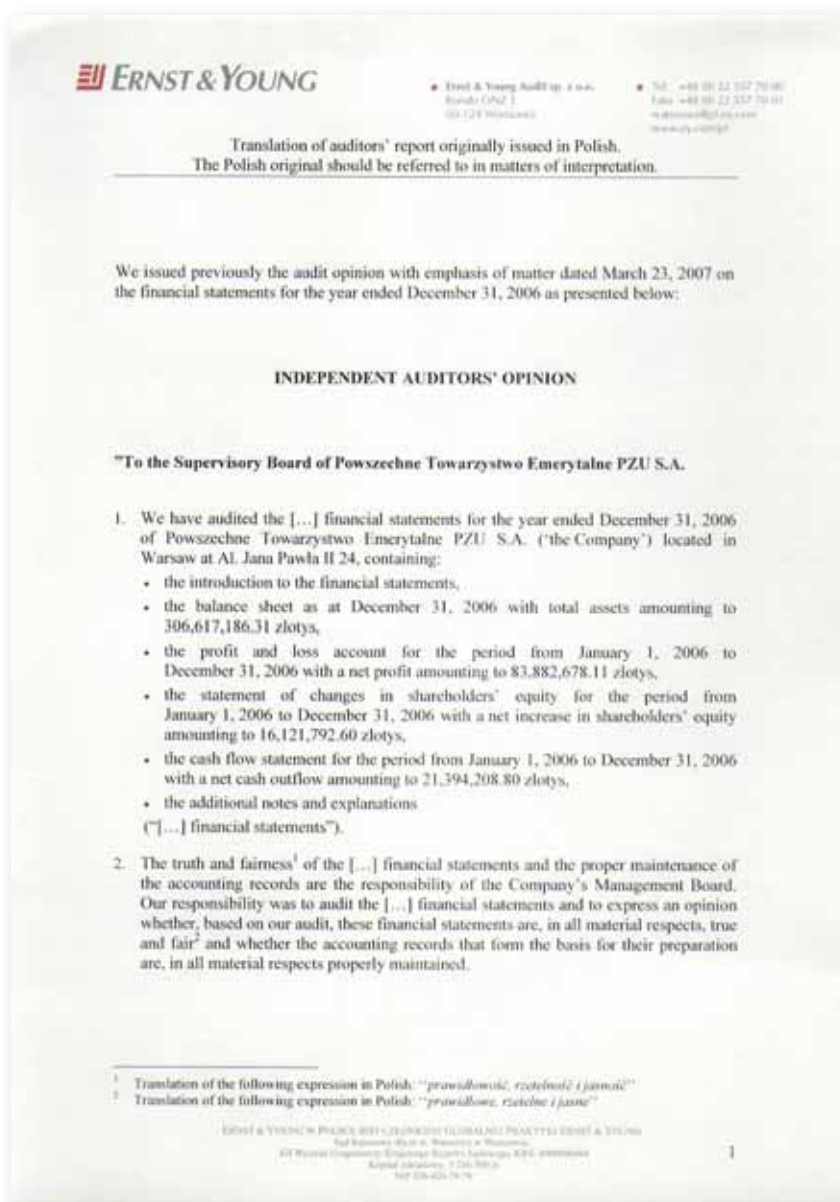


Statement of changes in equity	In PLN thousand	1 January – 31 December 2006	1 January – 31 December 2005
7.7. Closing balance of accumulated profit (loss) from previous years		-	-
8. Net result		1,936,329	1,415,208
a) net profit		1,936,329	1,415,208
b) net loss		-	-
c) deductions from net profit		-	-
II. Shareholders' equity at the end of the period		4,517,269	3,992,778
III. Shareholders' after proposed appropriation of profits / absorption of losses		4,517,269	2,577,570

\* on 28 June 2007, the General Meeting of Shareholders of PZU Życie SA resolved to designate PLN 1,926,329 thousand to reserve capital and PLN 10,000 thousand to the Company Social Fund



## V. Financial statements – PTE PZU SA





Translation of auditors' report originally issued in Polish.  
The Polish original should be referred to in matters of interpretation.

3. We conducted our audit of the [...] financial statements in accordance with the following regulations being in force in Poland:
  - chapter 7 of the Accounting Act, dated September 29, 1994 ("the Accounting Act"),
  - the auditing standards issued by the National Chamber of Auditors,
 in order to obtain reasonable assurance whether these financial statements are free of material misstatement. In particular, the audit included examining, to a large extent on a test basis, documentation supporting the amounts and disclosures in the [...] financial statements. The audit also included assessing the accounting principles adopted and used and significant estimates made by Management Board, as well as evaluating the overall presentation of the [...] financial statements. We believe our audit has provided a reasonable basis to express our opinion on the [...] financial statements treated as a whole.
4. The financial statements for the prior financial year ended December 31, 2005 were subject to our audit and we issued an opinion dated February 20, 2006 including an emphasis of matter on these financial statements. We draw your attention to this emphasis of matter also in this opinion, in point 6 below.
5. In our opinion, the [...] financial statements, in all material respects:
  - present truly and fairly all information material for the assessment of the results of the Company's operations for the period from January 1, 2006 to December 31, 2006, as well as its financial position<sup>3</sup> as at December 31, 2006;
  - have been prepared in accordance with the accounting principles specified in the Accounting Act and regulations issued based on that Act and based on properly maintained accounting records;
  - are in accordance with the Accounting Act and regulations issued based on that Act and the provisions of the Company's statute that affect their content.
6. Without qualifying our opinion, we draw attention to the following issue described in point 19 of the additional notes and explanations to the [...] financial statements. Based on the statute of Otwarty Fundusz Emerytalny PZU "Złota Jesień" ("the Fund"), the Company is entitled to receive the manipulation fee as a certain percentage of the members' contribution paid to the Fund or treasury bonds and the management fee as a percentage of the Fund's net assets. In accordance with the respective regulations, setting out the accounting principles to be followed by pension funds, the Fund discloses Fund's members' capital as the amount of members' contributions actually received either in a form of cash or treasury bonds. Data from the Fund's transfer agent and generally available information relating to the whole market of pension funds indicate the fact that for a certain number of the Fund's members the contributions have not been transferred at all or are transferred by Social Security Agency (Zakład Ubezpieczeń Społecznych, "ZUS") irregularly. In line with July 23, 2003 Act on taking over the ZUS liabilities resulting from not transferred contributions to pension funds by the State Treasury (Journal of Laws No 149, item 1450 with further amendments), the State Treasury started in 2003 and continued in years 2004 - 2006 to

<sup>3</sup> Translation of the following expression in Polish: "zyskacja majątkowa i finansowa"





Translation of auditors' report originally issued in Polish.  
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transfer overdue contributions to pension funds in a form of treasury bonds. However, according to the Company's Management Board estimations, the contributions received by the Fund by the end of 2006 constitute only a part of overall estimated State Treasury liability to the Fund. The Fund's financial statements for the year ended December 31, 2006 include only contributions received in a form of cash or treasury bonds until December 31, 2006. The financial statements of the Company for the year ended December 31, 2006 include only the manipulation fee income due from the contributions received by the Fund until December 31, 2006 in form of cash or treasury bonds and the management fee income calculated as a percentage of the net assets presented in the Fund's financial statements.

7. We have read the Directors' Report for the period from January 1, 2006 to December 31, 2006 ("the Directors' Report") and concluded that the information derived from the [...] financial statements reconciles with these financial statements. The information included in the Directors' Report corresponds with art. 49 of the Accounting Act."

In our opinion the information presented in the published, condensed financial statements on pages 212 to 226 of this annual report is in all material respects fairly stated in relation to the consolidated financial statements from which it has been derived. The financial statements that were audited by us include notes that were not fully presented in the attached condensed financial statements. In order for the reader to obtain a true and fair view of the state of affairs of the Company as at December 31, 2006 and the results of its operations for the period from January 1, 2006 to December 31, 2006, the reader must review the full financial statements in their entirety including supporting schedules and statutory disclosures as required by the Accounting Act and the regulations based thereof.

On behalf of  
Ernst & Young Audit Sp. z o. o.  
Rondo ONZ 1, 00-124 Warszawa  
Reg. No. 130

Marcin Dymek  
Certified Auditor No. 9899/7370

Dorota Sznarska-Kuman  
Certified Auditor No. 9667/7232

Warsaw, October 31, 2007

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## Balance sheet of PTE PZU SA

Assets	In PLN thousand	31 December 2006	31 December 2005
<b>A. Intangible assets</b>		<b>83,131</b>	<b>175,780</b>
I. Wartości niematerialne i prawne		81	63
1. Koszty zakończonych prac rozwojowych		-	-
2. Wartość firmy		-	-
3. Other intangibles		81	63
4. Advance payments towards intangible assets		-	-
<b>II. Tangible assets</b>		<b>1,327</b>	<b>1,358</b>
1. Fixed assets		1,327	1,358
a) land (including perpetual usufruct of land)		-	-
b) buildings, premises, civil engineering structures		-	-
c) technical plant and machinery		183	263
d) means of transport		1,043	958
e) other fixed assets		101	137
2. Fixed assets under construction		-	-
3. Advance prepayments for fixed assets under construction		-	-
<b>III. Long-term receivables</b>		<b>185</b>	<b>185</b>
1. from affiliated entities		185	185
2. from other entities		-	-
<b>IV. Long-term investments</b>		<b>80,408</b>	<b>172,736</b>
1. Real estate		-	-
2. Intangible assets		-	-
3. Long-term financial assets		80,408	172,736



Assets	In PLN thousand	31 December 2006	31 December 2005
a) in affiliated entities		-	-
- ownership interests or shares		-	-
- other securities		-	-
- granted loans		-	-
- other long-term financial assets		-	-
b) in other entities		80,408	172,736
- ownership interests or shares		-	-
- other securities		80,408	172,736
- granted loans		-	-
- other long-term financial assets		-	-
4. Other long-term investments		-	-
V. Long-term prepayments and accruals		1,130	1,438
1. Deferred income tax assets		1,130	1,438
2. Other accruals		-	-
<b>B. Current assets</b>		<b>223,486</b>	<b>114,705</b>
I. Inventory		-	-
1. Materials		-	-
2. Semi-finished products and products in progress		-	-
3. Finished products		-	-
4. Merchandise		-	-
5. Advance payments towards trade payables		-	-
II. Short-term receivables		7,407	7,421





Assets	In PLN thousand	31 December 2006	31 December 2005
1. Receivables from affiliated entities	-	-	2,616
a) for goods and services with a term of payment:	-	-	2,616
- up to 12 months	-	-	2,616
- over 12 months	-	-	-
b) others	-	-	-
2. Receivables from other entities	7,407	4,805	
a) for goods and services with a term of payment	7,334	4,578	
- up to 12 months	7,334	4,578	
- over 12 months	-	-	
b) on taxes, subsidies, customs duties, social security and health insurance or other services	-	215	
c) others	73	12	
d) under litigation	-	-	
III. Short-term investments	215,093	106,476	
1. Short-term financial assets	213,795	105,356	
a) in affiliates	-	-	
- ownership interests or shares	-	-	
- other securities	-	-	
- granted loans	-	-	
- other short-term financial assets	-	-	
b) in other entities	182,831	52,997	
- ownership interests or shares	-	-	
- other securities	182,831	52,997	
- granted loans	-	-	
- other short-term financial assets	-	-	





Assets	In PLN thousand	31 December 2006	31 December 2005
c) cash and other cash assets		30,964	52,359
- cash on hand and on accounts		30,964	52,359
- other cash		-	-
- other cash assets		-	-
2. Other short-term investments		1,298	1,120
IV. Short-term prepayments and accruals		986	808
Assets, total		306,617	290,485

Equity and liabilities	In PLN thousand	31 December 2006	31 December 2005
A. Equity		287,627	271,505
I. Share capital		32,000	32,000
II. Unpaid share capital (negative value)		-	-
III. Treasury shares (negative value)		-	-
IV. Reserve capital		171,191	288,000
V. Revaluation reserve		553	1,632
VI. Other reserve capital		-	-
VII. Profit (loss) from previous years		-	(116,809)
VIII. Net profit (loss)		83,883	66,682
IX. Charges to net profit (loss) for the financial year (negative value)		-	-
B. Liabilities and reserves for liabilities		18,990	18,980
I. Reserves for liabilities		3,135	3,678
1. Deferred income tax reserve		2,739	3,322
2. Reserves for pension and similar benefits		396	356
- long-term		391	352



Equity and liabilities	In PLN thousand	31 December 2006	31 December 2005
- short-term		5	4
3. Other reserves		-	-
- long-term		-	-
- short-term		-	-
II. Long-term liabilities		-	-
1. To affiliated entities		-	-
2. To other entities		-	-
a) credits and loans		-	-
b) by issuing debt securities		-	-
c) other financial liabilities		-	-
d) others		-	-
III. Short-term liabilities		5,767	7,175
1. To affiliated entities		174	3,521
a) for goods and services with maturity of:		174	3,521
- up to 12 months		174	3,521
- over 12 months		-	-
b) others		-	-
2. To other entities		5,481	3,614
a) credits and loans		-	-
b) by issuing debt securities		-	-
c) other financial liabilities		-	-
d) for goods and services with a maturity of:		1,687	1,545
- up to 12 months		1,687	1,545
- over 12 months		-	-



Equity and liabilities	In PLN thousand	31 December 2006	31 December 2005
e) advances received towards deliveries		-	-
f) bill of exchange liabilities		-	-
g) on taxes, customs, insurance and other benefits		2,330	908
h) on compensation		-	-
i) others		1,464	1,161
3. Special purpose funds		112	40
IV. Accruals and deferred income		10,088	8,127
1. Negative goodwill		-	-
2. Other accruals and deferred income:		10,088	8,127
- long-term		-	-
- short-term		10,088	8,127
Total equity and liabilities		306,617	290,485



## Profit and loss account of PTE PZU SA

Profit and loss account (comparable version)	In PLN thousand	1 January – 31 December 2006	1 January – 31 December 2005
A. Net sales revenues and equivalents, including:		226,926	187,978
- from affiliated entities		-	-
I. Net revenues on the sales of products		226,926	187,978
II. Change in the balance of products (increase positive value, decrease negative value)		-	-
III. Cost of manufacturing products for the entity's proprietary needs		-	-
IV. Net revenues on the sale of merchandise and materials		-	-
B. Operating expense		137,689	117,690
I. Depreciation and amortization		626	859
II. Consumption of materials and energy		1,041	1,124
III. Third party services		83,073	75,972
IV. Taxes and fees, including:		288	249
- excise tax		-	-
V. Payroll		14,695	12,182
VI. Payroll-related expenses		2,465	1,918
VII. Other types of cost		35,501	25,386
VIII. Cost of merchandise and materials sold		-	-
C. Profit (loss) on sales (A – B)		89,237	70,288
D. Other operating income		615	586
I. Profit on the sale of non-financial non-current assets		66	17
II. Subsidies		-	-
III. Other operating income		549	568



Profit and loss account (comparable version)	In PLN thousand	1 January – 31 December 2006	1 January – 31 December 2005
E. Other operating expense		276	1,593
I. Loss on the sale of non-financial non-current assets		-	-
II. Revaluation of non-financial assets		-	-
III. Other operating expenses		276	1,593
F. Operating profit (loss) (C + D – E)		89,576	69,281
G. Financial income		14,342	13,955
I. Dividends and profit-sharing, including:		-	-
– from affiliated entities		-	-
II. Interest, including:		2,933	2,294
– from affiliated entities		-	-
III. Profit on the sale of investments		3,492	3,785
IV. Revaluation of investments		7,913	7,876
V. Others		4	-
H. Financial expenses		142	127
I. Interest, including:		-	-
– from affiliated entities		-	-
II. Loss on the sale of investments		-	-
III. Revaluation of investments		-	-
IV. Others		142	127
I. Profit (loss) on economic activity (F + G – H)		103,776	83,109
J. Result on extraordinary events (J.I. – J.II.)		-	-
I. Extraordinary gains		-	-
II. Extraordinary losses		-	-



Profit and loss account (comparable version)	In PLN thousand	1 January – 31 December 2006	1 January – 31 December 2005
K. Gross profit (loss) (I ± J)		103,776	83,109
L. Income tax		19,893	16,427
M. Other tax charges (increasing of loss)		-	-
N. Net profit (loss) (K – L – M)		83,883	66,682



## Cash flow statement of PTE PZU SA

Cash flow statement (indirect method)	In PLN thousand	1 January – 31 December 2006	1 January – 31 December 2005
<b>A. Cash flow on operating activity</b>			
I. Net profit (loss)		83,883	66,682
II. Total adjustments		(13,826)	696
1. Depreciation and amortization		626	859
2. FX gains (losses)		-	-
3. Interest and profit distributions (dividends)		(14,416)	(14,208)
4. Profit (loss) on investing activities		(12)	50
5. Change in the balance of reserves		(544)	2,268
6. Change in the balance of inventories		-	-
7. Change in the balance of receivables		15	(1,441)
8. Change in the balance of current liabilities, except for credits and loans		(1,408)	4,771
9. Change in the balance of prepayments, deferred income and accruals		2,091	8,741
10. Other adjustments		(178)	(344)
III. Net cash flow on operating activity (I ± II)		70,057	67,378
<b>B. Cash flow on investing activity</b>			
I. Inflows		91,419	104,500
1. Sale of intangibles and tangible assets		148	116
2. Sale of investments in real estate and intangible assets		-	-
3. From financial assets, including:		91,271	104,384
a) in affiliated entities		-	17





Cash flow statement (indirect method)	In PLN thousand	1 January – 31 December 2006	1 January – 31 December 2005
b) in other entities		91,271	104,367
- sale of financial assets		86,403	102,070
- dividends and profit-sharing		-	-
- repayment of granted long-term loans		-	-
- interest		4,868	2,297
- other inflows from financial assets		-	-
4. Other investment inflows		-	-
II. Outflows		116,189	179,515
1. Purchase of intangibles and tangible fixed assets		749	456
2. Investments in real estate and intangible assets		-	-
3. For financial assets, including:		115,440	179,059
a) in affiliated entities		-	-
b) in other entities		115,440	179,059
- purchase of financial assets		115,440	179,059
- granted long-term loans		-	-
4. Other investment outflows		-	-
III. Net cash flow on investing activities (I – II)		(24,770)	(75,015)
C. Net cash flow on financing activity		-	-
I. Inflows		-	-
1. Net inflows on issuing ownership interests (issuing shares) and other capital instruments and prepayments to share capital		-	-
2. credits and loans		-	-
3. Issuance of debt securities		-	-
4. Other financial inflows		-	-



Cash flow statement (indirect method)	In PLN thousand	1 January – 31 December 2006	1 January – 31 December 2005
II. outflows		66,682	-
1. Re-acquisition of own shares		-	-
2. Dividends and disbursements to owners		66,682	-
3. outflows due to appropriation of profits other than disbursements to owners		-	-
4. Repayment of credits and loans		-	-
5. Redemption of debt securities		-	-
6. On other financial liabilities		-	-
7. Liability payments for financial lease agreements		-	-
8. Interest		-	-
9. Other financial expenditures		-	-
III. Net cash flow on financing activity (I - II)		(66,682)	-
D. Total net cash flow (A.III ± B.III ± C.III)		(21,395)	(7,637)
E. Balance sheet change in cash balance, including:		(21,395)	(7,637)
– change in the cash balance on account of FX gains		-	-
F. Cash and cash equivalents at the beginning of the period		52,359	59,996
G. Cash and cash equivalents at the end of the period (F +/- D), of which:		30,964	52,359
– of restricted use (Social Fund)		112	40



## Statement of changes in equity of PTE PZU SA

Statement of changes in equity	In PLN thousand	1 January – 31 December 2006	1 January – 31 December 2005
I. Equity at the beginning of the period (OB)		271,505	203,834
- adjustments due to errors		-	-
- changes in accounting policies		-	-
I. a. Equity at the beginning of the period, adjusted		271,505	203,834
1. Share capital at the beginning of the period		32,000	32,000
1.1. Changes to share capital		-	-
a) increases (due to)		-	-
- share issue		-	-
b) decreases (due to):		-	-
- share redemption		-	-
1.2. Share capital at the end of the period		32,000	32,000
2. Unpaid share capital at the beginning of the period		-	-
2.1. Changes to unpaid share capital		-	-
a) increases		-	-
b) decreases		-	-
2.2. Unpaid share capital at the end of the period		-	-
3. Own shares at the beginning of the period		-	-
a) increases		-	-
b) decreases		-	-
3.1. Own shares at the end of the period		-	-
4. Reserve capital at the beginning of the period		288,000	288,000
4.1. Changes to reserve capital		(116,809)	-



Statement of changes in equity	In PLN thousand	1 January – 31 December 2006	1 January – 31 December 2005
a) increases (due to):		-	-
- share issues in excess of par		-	-
- dividend paid out (statutory)		-	-
- dividend paid out (in excess of the statutory minimum value)		-	-
b) decreases (due to):		116,809	-
- loss covering		116,809	-
4.2. Reserve capital at the end of the period		171,191	288,000
5. Revaluation reserve at the beginning of the period		1,633	643
5.1. Changes to revaluation reserve		(1,079)	989
a) increases (due to):		-	989
- revaluation of investments		-	989
b) decreases (due to):		1,079	-
- revaluation of investments		1,079	-
5.2. Revaluation reserve at the end of the period		554	1,632
6. Other reserve capital at the beginning of the period		-	-
6.1. Changes to other reserves		-	-
a) increases		-	-
b) decreases		-	-
6.2. Other reserve capital at the end of the period		-	-
7. Profits (loss) from previous years at the beginning of the period		(50,127)	(116,809)
7.1. Opening balance of accumulated profit from previous years		66,682	45,610
- adjustments due to errors		-	-



Statement of changes in equity	In PLN thousand	1 January – 31 December 2006	1 January – 31 December 2005
7.2. Profits from previous years at the beginning of the period, adjusted		66,682	45,610
a) increases (due to):		-	-
- appropriation profits from previous years		-	-
b) decreases (due to):		66,682	45,610
- coverage of losses from previous years		-	45,610
- dividend paid		66,682	-
7.3. Profits from previous years at the end of the period		-	-
7.4. Losses from previous years at the beginning of the period		(116,809)	(162,419)
- adjustments due to errors		-	-
- adjustments for changes in accounting policies		-	-
7.5. Losses from previous years at the beginning of the period, adjusted		(116,809)	(162,419)
a) increases (due to):		-	-
- transfer of losses from previous years to be covered		-	-
b) decreases (due to):		116,809	45,610
- coverage with profits from previous years		-	45,610
- covering loss with reserve capital		116,809	-
7.6. Losses from previous years at the end of the period		-	(116,809)
7.7. Profit (losses ) from previous years at the end of the period		-	(116,809)
8. Net result		83,883	66,682
a) net profit		83,883	66,682
b) net loss		-	-
c) charges to profits		-	-
II. Equity at the end of the period (CB)		287,628	271,505
III. Equity after considering the proposed distribution of profits (coverage of losses)		203,745	271,505



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