Annual Report 2011

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PZU

GRUPA PZU

1. DESCRIPTION OF THE PZU GROUP

The Powszechny Zakład Ubezpieczeń Spółka Akcyjna Capital Group (hereinafter: PZU Group) is one of the largest financial institutions in Poland as well as in Central and Eastern Europe. The parent company of the PZU Group is Powszechny Zakład Ubezpieczeń Spółka Akcyjna (hereinafter PZU SA, PZU), the sole shareholder of Powszechny Zakład Ubezpieczeń na Życie Spółka Akcyjna (hereinafter PZU Życie SA, PZU Życie).

The PZU Group's detailed structure and the scope of operation of its entities have been presented in chapter 8 entitled „PZU Group's organizational structure". PZU's history dates back to 1803 when the first insurance company was established on Polish soil. As the successor of more than 200 years of tradition, PZU has for a host of years provided comprehensive insurance protection in all the most important areas of private, public and business life.

Today the PZU Group is among the most rapidly growing capital groups in Poland. In 2009 it generated a record-breaking net financial result in the history of the Polish insurance industry (PLN 3.8 billion), which put the PZU Group among the most profitable financial institutions in the nation and among the insurance undertakings generating the highest return on the European market.

On 12 May 2010 PZU debuted on Warsaw Stock Exchange S.A. The value of the offering was nearly PLN 8.1 billion. PZU's offering was the largest one in the Central and Eastern European region from the advent of economic transformation and the largest one across Europe from yearend 2007.

PZU's IPO ended the conflict between PZU's two largest shareholders, which had lingered for more than 10 years: the State Treasury and Eureko B.V. The interim dividend paid in 2009 in the amount of PLN 12 749 917 095 was the largest dividend in the history of the Polish capital market.

PZU's opening share price on the first day of trading climbed by 11.7% (above the offering price) to PLN 349.00, while the price at the close of that first day of trading was PLN 360.00 per share.

PZU's shares are listed on the Warsaw Stock Exchange's main floor in the continuous trading system under the abbreviated name of „PZU" and are designated as „PZU".

The PZU Group offers its customers the broadest range of products on Poland's insurance market. The PZU Group's customers may select from nearly 200 types of insurance offered within its core insurance activity including property and casualty (non-life) and life insurance. In addition to its insurance activity the PZU Group also manages an open-end pension fund, investment funds and savings programs.

The PZU Group is incessantly endeavoring to satisfy more fully its customers' needs, enhance the quality of service and expand opportunities for development. PZU's logo is one of the most recognized brand names in Poland. PZU is the most esteemed for its experience, tradition, Polish roots, strong financial position and convenient accessibility of its agents and branches.

2. MILESTONES IN THE PZU GROUP'S DEVELOPMENT

2010
IPO of PZU SA, delivery of IPO promises – restructuring and savings measures

2012
PZU Group's strategy for 2012 - 2014

New PZU's logo

2001
Conflict relating to the performance of the Share Purchase Agreement between Eureko, BIG Bank Gdański SA, BIG BG Inwestycje SA and the State Treasury

2009
Settlement and Divestment Agreement executed by and between the State Treasury, Eureko, PZU and Kappa

1998
Establishment of PTE PZU as a joint stock company

1999
Adoption of PZU's privatization strategy, Eureko and BIG Bank Gdański SA acquired shares representing a 20% and 10% stake in PZU, respectively

1952
Transformation by the power of law of Powszechny Zakład Ubezpieczeń Wzajemnych (Univeral Mutual Insurance Company) into Państwowy Zakład Ubezpieczeń (State-owned Insurance Company)

1991
Transformation of Państwowy Zakład Ubezpieczeń (State-owned Insurance Company) into a joint stock company wholly-owned by the State Treasury, establishment of PZU Życie as a joint stock company

1803
Towarzystwo Ogniowe dla Miast (Urban Fire Insurance Company) in Eastern Prussia formed

1927
Transformation of Polska Dyrekcja Ubezpieczeń Wzajemnych (Polish Mutual Insurance Directorate) into Powszechny Zakład Ubezpieczeń Wzajemnych (Universal Mutual Company)

3. SUMMARY OF 2011 CONSOLIDATED FINANCIAL RESULTS

In 2011 the PZU Group's financial results according to International Financial Reporting Standards („IFRS"), and compared with the previous year, were mainly shaped by:

- an increase in written premium in the PZU Group in both segments of insurance activities – life and non-life (a total of approximately + 5.1%);
- improved profitability in the non-life segment, mainly in motor insurance and property insurance products which led to significantly lower rate of natural disasters in the analyzed period, which in 2010 related mainly to snow and flood claims (PZU's net share in claims paid amounted to PLN 369.4 million);
- a decrease in the level of administrative expenses achieved thanks to the restructuring program implemented in 2010 and 2011 and the program for reducing fixed costs (-8.1%);
- a drop in income on investing activities resulting from the poor condition on the capital markets (-42.6%);
- consolidating the Armatura Capital Group – a one-off positive impact on net profit of PLN 118.9 million.

In 2011, the net profit of the PZU Group amounted to PLN 2,343.9 million and was 3.9% lower in comparison to the previous year.

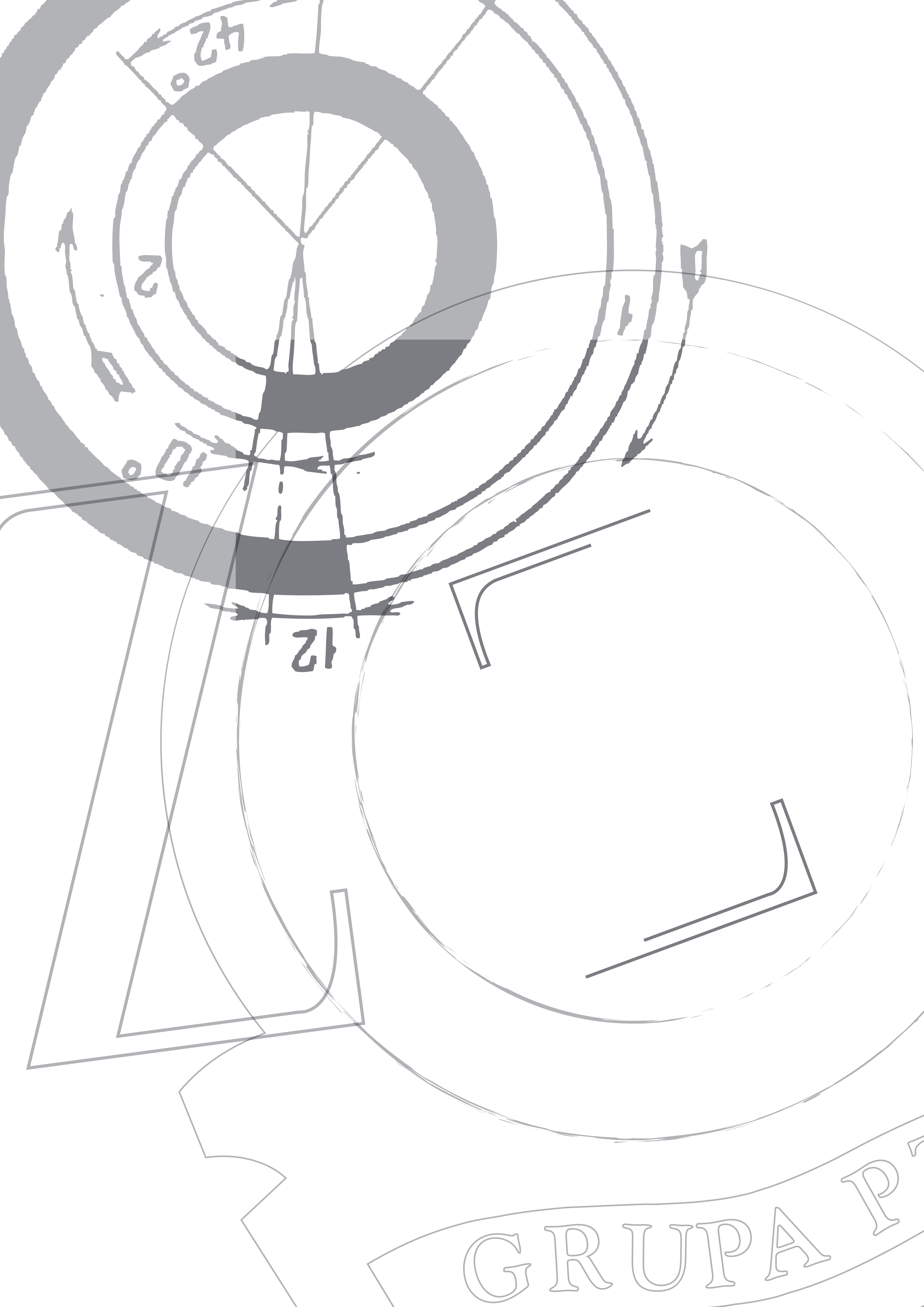
As at the end of 2011, ROE[1)] was 18.3% and had dropped by 2.0 p.p. compared with the end of the previous year.

[1)] ROE – the ratio is calculated as the ratio of the net profit/loss to the average value of equity as at the end and at the beginning of the reporting period.

4. PZU GROUP'S FINANCIAL HIGHLIGHTS

		Audited, prepared in accordance with IFRS (thousand PLN)				
		2007	**2008**	**2009**	**2010**	**2011**
1	Gross written premiums	14,077,123	14,563,147	14,362,717	14,541,022	15,279,262
1a	Property and casualty insurance	8,195,769	8,435,137	8,023,727	8,029,327	8,529,156
1b	Life insurance	5,883,867	6,130,153	6,340,822	6,512,541	6,751,770
1c	Unallocated operating profit	(2,513)	(2,143)	(1,832)	(846)	(1,664)
2	Revenue from commissions and fees*	316,849	338,022	340,876	288,037	281,351
3	Net result from investment activities	2,645,594	579,898	3,469,001	2,777,774	1,593,826
3a	Net investment income	1,807,102	2,411,755	2,363,384	1,824,518	1,970,254
3b	Net profit or loss on realization and impairment loss on	727,445	(855,895)	261,310	199,451	(187,247)
3c	Net change in the fair value of assets and liabilities plus equity	111,047	(975,962	844,307	753,805	(189,181)
4	Net claims and benefits paid out	(8,408,619)	(8,592,057)	(9,436,281)	(10,384,062)	(10,221,122)
5	Acquisition expense	(1,489,643)	(1,668,023)	(1,839,605)	(1,911,255)	(1,961,986)
6	Administrative expense	(1,696,325)	(1,774,846)	(1,808,881)	(1,505,784)	(1,383,897)
7	Operating profit (loss)	4,422,480	2,931,058	4,601,751	3,088,085	2,956,727
7a	Property and personal insurance	1,490,575	3,110,541	2,719,193	3,613,184	2,726,518
7b	Life insurance	2,865,873	1,983,587	3,282,367	2,591,639	1,880,259
7c	Pension funds	125,905	133,083	143,972	122,446	90,447
7d	Unallocated operating profit	(59,873)	(2,296,153)	(1,543,781)	(3,239,184)	(1,740,497)
8	Net profit (loss)	3,560,349	2,329,718	3,762,911	2,439,229	2,343,947
9	Total equity	17,836,090	20,052,390	11,266,879	12,799,926	12,869,505
10	Financial assets	49,366,335	54,220,993	48,237,593	45,345,032	46,775,359
11	Total assets	54,682,353	59,359,041	53,287,438	50,670,557	52,129,282
12	Technical provisions	30,866,621	30,767,412	30,825,046	31,822,990	32,522,729
	ROE**	**24%**	**12%**	**24%**	**20%**	**18%**

* Revenue from commissions and fees - pension segment.
** The ratio is calculated as the ratio of the net profit/loss to the average value of equity as at the end and at the beginning of the reporting period.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5. LETTER FROM THE CHAIRWOMAN OF THE PZU SUPERVISORY BOARD

Chairwoman of the PZU
Supervisory Board

Marzena Piszczek

Dear Stakeholders,

The year 2011 was a period of ongoing change for the PZU Group. The subsequent stages of restructuring were implemented in multiple areas; numerous projects intended to modernize PZU were also pursued. Though facing equivocal macroeconomic conditions during its extensive transformation program PZU generated robust performance and a high return on equity while simultaneously sustaining the Company's investment-grade rating and position as the clear leader on the Polish insurance market.

Last year both favorable and unfavorable macroeconomic conditions affecting insurance activity were in play. Relatively high GDP growth was accompanied by slow real income growth. The PLN's weakening against the Euro adversely affected the loss ratio in motor insurance. Despite the robust financial position of corporates and relatively high GDP growth, the main indices of the Polish equity markets, namely WIG and WIG20 slumped by 20.8% and 21.9%, respectively. The deepening debt crisis in the Eurozone, the fiscal problems in the US, the downgrading of its top-grade financial credibility rating and the revision of its GDP data contributed to a sharp intensification of risk aversion on the global financial markets.

The PZU Group's 2011 financial results were primarily driven by gross written premium growth, enhanced profitability in non-life insurance, lower administrative expenses and lower investment results (caused by the behavior of the capital markets). The gross written premium growth is a positive signal stemming above all from higher sales of life and non-life insurance. The total claims paid by the PZU Group in 2011 were 1.6% lower compared to the previous year. The lower investment results were largely compensated for by higher net earned premium and lower claims paid. It should be noted that ROE remained high at 18.3%.

PZU upheld its investment-grade „A" rating from Standard&Poor's confirming the financial strength of PZU SA and PZU Życie SA with a stable outlook for both companies. PZU's certainty and stability as a financial institution are one of its undeniable strengths. It continues to be the clear insurance market leader in Poland. Its market share measured by gross written premium in non-life insurance was 32.6% while in life insurance its market share climbed to 30.8%.

I would like to thank the Management Boards and the employees of the PZU Group for their perseverance in implementing the strategy. I believe that the ambitious plans intended for 2012 will be attained to the benefit of PZU's customers, employees and shareholders.

Respectfully yours.

6. LETTER FROM PZU'S CEO

Andrzej Klesyk

PZU's CEO

Dear Stakeholders,

On behalf of Management Boards of the PZU Group Companies, I hereby convey the 2011 Annual Report.

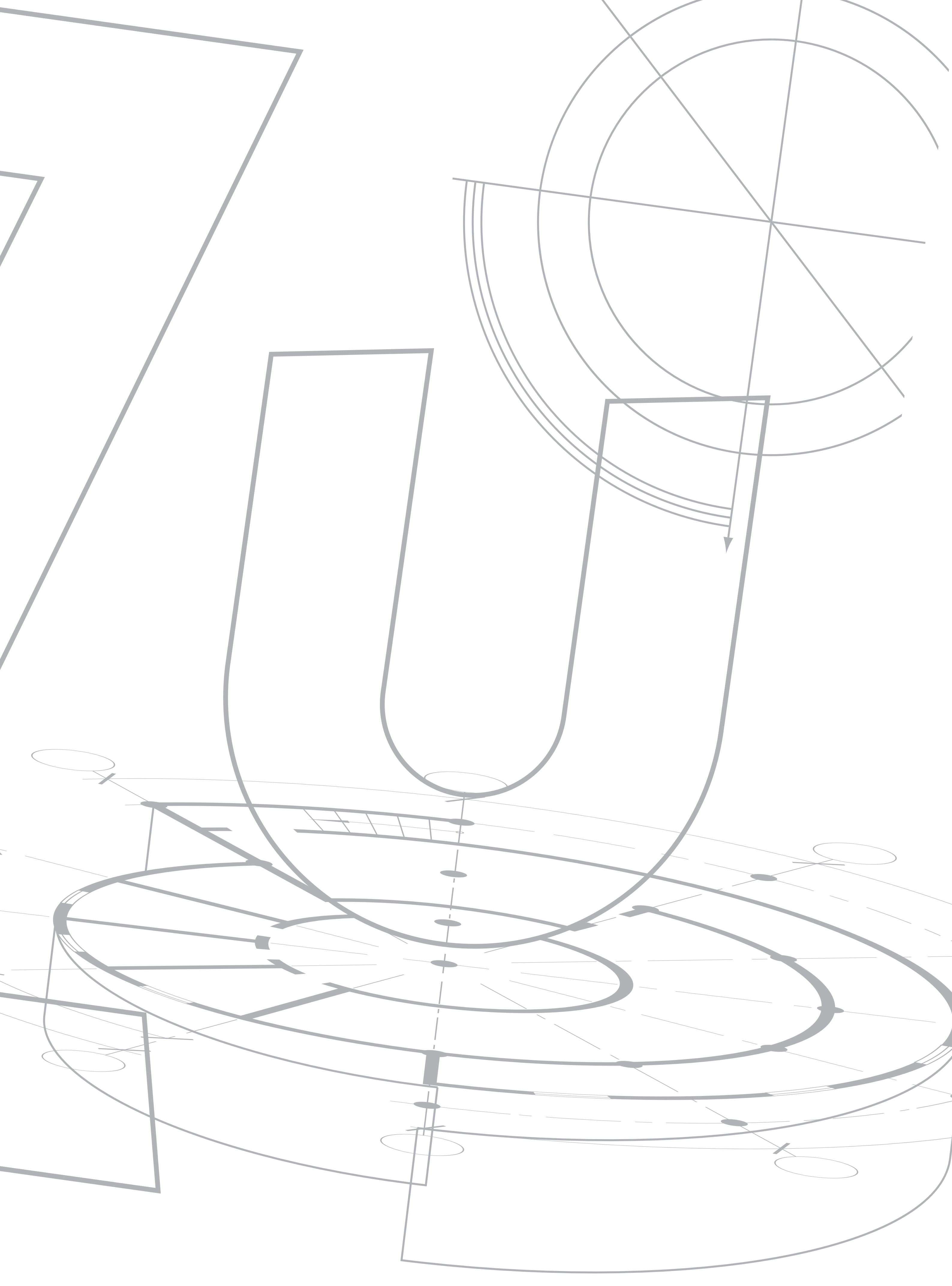
During the course of its implementation, the company's strategy aimed at making the PZU Group the most customer-oriented financial institution in this part of Europe. Last year witnessed continuation of changes in many areas of the company's operations. We executed projects to expedite work in operations, simplifying and streamlining administration, enhancing the standards of customer service and minimizing bureaucracy and the flow of hardcopy documents. Restructuring in the PZU Group also covered headcount, entailing layoffs. As part of the new approach to human resource management we launched a modern and efficient HR service center in the PZU Group. The new strategy for 2012-2014 adopted in December 2011 will continue the changes started in the PZU Group a few years ago.

In business terms, last year the non-life gross written premium structure continued to change following restructuring of the corporate client portfolio and the ongoing pursuit of the retail pricing policy. These measures prompted higher profitability in non-life business, mainly in motor and property insurance.

In 2011, the PZU Group collected PLN 15,279.3 million in insurance premiums. At the same time, the fixed costs reduction and restructuring program was continued. 2011 saw a stable increase in gross written premium in group protection insurance, lower claims and administrative expenses. PZU Group's results were largely impacted by investment income which was 42.6% lower in comparison to the year before, caused by poor overall conditions in the capital markets, including the Warsaw Stock Exchange (the WIG index slumped 20.8% while WIG20 fell by 21.9%). Operating profit was PLN 2,956.7 million.

In the difficult macroeconomic environment of 2011 and in the context of our broad restructuring efforts, PZU Group's result should be assessed as very good. This result is the product of the intense work expended by all our employees, managers and the management board. At this point I would like to thank all the contributors for their efforts to build PZU's value. I would like to thank the Supervisory Board for its cooperation and support at this important time for our Group.

Respectfully yours.



7. CALENDAR OF EVENTS

- **15 March 2011** – appointment of Andrzej Klesyk to the PZU Management Board for its new term of office and entrusting him with the function of Chief Executive Officer;
- **21 April 2011** – appointment of Przemysław Dąbrowski, Marcin Halbersztadt, Witold Jaworski, Bogusław Skuza, Tomasz Tarkowski and Ryszard Trepczyński to the PZU Management Board for its new term of office;
- **11 May 2011** – resolution adopted by the PZU Management Board concerning the Company's dividend policy and the recommendation to pay a dividend on the 2010 profits;
- **11 May 2011** – decision made by the PZU and PZU Życie Management Boards to continue the process of headcount restructuring in these two companies;
- **11 May 2011** – „trusted PZU" – PZU's brand ranked the highest in European Trusted Brands 2011 in the insurance company category;
- **30 May 2011** – execution of an agreement with the trade unions operating in PZU and PZU Życie prescribing the terms and conditions of headcount restructuring in 2011;
- **10 June 2011** – State Treasury's divestment of PZU shares in block trades representing a 10% stake in PZU and 10% of the votes at the Shareholder Meeting;
- **30 June 2011** – Ordinary Shareholder Meeting of PZU;
- **30 June 2011** – Appointment of Marzena Piszczek, Zbigniew Ćwiąkalski, Dariusz Daniluk, Zbigniew Derdziuk, Krzysztof Dresler, Dariusz Filar and Waldemar Maj to the PZU Supervisory Board for its new term of office;
- **1 July 2011** – PZU a patron of the National Cultural Program in the Polish Presidency of 2011 during Poland's presidency of the Council of the European Union;
- **22 July 2011** – confirmation of the financial strength rating held by PZU and PZU Życie by Standard & Poor's Ratings Services at the level of „A", rating outlook for both companies upheld as stable;
- **27 July 2011** – ING PTE SA's notification of ING Otwarty Fundusz Emerytalny exceeding 5% of the total number of votes at PZU's Shareholder Meeting;
- **20 September 2011** – publication of PZU's first Corporate Social Responsibility Report concerning the company's sustainable development and social activity prepared under GRI's guidelines and standards (Global Reporting Initiative) coupled with the Sustainability Reporting Guidelines & Financial Services Sector Supplement;
- **30 September 2011** – determination of the list of shareholders entitled to a dividend payout for 2010;

- **6 October 2011** – resignation tendered by Marcin Halbersztadt from being a Management Board member of PZU and PZU Życie;
- **21 October 2011** – 2010 dividend payout of PLN 2,245,159,800.00, i.e. PLN 26.00 gross per share;
- **1 December 2011** – launch of the E-szkoda system facilitating web-based end-to-end claims handling, on-line contact with PZU 24 hours a day, 7 days a week;
- **15 December 2011** – PZU recognized as the third most valuable and strongest brand in the annual ranking of the most valuable Polish brands published by the „Rzeczpospolita" daily (second place in the finance category);
- **31 January 2012** – inclusion of PZU in the Respect Index – the first CEE region index consisting of socially-responsible corporates;
- **15 March 2012** – publication of the PZU Group Strategy in 2012-2014.
- **10 May 2012** – Brand Refresh Day.

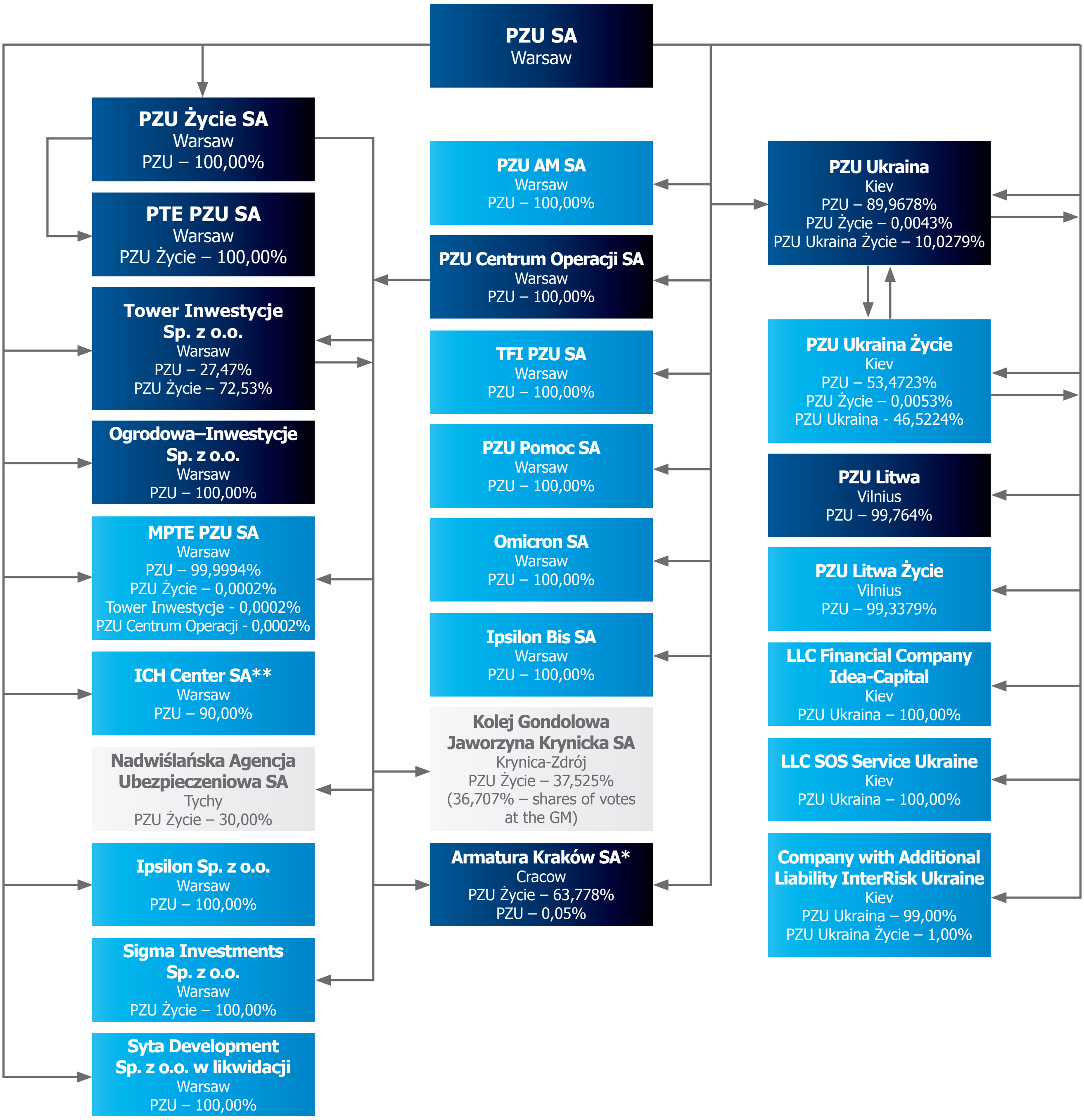
8. PZU GROUP'S ORGANIZATIONAL STRUCTURE

PZU is a member of the PZU Group as its parent company along with 8 consolidated companies which hold shares in 17 non-consolidated companies.

The operations of the PZU Group entail a variety of insurance services. PZU Group member companies offer services in life, property and casualty insurance and they manage customers' assets in an open-end pension fund and investment funds.

No considerable changes were made to the activity of the PZU Group's core companies in 2011.

PZU Group structure
Major companies as at 31/12/2011



* Armatura Capital Group includes following companies: Armatura Kraków SA, Armatoora SA, Armatoora SA i wspólnicy sp. k., Armagor SA.
** on 16 March 2012 saw the opening of liquidation of ICH Center SA

Consolidated subsidiaries | Non-consolidated subsidiaries | Associated companies

The scope of activities of the PZU Group entities

No.	Entity's name	Registered office	Date of commencing/significant impact	Business activity
Consolidated entities				
1	Powszechny Zakład Ubezpieczeń SA	Warsaw	nd.	Property and casualty insurance.
2	Powszechny Zakład Ubezpieczeń na Życie SA	Warsaw	18.12.1991	Life insurance.
3	Powszechne Towarzystwo Emerytalne PZU SA („PTE PZU”)	Warsaw	08.12.1998	Pension fund managment.
4	PZU Centrum Operacji SA („PZU CO”)	Warsaw	30.11.2001	Auxiliary activity related to insurance and pension funds.
5	Tower-Inwestycje Sp. z o.o. („Tower-Inwestycje”)	Warsaw	27.08.1998	Acquisition, operation, lease and disposal of real property.
6	PrJSC IC PZU Ukraine („PZU Ukraine”)	Kiev (Ukraine)	01.07.2005	Property insurance.
7	UAB DK PZU Lietuva („PZU Lietuva”)	Vilnius (Lithuania)	26.04.2002	Property insurance.
8	Ogrodowa-Inwestycje Sp. z o.o.	Warsaw	15.09.2004	Acquisition, operation, lease and disposal of real property.
9	Armatura Kraków SA[1)]	Cracow	07.10.1999	Production of kitchen and bathroom fixtures.
10	Armatoora SA[1)]	Nisko	10.12.2008	Production of radiators and aluminium casts.
11	Armatoora SA i wspólnicy sp. k.[1)]	Cracow	10.02.2009	Use of free funds, development investments.
12	Armagor SA (until to 5 April 2011: Armagor Sp. z o.o.)[1)]	Gorzów Śląski	06.09.2009	Production of valves, tooling services.
13	PZU Specjalistyczny Fundusz Inwestycyjny Otwarty Dłużny[2)]	Warsaw	15.12.2009	Investments of funds collected from members.
Unconsolidated subsidiaries				
14	PZU Pomoc SA	Warsaw	18.03.2009	Assistance services.
15	Ipsilon Sp. z o.o.[3)]	Warsaw	02.04.2009	Assistance and medical services.
16	Ipsilon Bis SA	Warsaw	02.09.2011	The Company does not conduct activities.
17	Omicron SA	Warsaw	13.09.2011	The Company does not conduct activities.
18	Syta Development Sp. z o.o. w likwidacji	Warsaw	29.04.1996	Acquisition and disposal of real property, trade agency and administration of real property.
19	Towarzystwo Funduszy Inwestycyjnych PZU SA („TFI PZU”)	Warsaw	30.04.1999	Creation, representing and management of mutual funds.
20	Sigma Investments Sp. z o.o.[3)]	Warsaw	28.12.1999	Investment activity, Acquisition and disposal of shares in public companies, bonds and other listed securities.
21	PZU Asset Management SA („PZU AM”)	Warsaw	12.07.2001	Managed account services.

The scope of activities of the PZU Group entities – cont.

No.	Entity's name	Registered office	Date of commencing/significant impact	Business activity
22	Międzyzakładowe Pracownicze Towarzystwo Emerytalne PZU SA („MPTE PZU SA")	Warsaw	13.08.2004	Management of employee pension fund.
23	PrJSC IC PZU Ukraine Life Insurance („PZU Ukraine Life")	Kiev (Ukraine)	01.07.2005	Life insurance.
24	LLC SOS Services Ukraine	Kiev (Ukraine)	01.07.2005	Assistance services.
25	Company with Additional Liability Inter-Risk Ukraine („Inter Risk")[4)]	Kiev (Ukraine)	01.07.2005	Legal services.
26	LLC Finansowa Kompania Idea-Kapitał	Kiev (Ukraine)	06.10.2011	Financial services.
27	UAB PZU Lietuva Gyvybes Draudimas	Vilnius (Lithuania)	26.04.2002	Life insurance.
28	ICH Center SA[5)]	Warsaw	31.01.1996	Motor claims handling under the Green Card (from the beginning of 2011 the Company is inactive).
Associated companies				
29	Kolej Gondolowa Jaworzyna Krynicka SA	Krynica	17.08.1998	Operation of gondola lifts.
30	Nadwiślańska Agencja Ubezpieczeniowa SA	Tychy	08.06.1999	Insurance activities.

1) Consolidated using the full method since 1 January 2011.
2) Consolidated using the full method since 30 June 2011.
3) Company does not conduct operations.
4) On 22 December 2011 PZU Ukraine and PZU Ukraine Life concluded an agreement with PKO BP SA for the sale of Inter-Risk, on 16 January 2012 the ownership rights to shares in Inter Risk were transferred to the acquirer.
5) Since 1 January 2011, the Company does not conduct operations, the Extraordinary Shareholder Meeting Resolution of 8 March 2012 decided to initiate the process of liquidation on 16 March 2012.

In the latter part of the document describing the scope of operations and the results of the PZU Group, the following entities in particular were incorporated having regard for their participation in the main areas of the PZU Group's activity:
- PZU SA (PZU)
- PZU Życie SA (PZU Życie)
- PTE PZU SA (PTE PZU)
- PZU Lietuva
- PZU Ukraine
- TFI PZU SA (TFI PZU)
- PZU Asset Management SA (PZU AM)
- PZU Pomoc SA (PZU Pomoc)
- PZU Centrum Operacji SA (PZU CO SA)

9. THE PZU MANAGEMENT BOARD AND SUPERVISORY BOARD

PZU Management Team (as at 31 March 2012)

Andrzej Klesyk
CEO of PZU
Head of the PZU Group.

Przemysław Dąbrowski
Management Board Member of
PZU and PZU Życie
CFO
Responsible for accounting, planning and controlling, tax policy and actuarial issues.

Witold Jaworski
Management Board Member of
PZU and PZU Życie
Responsible for retail insurance, bancassurance, sales network and marketing.

Bogusław Skuza
Management Board Member
of PZU
Responsible for corporate insurance and reinsurance.

Tomasz Tarkowski
Management Board Member of
PZU and PZU Życie
Responsible for claims handling and assistance.

Ryszard Trepczyński
Management Board Member of
PZU and PZU Życie
Responsible for investments and macroeconomic analyses.

Dariusz Krzewina
CEO of PZU Życie
PZU Group Director
Responsible for life insurance, HR and the PZU Group's network

Rafał Grodzicki
Management Board Member of
PZU Życie
PZU Group Director
Responsible for the contact center and insurance operations.

Przemysław Henschke
Management Board Member
of PZU Życie
PZU Group Director
Responsible for IT.

Sławomir Niemierka
Management Board Member of
PZU Życie
PZU Group Director
Responsible for security and risk management.

Composition of the PZU Management Board

On 1 January 2011 the composition of the PZU Management Board was as follows:
- **Andrzej Piotr Klesyk** – CEO of PZU;
- **Witold Jaworski** – PZU Management Board Member;
- **Przemysław Dąbrowski** – PZU Management Board Member.

The Supervisory Board appointed Mr. Tomasz Tarkowski to be a Management Board Member as of 21 April 2011.

The Supervisory Board appointed Mr. Marcin Halbersztadt to be a Management Board Member as of 15 May 2011.

The Supervisory Board appointed Mr. Bogusław Skuza and Mr. Ryszard Trepczyński to be Management Board Members as of 1 July 2011.

On 6 October 2011 Marcin Halbersztadt tendered his resignation from being a PZU Management Board Member.

As of 31 December 2011 the PZU Management Board's composition was as follows:
- **Andrzej Piotr Klesyk** – CEO of PZU;
- **Witold Jaworski** – PZU Management Board Member;
- **Przemysław Dąbrowski** – PZU Management Board Member.
- **Tomasz Tarkowski** – PZU Management Board Member;
- **Bogusław Skuza** – PZU Management Board Member;
- **Ryszard Trepczyński** – PZU Management Board Member.

The PZU Management Board's current term of office commenced on 28 June 2011 and lasts for three consecutive full financial years. The mandates of Management Board members expire at the latest on the date of holding the Shareholder Meeting approving the financial statements for the most recent full financial year when they are in office.

Composition of the PZU Supervisory Board

As at 1 January 2011 the following persons sat on the PZU Supervisory Board:
- **Marzena Piszczek** – Supervisory Board Chairwoman;
- **Zbigniew Ćwiąkalski** – Supervisory Board Vice-Chairman;
- **Krzysztof Dresler** – Supervisory Board Member;
- **Dariusz Filar** – Supervisory Board Member;
- **Waldemar Maj** – Supervisory Board Member;
- **Piotr Maciej Kamiński** – Supervisory Board Member,
- **Grażyna Piotrowska-Oliwa** – Supervisory Board Secretary

On 30 June 2011 the Ordinary Shareholder Meeting appointed the following persons to the PZU Supervisory Board:
- **Marzena Piszczek** – Supervisory Board Member
- **Zbigniew Ćwiąkalski** – Supervisory Board Member
- **Krzysztof Dresler** – Supervisory Board Member
- **Dariusz Filar** – Supervisory Board Member
- **Waldemar Maj** – Supervisory Board Member
- **Zbigniew Derdziuk** – Supervisory Board Member
- **Dariusz Daniluk** – Supervisory Board Member

On 30 June 2011, the Supervisory Board of PZU was constituted. The Supervisory Board decided to entrust the function of its Chairman to Marzena Piszczek, the function of Deputy Chairman to Zbigniew Ćwiąkalski and the function of Secretary of the Board to Krzysztof Dresler.

The current term of office of the Supervisory Board of PZU started on 30 June 2011 and will end after three consecutive full financial years. The mandates of the Supervisory Board members shall expire at the latest on the date of holding the General Meeting to approve the financial statements for the last full financial year of their performing their functions, i.e. on the date of holding the Annual General Meeting in 2015.

10. CORPORATE GOVERNANCE

Corporate governance principles

In 2011, PZU complied with „The Best Practices of Companies Listed on the Warsaw Stock Exchange" binding on the Warsaw Stock Exchange (hereinafter: „The Best Practices of WSE Listed Companies"). The code of „The Best Practices of the WSE Listed Companies" is available on the website (www.corp-gov.gpw.pl) devoted to corporate governance on the Warsaw Stock Exchange and on the Company's website www.pzu.pl in the section dedicated to PZU's shareholders – „Investor Relations".

In addition to the above-mentioned corporate governance principles, PZU adheres to the principles of ethics and social responsibility set forth in the following documents:

- Principles of Good Insurance Practices enacted on 8 June 2009 by the General Meeting of the Polish Insurance Association („PIA") whose members are insurance companies operating on the Polish market. The principles adopted by PZU regulate the rules of conduct for insurance companies in relations with clients, insurance agents, the Polish Financial Supervision Authority (KNF), the Polish Insurance Ombudsman and the media. They also regulate relations between insurers and how insurance companies act in public securities trading. This document is available on PIA's website.
- The Best Practices in PZU. This document underlines the role of ethical values binding in all aspects of PZU's operations. It describes the best business practices in PZU. It promulgates and promotes a culture of compliance with the binding law, making decisions based on ethical criteria and taking responsibility for the decisions made. This document is available on PZU's website.
- PZU's social responsibility report. This is the first report concerning PZU's sustainable development and social responsibility and was prepared based on the guidance and standards of the Global Reporting Initiative (GRI) using the Sustainability Reporting Guidelines & Financial Services Sector Supplement. This report is part of implementing PZU's corporate social responsibility (CSR) strategy and raises a number of issues in various areas, including: corporate governance, availability of services, product quality, data security, the effect of PZU's operations on the natural environment and PZU's active involvement in social activities. This document is also available on PZU's website.

Application of „The Best Practices of WSE Listed Companies"

2011 confirmed PZU's dedication to pursuing the highest corporate governance standards in that it did not breach any of the rules in The Best Practices of WSE Listed Companies, described in chapters II, III and IV, in line with the recommendations in points I.5. and I.9. of The Best Practices of WSE Listed Companies. The announcement of not fully complying with those recommendations was not made, in line with the exemption based on the resolution of the Management Board of WSE of 11 December 2007 concerning the obligation to publish reports referred to in § 29 clause 3 of the Rules and Regulations of WSE in respect of corporate governance rules contained in section I of The Best Practices of WSE Listed Companies. With regard to chapter I of The Best Practices of WSE Listed Companies containing „Recommendations", two points deserve additional commentary.

With reference to recommendation I.5 of The Best Practices of WSE Listed Companies concerning compensation policy for members of management and supervisory bodies, the decision on the compensation of Supervisory Board members is one of the powers of PZU's Shareholder Meeting while the PZU Supervisory Board makes decisions on the compensation of the Management Board members by resolution.

The compensation of Supervisory Board members is clearly specified in a Shareholder Meeting resolution. The level of compensation depends on the function performed in the Supervisory Board and is not due in a month in which a given Supervisory Board member is absent from a meeting for an unjustified reason. The Supervisory Board decides by resolution whether the absence of a Supervisory Board member is justified or unjustified.

The principles for compensating Management Board members are specified by the Supervisory Board. The compensation of Management Board members consists of several components and comprises basic monthly salary, additional benefits and an annual bonus paid once a year depending on the Supervisory Board's decision made in the form of a resolution based on the economic and financial results for a given financial year.

The compensation policy for members of management and supervisory bodies does not contain all the elements indicated in the Recommendation of the European Commission of 14 December 2004 fostering an appropriate regime for the remuneration of directors of listed companies (2004/913/EC), as supplemented by the Recommendation of the EC of 30 April 2009 (2009/385/EC).

Another matter requiring clarification is the recommendation contained in point I. 9 of The Best Practices of WSE Listed Companies referring to ensuring balanced participation of women and men in the company's bodies. PZU has always maintained a policy of appointing competent and creative persons who have the appropriate professional experience and education as members of its bodies. The composition of the Management and Supervisory Boards is determined by a decision of the Supervisory Board and the Shareholder Meeting, and other factors, including the person's gender, are not taken into account.

Currently, there is one woman in the seven-member Supervisory Board, namely Marzena Piszczek who is the Supervisory Board Chairwoman.

Since 1 January 2012 PZU adheres to and executes the recommendations in the amended set of The Best Practices of WSE Listed Companies (resolution of the Supervisory Board of WSE no. 20/1287/2011 concerning the amendment of the principles of The Best Practices of WSE Listed Companies binding from 1 January 2012).

The Shareholder Meeting and shareholder rights

PZU's Annual Shareholder Meeting should be held within six months after the end of each financial year of the Company.

An Extraordinary Shareholder Meeting is convened in the cases specified in the Commercial Companies Code Act dated 15 September 2000 (Journal of Laws, No. 94 of 2000, Item 1037. as amended, „the Commercial Companies Code"), the Insurance Activity Act, the Articles of Association and when PZU's bodies or persons authorized to convene an Extraordinary Shareholder Meeting consider it appropriate.

In accordance with the provisions of the Articles of Association, the Supervisory Board convenes:
- the Annual Shareholder Meeting when the Management Board fails to convene such Annual Shareholder Meeting by the prescribed deadline;
- an Extraordinary Shareholder Meeting when it considers it appropriate;
- an Extraordinary Shareholder Meeting when the Management Board fails to convene an Extraordinary Shareholder Meeting based on the motion of an authorized shareholder, authorized shareholders or the Supervisory Board within 14 days of the date of submitting such a motion

The Articles of Association also provide that shareholders representing at least one half of the share capital or at least one half of the total number of votes in the Company may convene an Extraordinary Shareholder Meeting. These shareholders appoint the chairman of such Extraordinary Shareholder Meeting.

The Supervisory Board and the shareholder or shareholders in PZU representing at least one twentieth of the share capital may request that individual matters be put on the agenda of the next Shareholder Meeting. This request should contain a justification for the draft resolution concerning the proposed point on the agenda and should be reported to the Management Board no later than twenty one days before the set date of the Shareholder Meeting. The Management Board is obliged to announce changes to the agenda introduced at the request of shareholders immediately, no later however than eighteen days before the set date of the Shareholder Meeting. The announcement should be made on PZU's website and in accordance with the procedure for announcing current information specified in the provisions of the Act dated 19 July 2005 on public offering and terms and conditions of introducing financial instruments to an organized trading system and on public companies (Journal of Laws, No. 184 of 2005, Item 1539 as amended, „the Act on public offering"), i.e. in the form of current reports.

Before the date of the Shareholder Meeting, PZU's shareholder or shareholders representing at least one twentieth of the company's share capital may submit to the company in writing or using electronic communication means, draft resolutions concerning matters introduced onto the agenda of the Shareholder Meeting or matters which are to be introduced onto the agenda. The Company immediately announces draft resolutions on its website. During the Shareholder Meeting, each shareholder of PZU may propose draft resolutions concerning matters introduced onto the agenda.

The Shareholder Meeting is convened by an announcement published on PZU's website and in line with the procedure for reporting current information specified in the provisions of the Act on public offering, i.e. in the form of current reports. The announcement should be made at least twenty six days before the date of the Shareholder Meeting.

A properly convened Shareholder Meeting is valid, regardless of the number of shareholders in attendance or shares represented at the meeting.

The Shareholder Meeting is held in Warsaw.

The right to participate in the Shareholder Meeting is vested only in persons who are PZU shareholders sixteen days before the date of a Shareholder Meeting (record date to participate in the Shareholder Meeting).

At the request of an authorized entity based on dematerialized shares in PZU submitted no earlier than after the announcement of the Shareholder Meeting being convened and no later than on the first working day after the record date to participate in a Shareholder Meeting, the entity maintaining the securities account issues a registered certificate of the right to participate in the Shareholder Meeting.

The certificates concerning the right to participate in a Shareholder Meeting issued by an entity maintaining securities accounts shall constitute the basis for that entity to prepare a list, which shall then be sent to the National Securities Depository („KDPW") as the entity maintaining the securities depository. On this basis, KDPW shall prepare a list of the shares authorized to participate in a Shareholder Meeting. The list prepared by KDPW shall be sent to the Company and shall constitute the basis for PZU to prepare a list of shares authorized to participate in a Shareholder Meeting.

In the period between the record date to participate in a Shareholder Meeting and the date of closing such a Shareholder Meeting, a PZU shareholder may transfer shares.

Each share gives the right to one vote at the Shareholder Meeting, taking into account the restrictions concerning the exercise of voting rights. A shareholder may vote each share differently. PZU shareholders may participate in a Shareholder Meeting and exercise voting rights in person or through a proxy.

Powers of the Shareholder Meeting

The Shareholder Meeting is a body authorized to make decisions through resolutions in matters related to PZU's organization and operation. Shareholder Meeting resolutions are adopted by an absolute majority of votes, except for the special cases provided for in the Commercial Companies Code or the Articles of Association. In accordance with the Articles of Association, Shareholder Meeting resolutions concerning the following matters require a qualified majority of three fourths of the votes: (i) changing the Articles of Association, (ii) reducing share capital, (iii) selling and leasing the enterprise or a business unit and establishing a limited property right on them. Shareholder Meeting resolutions relating to preference shares and matters of the Company's business combination by transferring all its assets to another company or a merger by forming a new company, closing the Company (also as a result of moving its seat or main office abroad), its liquidation, transformation or reduction in share capital by cancellation of a portion of the shares without at the same time increasing it, require a 90% majority of the votes cast.
The most significant powers of the Shareholder Meeting specified in the Commercial Companies Code and PZU's Articles of Association include passing resolutions concerning, in particular, the following:

- reviewing and approving the Directors' Report and the financial statements for the prior financial year and granting discharges to individual members of the Company's bodies for performing their duties;
- distributing profit or covering loss;
- making decisions relating to claims to remedy losses arising in the course of forming the Company or its management or supervision;
- selling and leasing the enterprise or a business unit and placing restricted property rights upon them;
- cancelling shares and issuing bonds;
- forming reserve capital accounts and deciding on their use or how to use them;
- demerging the Company, merging the Company with another company, liquidating or closing the Company;
- appointing and dismissing Supervisory Board members, in recognition of the State Treasury's personal right to appoint and dismiss one Supervisory Board member.
- Company buying or selling real property, perpetual usufruct or a share in real property or in perpetual usufruct with a gross value exceeding the equivalent of EUR 30,000,000 (thirty million Euro).

Shareholder rights and their exercise

Shareholder rights stem from the provisions of the Commercial Companies Code and PZU's Articles of Association.
Company shareholders have the right to view the list of shareholders entitled to participate in a Shareholder Meeting and request a copy of the list, while reimbursing the costs of its preparation.

Company shareholders may request that the list of shareholders be sent to them free of charge by electronic mail, after giving the address to which the list should be sent.

Each Company shareholder has the right to request a copy of the motions concerning the issues on the agenda of the next Shareholder Meeting one week before the Shareholder Meeting. The request should be submitted to the Management Board.

Immediately after selecting the chairman of the Shareholder Meeting, an attendance list should be prepared containing the list of participants in the Shareholder Meeting, including the number of shares represented by each shareholder and the number of votes attached to them. The attendance list should be signed by the chairman of the Shareholder Meeting and displayed during the meeting.

At the request of shareholders holding one tenth of the share capital represented at the Shareholder Meeting, the attendance list should be verified by a commission elected for this purpose, composed of at least three persons. The persons presenting this motion have the right to elect one member to this commission.

At the request of shareholders representing at least one fifth of the Company's share capital, the election of the Supervisory Board should be performed by the next Shareholder Meeting through voting in separate groups, even if the Articles of Association provide for a different manner of appointing the Supervisory Board. Persons representing such a percentage of the shares at the Shareholder Meeting arrived at by dividing the total number of shares represented at a Shareholder Meeting by the number of Supervisory Board members (in the Company's case – five Supervisory Board members) may form a separate group in order to elect one Supervisory Board member, but they may not participate in the election of the remaining Supervisory Board members. Mandates in the Supervisory Board not filled by an appropriate group of shareholders as part of the procedure described above, shall be filled by a vote of all the Company's shareholders who do not cast votes when electing Supervisory Board members by voting in separate groups. In the event that shareholders representing at least one fifth of the Company's share capital file a motion for electing the Supervisory Board by voting in separate groups, the provisions of the Articles of Association providing for a different manner of appointing the Supervisory Board shall not apply in respect of such election of the Supervisory Board, in recognition of the fact that if the Supervisory Board contains a person appointed by an entity specified in a separate Act, only the remaining members of the Supervisory Board shall be elected.

During the Shareholder Meeting, the Management Board is obliged to provide Company-related information to a shareholder at his request, if it is justified for the purpose of evaluating the issue covered by the agenda of the Shareholder Meeting. The Management Board shall refuse to provide information if it could cause damage to the Company, a related company or a subsidiary company or cooperative, in particular should it disclose technical, trade or organizational secrets of the enterprise. A Management Board member may refuse to provide information should it constitute a basis for his or her penal, civil law or administrative liability. A response shall be considered to have been given if the relevant information is available on PZU's website in the place designated for shareholders to ask questions and to answer them. In response to a shareholder request, the Management Board may respond in writing outside the Shareholder Meeting if there are valid reasons to do so. The Management Board is obliged to provide an answer no later than within two weeks from the date of a request during a Shareholder Meeting. In the event of a shareholder request for Company-related information outside the Shareholder Meeting, the Management Board may respond to the shareholder in writing, taking into account the restrictions concerning the possibility of causing damage, referred to above. In the documentation submitted to the next Shareholder Meeting, the Management Board discloses in writing the information provided to shareholders outside the Shareholder Meeting, including the date of its provision and its recipients. The information provided to the next Shareholder Meeting need not comprise publicized information and provided during a Shareholder Meeting.

Shareholders whose information requests during a Shareholder Meeting are denied and who file an objection in the minutes, may file an application with the registration court to oblige the Management Board to provide the information. The application should be submitted within one week of the closing of the Shareholder Meeting at which the information request was denied. Shareholders may also file an application with the registration court to oblige the Company to publish the information provided to another shareholder outside the Shareholder Meeting. In accordance with the Decree of 19 February 2009 on current and periodic information to be prepared by issuers of securities and conditions for considering as equivalent the information required by the provisions of the law of a non-EU state (Journal of Laws, No. 33 of 2009, Item 259; „the Decree on current and periodic information"), the Company shall be obliged to provide, in the form of a Periodic Report, information provided to a shareholder due to Management Board having been obliged to do so by the registration court in the cases referred to above.

The PZU's management and supervisory bodies and their committees

PZU Management Board

In accordance with PZU's Articles of Association, the Management Board is composed of three to seven members appointed for a joint term of office which covers three full consecutive financial years. The members of the Management Board, including the CEO, are appointed and dismissed by the Supervisory Board, and additionally, Management Board Members are appointed and dismissed by the Supervisory Board on a motion submitted by the CEO. The CEO for a new term of office appointed before the expiry of the current term of office may submit a motion to the Supervisory Board to appoint the remaining Management Board Members for the new term of office before the expiry of the current term of office.

The operation and powers of the Management Board arising from the Articles of Association

The Management Board exercises all the rights in the scope of managing the Company, which are not reserved by the provisions of the law or the provisions of the Articles of Association to the Shareholder Meeting or the Supervisory Board.

The Management Board enacts its rules and regulations which are approved by the Supervisory Board. The operations of the Management Board are directed by the CEO who establishes the scope of responsibilities for individual Management Board Members. Management Board resolutions are passed only in the presence of the CEO or a person appointed to direct the work of the Management Board in his absence, and provided that at least one half of the Management Board Members are present at the meeting. Management Board resolutions are passed by an absolute majority of votes and if the number of votes is equal, the CEO has the casting vote. The Management

Board, with the CEO's approval, may pass resolutions by circulation, in a written or electronic form (i.e. using remote means of communication and using a qualified electronic signature). The Articles of Association also provide for the possibility of holding Management Board meetings using remote means of direct communication. Two Management Board Members acting jointly or one Member acting jointly with a commercial proxy are authorized to represent the Company.

The operation and powers of the Management Board arising from the Management Board's rules and regulations

The Management Board's rules and regulations were enacted by the Management Board on 23 February 2010 and approved by the Supervisory Board by a resolution dated 4 March 2010.

The Management Board's rules and regulations regulate: (i) the scope of the Management Board's powers and the scope of actions requiring the Supervisory Board's permission or approval; (ii) the powers of the CEO and of the remaining Management Board Members; (iii) the rules and organization of the Management Board's work, including organization of meetings and the procedure for making decisions; and (iv) the rights and obligations of Management Board Members who tender their resignations.

In accordance with the Management Board's rules and regulations, the following issues in particular require a Management Board resolution:

- adopting a long-term plan for the Company's development and its operation;
- adopting a plan for the operations and development of the PZU Group;
- adopting an annual financial plan and a report on its execution;
- adopting the financial statements for the prior financial year and the Directors' Report of the Company;
- adopting a proposition concerning the distribution of profit or covering a loss;
- establishing tariffs for compulsory and voluntary insurance contributions and the general terms and conditions for voluntary insurance;
- establishing the scope and size of outward reinsurance and tasks in the scope of inward reinsurance;
- adopting the annual audit and control plan and report on its execution including conclusions;
- establishing the principles for investment, prevention and sponsorship activities;
- granting warranties and guarantees (excluding those which constitute insurance procedures) and drawing and granting loans and borrowings by the Company (excluding loans and borrowings granted from the Company Social Fund); and
- granting powers of attorney.

In accordance with the Management Board's Rules and Regulations, Management Board meetings are held no less frequently than once every two weeks. The work of the Management Board is directed by the CEO, whose powers include in particular:

- establishing the scope of responsibilities for individual Management Board Members;
- convening Management Board meetings;
- drawing up the agenda for Management Board meetings;
- applying to the Supervisory Board to appoint or dismiss Management Board members;
- appointing a person to direct the Management Board's work in the CEO's absence.

The CEO makes decisions in the form of directives and official orders. The remaining Management Board Members direct the Company's activities within the scope of responsibilities established by the CEO.

PZU's Articles of Association do not specify any particular rights for the Management Board to make decisions on the issue or redemption of shares.

Supervisory Board

The Supervisory Board is composed of seven to eleven members: The number of Supervisory Board members is established by the Shareholder Meeting. The Supervisory Board members are appointed by the Shareholder Meeting for a joint term of office lasting for three full consecutive financial years. At least one member of the Supervisory Board must have accounting or auditing qualifications as defined in and in accordance with the provisions of the Act of 7 May 2009 on statutory auditors and their self-government, audit firms authorized to audit financial statements and on public supervision (Journal of Laws, No. 649 of 2009, Item 77, „the Act on Statutory Auditors"). Additionally, at least one Supervisory Board member should meet all the independence criteria specified in the Articles of Association (the Independent Member) concerning, among others, professional relations or kinship, in particular with members of management and supervisory bodies of the PZU and the PZU Group companies. The Independent Member is obliged to submit a written statement to the Company concerning his meeting all the independence criteria provided for in the Articles of Association and inform PZU of ceasing to meet those criteria. Moreover, the Articles of Association grant the State Treasury the personal right to appoint and dismiss one Supervisory Board member by written statement submitted to the Management Board. This right shall expire when the State Treasury ceases to be a PZU shareholder.

The operation and powers of the Supervisory Board arising from the Articles of Association

The Supervisory Board exercises constant supervision over PZU's operations in all areas of its activity.
In accordance with the Articles of Association, the Supervisory Board's powers include:

- evaluating the Directors' Report and the financial statements for the prior financial year in terms of their compliance with ac-

counting ledgers and documents and the actual state of affairs;
- evaluating the Management Board's proposals concerning the distribution of profit or coverage of loss;
- submitting a written report to the Shareholder Meeting on the results of the evaluation referred to in the points above and submitting a brief annual assessment of the Company's standing, including an assessment of the internal control system and the system for managing the Company's significant risks , and an annual report on the activities of the Supervisory Board;
- concluding, terminating and amending contracts with Management Board members and establishing the principles for their compensation as well as the level of compensation;
- appointing, suspending and dismissing the CEO, the Management Board Members and the entire Management Board as well as making decisions on ceasing any such suspension;
- granting approval for the transfer of a whole or part of the insurance portfolio;
- accepting the Management Board's motions concerning the purchase, taking up or selling of shares in companies and concerning the Company's participation in other entities – the Supervisory Board may specify up to what amount and on what terms and in what mode the Management Board can perform the aforementioned actions without the obligation to obtain the Supervisory Board's approval;
- delegating members of the Supervisory Board to perform temporarily the duties of Management Board members who are dismissed, resign or are unable to perform their duties for other reasons;
- accepting instructions concerning the exercise of voting rights by the Company's representatives at Shareholder Meetings of PZU Życie in matters relating to: increasing or reducing share capital, issuing bonds, selling and leasing out the PZU Życie enterprise and establishing the right of use thereon, demerger of PZU Życie, merger of PZU Życie with another company, liquidation or closing of PZU Życie;
- electing the audit firm authorized to audit the financial statements to whom the audit of the Company's annual financial statements shall be entrusted;
- establishing the consolidated text of the amended Articles of Association;
- approving the Company's long-term development plans and the annual financial plans prepared by the Management Board;
- approving the Management Board's rules and regulations;
- analyzing and giving opinions on issues brought by the Management Board for the consideration of the Shareholder Meeting.

Moreover, the Supervisory Board's powers include granting approval to:
- buy or sell real property, perpetual usufruct or a share in real property or in perpetual usufruct with a value exceeding the equivalent of EUR 3 million;
- the Company to conclude a significant contract with a related entity as defined in the Decree on current and periodic information, excluding typical contracts concluded by the Company on an arm's length basis as part of its operating activities;
- the Company to conclude a contract with a standby underwriter referred to in Art. 433 § 3 of the Commercial Companies Code;
- make payments of interim dividends;
- form and close regional branches and foreign branches.

The Supervisory Board enacts rules and regulations regulating its organization and mode of operation. In accordance with the Articles of Association, Supervisory Board meetings are held at least once every quarter. The Supervisory Board may delegate its members to perform specific supervision tasks independently and appoint ad hoc committees for this purpose. The scope of duties of a delegated Supervisory Board member and of a committee are specified in a Supervisory Board resolution.

Supervisory Board resolutions are passed by an absolute majority of votes. If the number of votes is equal, the Supervisory Board Chairman has the casting vote. The Supervisory Board may pass resolutions both using remote means of direct communication and in writing by circulation. Moreover, the Articles of Association provide for the possibility of casting votes in writing through another Supervisory Board member. In accordance with the Articles of Association, the Supervisory Board resolutions are passed in an open ballot, except for resolutions concerning the delegation of Supervisory Board members to perform temporarily the functions of Management Board members and concerning the appointment, suspension and dismissal of the CEO, Management Board Members or the entire Management Board, as well as making decisions on ceasing such suspension, which are made in a secret ballot. Moreover, a secret ballot can be ordered based on a motion submitted by a Supervisory Board member.

The operation and powers of the Supervisory Board arising from the Supervisory Board's Rules and Regulations

The Supervisory Board's Rules and Regulations were enacted by the Supervisory Board on 4 March 2010.

The Supervisory Board's Rules and Regulations specify the composition and the manner of appointing the Supervisory Board as well as the scope of the Supervisory Board's operations and the method for convening the Supervisory Board and conducting meetings.

The Supervisory Board elects from among its members the Supervisory Board Chairman and Deputy Chairman. In accordance with the Supervisory Board's Rules and Regulations, apart from appointing the IPO committee provided for in the Articles of Association, the audit committee and the nomination and compensation committee, in order to perform its supervisory duties properly the Supervisory Board may appoint other standing advisory and consultative committees with powers, in a composition, and with work procedures established in the rules and regulations of a given committee enacted by the Supervisory Board. The Supervisory Board's Rules and Regulations provide for the possibility of the Supervisory Board and the committees appointed by it availing themselves of the services of experts and advisory firms. Management Board Members (invited by the Supervisory Board) and the Company's employees named by the competent Management Board in the matters discussed at the meeting may participate, among others, in the Supervisory Board's meetings without a voting right. The PZU Supervisory Board may also invite members of the management and supervisory bodies of other PZU Group companies to a joint meeting for a specific purpose. Moreover, Supervisory Board members are entitled, with the Supervisory Board's approval, to select no more than one advisor authorized to participate with an advisory vote in Supervisory Board meetings devoted to financial reports and financial statements, provided that such persons maintain confidentiality and sign a non-disclosure agreement.

Supervisory Board Committees

Audit Committee

The Articles of Association provide for the Supervisory Board to appoint an audit committee. The committee is composed of three members, including at least one independent member with accounting or audit qualifications. The detailed tasks and principles for the appointment and operation of the audit committee are specified in a Supervisory Board resolution, which when electing audit committee members takes into account the skills and experience of the candidates in the matters entrusted to this committee.

In accordance with the rules and regulations, the audit committee is an advisory and consultative body to the Supervisory Board and is appointed in order to increase the effectiveness of the supervisory activities performed by the Supervisory Board in the scope of examining the correctness of financial reporting, the effectiveness of internal control, including the internal audit and risk management system. Moreover, the audit committee may apply to the Supervisory Board to commission the performance of specified control activities in the Company, and the controls commissioned may be performed by an internal unit or an external company.

The audit committee was appointed by a Supervisory Board resolution on 3 June 2008. As at 31 December 2011, the audit committee consisted of the following persons: Marzena Piszczek (Committee Chairwoman), Dariusz Filar (Committee member) and Dariusz Daniluk (Committee member). Dariusz Filar was named by the Supervisory Board as the independent member having accounting / audit qualifications as defined in Art. 86 clause 4 of the Act on Statutory Auditors.

Nomination and Compensation Committee

In accordance with the Articles of Association, from the moment of introducing the Company's shares to be traded on the regulated market as defined in the Act on trading in financial instruments dated 29 July 2005 (Journal of Laws, No. 183 of 2005, Item 1538 as amended), the Supervisory Board may appoint the nomination and compensation committee. The detailed tasks and principles for the appointment and operation of the nomination and compensation committee are specified by the Supervisory Board in a resolution. The committee should include at least one independent member. If the Supervisory Board is composed of five members as a result of voting on its composition, the nominations and salary committee shall not be formed and its tasks shall be performed by the Supervisory Board as a whole.

The nomination and compensation committee performs an advisory and consultative function for the Supervisory Board in the scope shaping the management structure, including organizational issues, the remuneration system and salaries and selecting staff with appropriate qualifications.

The Supervisory Board decided that the nomination and compensation committee shall be composed of four persons. On 30 June 2011, the Supervisory Board appointed a nomination and compensation committee composed of the following persons: Zbigniew Ćwiąkalski (Committee Chairman), Marzena Piszczek (Committee Member), Zbigniew Derdziuk (Committee Member), and Dariusz Filar (Committee Member). As at 31 December 2011, the composition of the nomination and compensation committee had not changed. The committee shall be dissolved on the date of appointing five members of the Supervisory Board by voting in groups, and its rights shall be taken over by the Supervisory Board as a whole.

Strategy Committee

In order to perform supervisory functions in the Company properly, the Supervisory Board may appoint standing committees with an advisory and consultative role. On 30 June 2011, the Supervisory Board appointed a strategy committee composed of the following persons: Waldemar Maj (Committee Chairman), Krzysztof Dresler (Committee Member), Marzena Piszczek (Committee Member) and Zbigniew Derdziuk (Committee Member). As at 31 December 2011, the composition of the strategy committee had not changed.

The objective of the strategy committee is to give opinions on all documents of a strategic nature submitted to the Supervisory Board by the Management Board (in particular, the Company's development strategy) and presenting recommendations to the Supervisory Board concerning planned investments which have a significant effect on the Company's assets.

PZU Group Directors

In addition to the members of the Management Board and the Supervisory Board, persons holding key senior management positions in the Company referred to as Group Directors are of significant importance to the operations of PZU and the PZU Group. These persons are also Management Board Members of PZU Życie.

As at 1 January 2011, the following persons were PZU Group Directors:
- Dariusz Krzewina;
- Krzysztof Branny.
- Przemysław Dąbrowski;
- Rafał Grodzicki;
- Mariusz J. Sarnowski.

On 2 January 2011, Przemysław Dąbrowski resigned as PZU Group Director and on 24 January 2011, the PZU Management Board dismissed Przemysław Dąbrowski from this post and appointed Tomasz Tarkowski Group Director from 1 February 2011.

On 4 May 2011, the PZU Management Board dismissed Tomasz Tarkowski as PZU Group Director. On 7 July 2011, the Management Board dismissed Mariusz Sarnowski as PZU Group Director effective from 20 June 2011. On 24 August 2011, the PZU Management Board dismissed Krzysztof Branny as PZU Group Director effective from 16 August 2011.

On 7 February 2012, the PZU Management Board appointed Przemysław Henschke PZU Group Director as of 1 February 2012. On 16 March 2012, the PZU Management Board appointed Sławomir Niemierka PZU Group Director as of 19 March 2012. As a result, as at 31 March 2012, the following persons were PZU Group Directors

- Dariusz Krzewina;
- Rafał Grodzicki;
- Przemysław Henschke;
- Sławomir Niemierka.

Discussion of the main features of the internal control and risk management systems applied in the PZU's enterprise in respect of the process of preparing financial statements and consolidated financial statements

The process of preparing financial statements is performed by the Finance Division of PZU supervised by a PZU Management Board Member.

The elements enabling proper performance of the process are: the accounting policies adopted by the PZU Management Board and the chart of accounts with a commentary, which set out the main principles for recording economic events in PZU, and the dedicated reporting systems.

The preparation of data in the source systems is subject to formalized operational and acceptance procedures, which define the scope of powers of individual persons.

PZU monitors changes in external regulations concerning, for example, accounting policies and reporting requirements for insurance companies, and carries out appropriate adaptation processes in these areas.

The process of closing the books and preparing financial statements is regulated by detailed schedules covering the key actions and control points as well as allocating responsibilities for timely and proper execution.

The key controls in the process of preparing financial statements comprise:

- controls and regular monitoring of the quality of the input data, supported by financial systems in which data correctness rules have been defined in accordance with the internal documents of PZU regulating the principles for controlling the correctness of accounting data;
- mapping data from source systems to the financial statements, supporting the correct presentation of data;
- analytical review of financial statements by specialists in order to confront them with the knowledge of the business and the business transactions conducted;
- formal review of the financial statements in order to confirm compliance with the binding legal regulations and market practice in the scope of the required disclosures.

PZU's standalone and consolidated financial statements are subject to:

- review by a statutory auditor - in the case of interim financial statements;
- audit by a statutory auditor - in the case of annual financial statements.

In accordance with PZU's Articles of Association, the PZU Supervisory Board appoints an audit committee composed of three members, including at least one member with accounting or auditing qualifications as defined in and in accordance with the requirements of the Act on statutory auditors. The audit committee is an advisory and consultative body to the PZU Supervisory Board and is appointed in order to increase the effectiveness of the supervisory activities performed by the PZU Supervisory Board within the scope of examining the correctness of PZU's financial reporting, the effectiveness of internal controls, including the internal audit and risk management system.

Consolidated financial reporting

Coordination of activities in consolidated financial reporting processes is achieved, among other things, by the organizational structure of the Finance Division in the Head Offices of PZU and PZU Życie, which is a joint unit, i.e. it is organized under a personal union, and additionally it also employs key persons on a part-time basis responsible for the reporting of the majority of the consolidated companies with their seats in Poland. In the case of all the consolidated subsidiaries, PZU performs control functions through the Management and Supervisory Boards of these companies.

The process of consolidated financial reporting is regulated by a number of internal documents regulating the accounting policies adopted in the PZU Group and the applied reporting standards, and by detailed schedules covering the key actions and control points as well as allocating responsibilities for timely and proper execution.

List of PZU shareholders directly or indirectly holding significant blocks of shares

As at 31 December 2011, PZU's shareholders holding significant blocks of shares are the State Treasury and ING Otwarty Fundusz Emerytalny. The State Treasury holds 30,385,253 shares, representing 35.19% of the Company's share capital and ING Otwarty Fundusz Emerytalny holds 4,339,308 shares, representing 5.02% of the Company's share capital.

The remaining shareholders hold a total of 51,627,739 shares, representing 59.79% of the Company's share capital.

PZU's share capital is divided into 86,352,300 registered and bearer shares with a nominal value of PLN 1 each, giving a right to 86,352,300 votes at the Shareholder Meeting.

Shareholding structure – as at 31 December 2010

Shareholders	31 December 2010		
	Number of shares	**% of share capital**	**% of votes at the Shareholder Meeting**
State Treasury	39,020,483	45.19%	45.19%
Other shareholders	47,331,817	54.81%	54.81%
Total	**86,352,300**	**100.00%**	**100.00%**

Shareholding structure – as at 31 December 2011

Shareholders	31 December 2011		
	Number of shares	**% of share capital**	**% of votes at the Shareholder Meeting**
State Treasury	30,385,253	35.19%	35.19%
ING Otwarty Fundusz Emerytalny	4,339,308	5.02%	5.02%
Other shareholders	51,627,739	59.79%	59.79%
Total	**86,352,300**	**100.00%**	**100.00%**

The PZU Management Board is not aware of any contracts concluded as a result of which changes might occur in the future in the percentage of shares held by current shareholders. Moreover, PZU did not buy any treasury stock in 2010 and 2011.

Holders of any securities awarding special controlling rights, including a description of those rights

PZU has not issued any securities that would give special controlling rights to the shareholders.

Restrictions on exercising voting rights

In accordance with PZU's Articles of Association, shareholders' voting rights have been restricted so that, at the Shareholder Meeting, no shareholder may have more than 10% of the total number of votes in the Company on the date of holding a Shareholder Meeting, with the reservation that for the purpose of establishing the obligations of the acquirers of significant blocks of shares provided for in the Act on public offering and in the Act on insurance activities, this restriction of voting rights shall be considered non-existent.

The above restriction of voting rights does not apply to:
- shareholders who on the date of passing the resolution of the Shareholder Meeting introducing the restriction had

rights under shares representing more than 10% of the total number of votes in the Company;
- shareholders acting with the shareholders referred to in point 1 on the basis of concluded agreements concerning the joint exercise of voting rights under shares.

Restriction concerning the transfer of ownership rights to securities

PZU's Articles of Association do not introduce any restrictions concerning the transfer of ownership rights to securities issued by the Company.

The principles for amending PZU's Articles of Association

Amending PZU's Articles of Association is one of the powers of the Shareholder Meeting and requires the adoption of a resolution by a three fourths majority, obtaining approval from the Polish Financial Supervision Authority (KNF) in the cases indicated in the Act on insurance activities and entry in the National Court Register. PZU's Articles of Association provide for the Supervisory Board's power to establish a consolidated amended text of the Company's Articles of Association.

Amendments to PZU's Articles of Association

On 1 June 2011, based on a State Treasury proposal, an Extraordinary Shareholder Meeting of PZU passed a resolution on amending PZU's Articles of Association and enacted all the amendments proposed by the shareholder.

The amendments to PZU's Articles of Association concerned the following issues:
- editorial changes concerning deleting from PZU's Articles of Association transitional provisions in the period of PZU's operations before and after entry onto the regulated market in order to increase the transparency of PZU's Articles of Association by resigning from provisions which became redundant when the actual status described therein came true;
- restricting the voting rights of shareholders, including the adoption of the principles for the accumulation and reduction of votes.
  Shareholders' voting rights have been restricted so that no shareholders at the Shareholder Meeting can have more than 10% of the total number of votes in PZU on the date of holding a Shareholder Meeting, with the reservation that for the purpose of establishing the obligations of the acquirers of significant blocks of shares provided for in the Act dated 29 July 2005 on public offering and the terms and conditions of introducing financial instruments to an organized trading system and on public companies (Journal of Laws, No. 185 of 2005, Item 1539 as amended) and in the Act on insurance activities, this restriction of voting rights shall be considered non-existent. For the purpose of restricting the voting rights, the votes of shareholders between whom there is a controlling or subsidiary relationship are added to one another. The restrictions do not apply to the State Treasury and shareholders acting with it based on concluded agreements concerning joint exercise of voting rights on shares. The restrictions of voting rights shall expire when the State Treasury's share in PZU's share capital drops below 5%.
- the procedure for appointing the Supervisory Board:
  – Members of the PZU Supervisory Board are appointed and dismissed by the Shareholder Meeting.
  – Until such time as the State Treasury's share in PZU's share capital drops below 20%, half of the Supervisory Board members are appointed by the Shareholder Meeting from among persons named by the State Treasury.
  – At the moment of the expiry of the State Treasury's right, it shall be acquired by a different shareholder representing the highest share in PZU's share capital if that shareholder holds at least 20% of the share capital.
  – Additionally, until the State Treasury ceases to be a shareholder in the Company, it has the right, in accordance with Art. 354 § 1 of the Commercial Companies Code, to appoint and dismiss one Supervisory Board member by virtue of a written statement submitted to the Company's Management Board. Such appointment or dismissal shall be effective from the moment of delivery of the relevant statement to the Management Board and shall not require a resolution to be passed by the Shareholder Meeting.

On 6 June 2011, in accordance with Art. 32 clause 2 points 4 and 7 of the Act on insurance activities, PZU applied to the Polish Financial Supervision Authority (KNF) for approval of the amendments to PZU's Articles of Association. On 28 June 2011, the Polish Financial Supervision Authority (KNF) issued a decision approving the amendments

The amendments to the Articles of Association came into force on the date of their entry by the registration court. On 17 October 2011, PZU received the court's decision concerning entering the amendments to PZU's Articles of Association in the National Court Register with effect from 6 October 2011.

The above amendments to the Articles of Association were dictated by the need to ensure the stabilization of PZU's position. They ensure stability to the exercise of voting rights to shares and thus discourage any actions leading to speculative trading in PZU's shares, especially such as might lead to short-term investment decisions. The amendments related to the principles for appointing the Supervisory Board are intended to ensure long-term stability of PZU's management and consistent execution of the adopted objectives.

These amendments prevent a strategic investor entering PZU.

On 8 February 2012 an Extraordinary Shareholder Meeting of PZU adopted resolution No. 3/2012 amending PZU's Articles of Association by way of adding item 11 to Article 18 and changing the wording of Article 25 clause 2 point 12 of the Articles of Association.

The changes to PZU's Articles of Association concern the powers of the Company's bodies with respect to approving the acquisition or sale of real property, perpetual usufruct right or share in real property or perpetual usufruct right.

Under Article 393 point 4 of the Commercial Companies Code, the acquisition or sale of real property, perpetual usufruct right or a share in real property or perpetual usufruct right requires consent of the shareholder meeting, unless the company's articles of association stipulate otherwise. PZU's Articles of Association specify the Supervisory Board's powers with respect to approving the acquisition or sale of real property, perpetual usufruct right or share in real property or perpetual usufruct right whose value exceeds Euro 3,000,000 (Article 25 clause 2 point 12 of the Articles of Association) and do not exclude such approvals from the Shareholder Meeting's powers. Therefore, any acquisition or sale of real property, perpetual usufruct right or a share in real property or perpetual usufruct right by PZU requires the approval of the Shareholder Meeting, irrespective of the value of the transaction. Moreover, if the value of the transaction exceeds Euro 3,000,000, such transaction requires additional approval from the Supervisory Board. PZU's Articles of Association, however, do not specify whether this amount includes VAT.

On 2 April 2012 the Company received the decision of the District Court for the Capital City of Warsaw in Warsaw, 12th Commercial Division of the National Court Register of 26 March 2012, by whose power the amendments to PZU SA's Articles of Association adopted by resolution no. 3/2012 of the Company's Ordinary Shareholder Meeting of 8 February 2012 were entered into the register of entrepreneurs on 27 March 2012. At the same time, as of the date of registering the amendments to the Articles of Association by the court of registration, the resolution adopted by the Company's Supervisory Board on 14 March 2012 on establishing the consolidated text of the Company's Articles of Association took binding force (The consolidated text of the Company's Articles of Association was published in current report no. 6/2012 of 15 March 2012).

The amendments in question intend to split powers in this respect between the competent PZU bodies and eliminate interpretation differences which may occur due to the fact that there no clear instructions specifying if the transaction amount includes VAT.

11. PZU'S SHARES ON THE WARSAW STOCK EXCHANGE

Highlights regarding PZU's shares

PZU made its debut on the Warsaw Stock Exchange on 12 May 2010. The Company's shares are continuously traded on the primary market. In 2011, the shares of PZU were included in the WIG, WIG20 and WIG Poland indices and from 1 February 2012 also in the RESPECT Index.

- IPO issue price – PLN 312.50 per share
- Opening price on the first day of trading on WSE – PLN 349.00
- Closing price on the first day of trading on WSE – PLN 360.00
- Average market price in 2011 – PLN 349.40
- (Gross) dividend paid during the financial year under distribution of profits for 2010 – PLN 26.00 per share
- WIG 20 Index – since 17 May 2010
- MSCI POLAND Index – since 27 May 2010
- RESPECT Index – since 1 February 2012

RESPECT Index

As of 1 February 2012 PZU's shares were incorporated in the RESPECT Index. PZU thereby joined 23 companies listed on the Warsaw Stock Exchange, which are governed in a responsible and sustainable manner in all areas while giving consideration to environmental, social and employee factors.

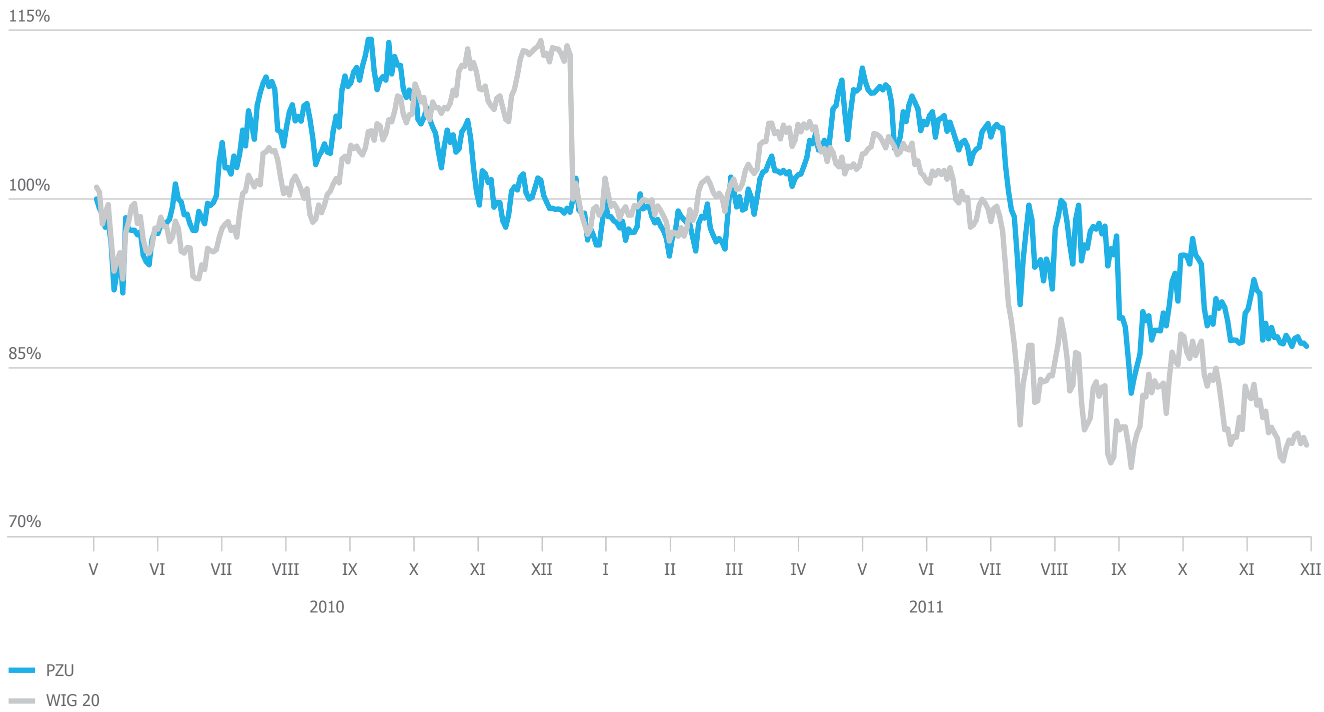
To be included in this index, companies must demonstrate good quality reporting, a high level of investor relations and the highest standards of information governance. These public companies always treat with integrity their reporting duties and investor relations and they undertake measures aiming at enhancing the transparency expected of public companies in compliance with the Best Practices of Companies Listed on the Warsaw Stock Exchange.

Ever more investors are currently guided by the principles for responsible investment (SRI) in their investment decisions. Socially-responsible investors give weight to aspects related to the environment, the public at large and corporate governance in their investment decisions.

The inclusion of PZU's shares in the RESPECT Index may enhance PZU's investment attractiveness and it does testify to the Company continually undertaking new measures confirming its high commitment to, and focus on, investors' needs.

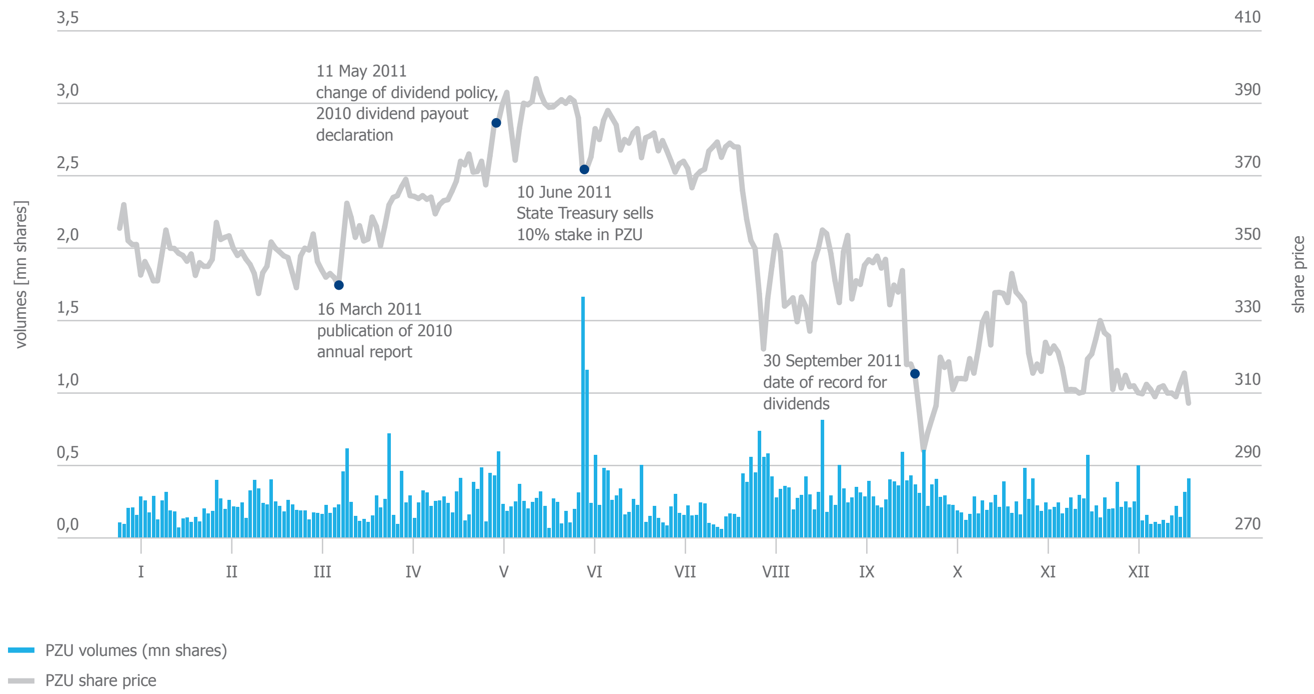
PZU's share price

PZU share price movement from the IPO on the WSE compared with the WIG20 index



12 May 2010 = 100%

PZU's share price in 2011



In 2011, the PZU share price was affected by not very optimistic factors shaping the situation on the WSE, and by global investor sentiments regarding the Eurozone and the Polish market. On the other hand, the decisions of investors interested in PZU's equities were affected by the State Treasury selling a 10% stake in PZU and the 2010 dividend payout.

The closing price of PZU shares on the last trading session in 2011 was PLN 309.00, which represented a 13.1% decrease compared with the price on the last day of December 2010 of PLN 355.50. At the same time, WIG20 and WIG indices had slumped 21.9% and 20.8% respectively. For the majority of 2011, PZU's share price lost less ground than the overall market.

In 2011, PZU shares closed 124 trading sessions declining, 122 trading sessions gaining, and 5 trading sessions unchanged. The highest closing price (PLN 396.80) was achieved on 25 May and the lowest (PLN 294.20) on 4 October. PZU's average market share price in 2011 was PLN 349.40 which was PLN 22.93 lower than in 2010. The average daily trading volume of PZU shares in 2011 was 265,862 shares, with the highest level (1,659,172 shares) recorded on 9 June 2011.

Capital market ratios

Capital market ratios for PZU as at	31 December 2011	31 December 2010
P / BV Market price of shares / book value per share	2.07	2.40
BVPS Book value per share	149.03	148.23
P / E Price / net earnings per share	11.38	12.59
EPS (PLN) Net earnings (loss) / number of shares	27.14	28.25
DY Dividend yield (%) Dividend per share / market price of shares	8.4%	3.1%
DPS (PLN) Dividend per share	26.00	10.91*
TSR Total shareholder return Market price of shares at the end of the period – market price of shares at the start of the period + dividend paid out in the period) / market price of shares at the start of the period	(5.8)%	17.3%**

* Excluding the dividend paid on 26 November 2009 as an interim dividend toward the dividend anticipated at the end of the 2009 financial year of PLN 12,749,917 thousand (PLN 147.69 per share).
** Total Shareholder Return = (market price of shares at the end of the period - market price of shares in the offering + dividend paid in the period) / market price of shares in the offering.

Recommendations concerning PZU's shares

In 2011 PZU was covered by 21 domestic and international financial institutions whose analysts issued a total of 49 recommendations concerning PZU's shares. The prevailing recommendations were „Buy", „Accumulate", „Overweigh" with a total of 31 recommendations; 17 recommendations were neutral („Hold" or „Neutral") and there was 1 „Underweight".

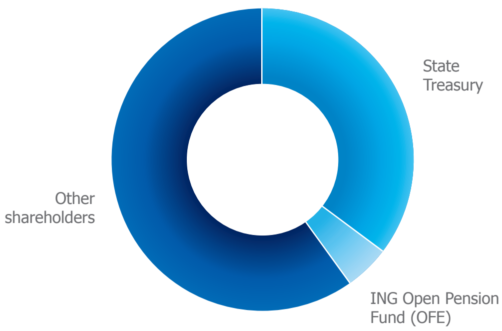
The institutions that analyze PZU's operations and results on an ongoing basis and make valuations and issue recommendations concerning the target share price are as follows:

- Barclays Capital
- Credit Suisse Securities
- Deutsche Bank AG
- Dom Inwestycyjny BRE Banku S.A.
- Dom Maklerski Banku Handlowego SA
- Erste Group Research
- Espirito Santo Investment Bank
- Goldman Sachs Global Investment Research
- HSBC Global Research
- ING Securities
- IPOPEMA Securities S.A.
- Jefferies International Limited
- J.P. Morgan Cazenove
- KBC Securities
- Millennium Dom Maklerski S.A.
- Morgan Stanley
- Silkroutefinancial
- Societe Generale
- Trigon Dom Maklerski
- UBS
- UniCredit

12. SHAREHOLDING STRUCTURE

Shareholders	31 December 2011		
	Number of shares	**% of share capital**	**% of votes at the Shareholder Meeting**
State Treasury	30,385,253	35.19%	35.19%
ING Open Pension Fund (ING OFE)	4,339,308	5.02%	5.02%
Other shareholders	51,627,739	59.79%	59.79%
Total	**86,352,300**	**100.00%**	**100.00%**

Shareholding structure



13. DIVIDEND

Dividend policy

On 11 May 2011, the PZU Management Board passed a resolution concerning PZU's dividend policy.

The adopted dividend policy provides for the following:
- The consolidated profit or loss of the PZU Group in accordance with IFRS shall be the basis for establishing the dividend to be paid out by PZU for a given financial year.
- The amount of the dividend:
  - shall not be lower than 50% or higher than 100% of the net profit shown in the consolidated IFRS financial statements;
  - shall not be higher than PZU's stand-alone net profit in accordance with PAS;
  - shall not result in reducing PZU's equity below the amount corresponding to 250% of the solvency margin;
  - shall not result in reducing the PZU Group's financial strength below a level corresponding to the AA rating according to Standard & Poor's methodology;
  - should take into account PZU's additional capital requirements in a 12-month perspective from the moment of approving the PZU Group's consolidated financial statements for a given year by the PZU Management Board.
- The equity and solvency margin are calculated in accordance with the prudence norms established for the Polish insurance market.

The resolution on the dividend policy is binding from the date of coming into force of the articles referred to in Art. 311 of the Directive 2009/138/EC of the European Parliament and Council of 25 November 2009 on the taking-up and pursuit of the business of Insurance and Reinsurance (Solvency II).

Distribution of profit for the 2010 financial year

On 11 May 2011, the PZU Management Board passed a resolution to accept a motion concerning the distribution of PZU's net profit for the year ended 31 December 2010 of PLN 3,516,709 thousand as follows:
- PLN 2,245,160 thousand for payment of dividend to shareholders;
- PLN 1,271,549 thousand to supplementary capital.

On 30 June 2011, PZU's Annual Shareholder Meeting passed resolution no. 7/2011 concerning the distribution of PZU's net profit for the financial year ended 31 December 2010 according to which PLN 2,245,160 thousand, i.e. PLN 26.00 per share was earmarked for payment of dividend. In accordance with the above-mentioned resolution, 30 September 2011 was the record date when the list of shareholders entitled to payment of dividend for the financial year ended 31 December 2010 was established, and 21 October 2011 was the date of payment of the said dividend.

On 12 April 2012 the PZU Management Board adopted a resolution accepting the motion to distribute PZU's net profit for 2011 in the amount of PLN 2,582,302,727.40 in the following manner:
- designate for a dividend payout PLN 1,752,951,690.00 i.e. PLN 20.30 per share;
- designate for reserve capital PLN 819,351,037.40;
- designate as a charge to the Company Social Benefits Fund PLN 10,000,000.00.

The Management Board resolved to submit the foregoing motion to the Shareholder Meeting and a request to the PZU Supervisory Board to evaluate this motion.

As of the date of preparing this annual report of the PZU Group, the PZU Shareholder Meeting has not adopted the relevant resolution on the distribution of profit in 2011.

14. INVESTOR RELATIONS

Endeavoring to meet the highest standards of information governance in public companies the PZU Management undertakes measures aimed at enhancing the Company's transparency by addressing the information needs of various stakeholder groups.

The overriding objective of investor relations (IR) in PZU is to create PZU's value at the level of communication with capital market participants with whom the Company wants to build long-term relations. In 2011 the fundamental task of IR was to provide transparent information about the Company's operations and results, mold the Company's positive image among its investors and analysts and build confidence in PZU among capital market participants.

The Management Board Office is responsible for organizing and conducting investor relations at PZU discharging statutorily-required reporting duties as a securities issuer, for organizing Shareholder Meetings and for coordinating the dividend distribution. Investor relations activities entail not just obligatory actions stemming directly from legal regulations. The Company takes measures addressed and customized to the information needs of specific groups of capital market participants. These measures are taken by the Investor Relations Team of the PZU Management Board Office. The employees of this Team maintain ongoing contact with the analysts of investment banks, brokerage houses and Polish and global institutional investors; they are also at the disposal of individual investors and respond to numerous inquiries posed by telephone and e-mail.

In 2011 PZU's financial results were presented and discussed after every quarter by the Company's Management Board at meetings with capital market analysts. All these meetings, like Shareholder Meetings, were aired live via webcasts. In 2011 representatives of the Company's Management Board and the Investors Relations Team of the PZU Management Board Office participated in two road shows in Europe and the United States organized after publication of annual and interim results, in 9 financial conferences abroad with the participation of global investors and 1 conference in Poland as well as in numerous group meetings, one-on-one meetings and conference calls with equity portfolio fund managers in the Company's registered offices. In 2011 more than 180 meetings were held in total with more than 300 institutional investors and more than 100 meetings were held with analysts who give recommendations concerning PZU's shares.

Communication measures targeting individual investors were also undertaken. PZU representatives took part in the WallStreet conference in Zakopane organized by the Association of Individual Investors (SII). This is the largest meeting of individual investors in Central and Eastern Europe. After publishing the interim results for 1H 2011 PZU representatives met with individual investors at Investors' Day on the Stock Exchange. In 2012 forms and tools of communicating with individual investors will be developed. After publishing the 2011 annual results a chat with a PZU Management Board Member was held with individual investors. The Company also participates in the program entitled „10 of 10 – Communicate Effectively", which is a proprietary program of the Association of Individual Investors whose purpose is to create high standards in communication between public companies and individual investors.

In 2010 an initiative was launched to create a modern IR web service in compliance with the best global practices enabling interested investors to obtain the necessary information about the Company in a convenient manner. This service is constantly being expanded to include new information and functionalities in order to satisfy the information needs of investors and analysts as best as possible.

In 2012 further work will be conducted to develop tools for communicating with capital market participants in the framework of ongoing investor relations.

15. RATING

PZU and PZU Życie are rated by rating agencies on a regular basis. The rating awarded to PZU and PZU Życie is an evaluation following from analysis of financial data, competitive position, management and corporate strategy. The rating also includes a rating outlook, i.e. the future assessment of the company's position if specific circumstances arise.

As at the date of this Annual Report, both PZU Group companies had a long-term credit rating and a financial strength rating (awarded by Standard & Poor's Ratings Services on 16 July 2009) of A with a stable outlook. On 22 July 2011 Standard & Poor's Ratings Services upheld the above rating.

The table below shows the ratings granted to PZU and PZU Życie by Standard&Poor's with the ratings awarded a year earlier.

Rating

Name	Rating and outlook	Date of update	Previous rating and outlook	Date of previous update
PZU				
Financial strength rating	A /stable/	22 July 2011	A /stable/	5 July 2010
Credit rating	A /stable/	22 July 2011	A /stable/	5 July 2010
PZU Życie				
Financial strength rating	A /stable/	22 July 2011	A /stable/	5 July 2010
Credit rating	A /stable/	22 July 2011	A /stable/	5 July 2010

16. RISK MANAGEMENT

Risk management policy

The risk management system implemented by the PZU Group is directed at risk control and at maintaining an appropriate capitalization level. Through identifying, analyzing, measuring, controlling, managing and reporting the risk related to the operating activities conducted, the PZU Group is able to discharge its obligations toward clients and business partners and fulfill the requirements arising from the provisions of the law and external regulations.

Risk management in the PZU Group is based on the following main principles:

- Taking controlled risk – financial strength and constant value growth are an integral part of the PZU Group's business strategy. In order to achieve these objectives the PZU Group conducts operations in accordance with a clearly defined risk policy and within the established risk limits;
- Clearly defined responsibilities – the PZU Group operates in line with the principle of allocating tasks, competencies and responsibilities. The delegated employees are responsible for the risk they undertake, and their incentives are harmonized with the business objectives of the PZU Group;
- Adapting to changes occurring in the business environment – the ability to respond to changes occurring in the business environment, both those arising from external and internal conditions of the PZU Group, are an integral part of the risk control process in the PZU Group.

PZU and PZU Życie manage insurance risk by applying the following tools:

- calculating and monitoring the adequacy of technical reserves;
- tariff strategy and monitoring current estimates and assessing the adequacy of premium;
- reinsurance.

Sensitivity to risk

Sensitivity of the asset portfolio

PLN million

Sensitivity of the asset portfolio	Change in the risk factor	31 December 2011		31 December 2010	
		Effect on net profit/loss	Effect on equity	Effect on net profit/loss	Effect on equity
Interest rate risk	drop by 100 bp	135	281	156	299
	growth by 100 bp	(126)	(264)	(149)	(283)
Currency risk	increase by 20%	232	232	167	167
	decrease by 20%	(232)	(232)	(167)	(167)
Price risk of equity instruments	increase by 20%	254	336	283	416
	decrease by 20%	(254)	(336)	(283)	(416)

The table above summarizes the results of the analysis of the sensitivity of net profit and equity on changes in interest rate risk, currency risk and price risk of equity instruments. The analysis does not take into account the effect on net profit and equity of changes in investment measurement, which are taken into account when calculating the amount of provisions.

The decrease in sensitivity to interest rate risk as at the end of 2011 compared with the end of 2010 was due to the increased share of instruments measured at amortized cost in the portfolio.

Financial assets exposed to currency risk include deposit transactions and debt securities constituting security of the realization of expenses in respect of technical reserves denominated in foreign currencies, and exposure in equity instruments listed on stock exchanges other than the WSE, exposures to derivatives denominated in foreign currencies and financial assets of consolidated insurance companies in Lithuania and the Ukraine. The increase in sensitivity to currency risk at the end of 2011 compared with 2010 is mainly due to the increased exposure in deposits denominated in foreign currencies and the increase in foreign exchange rates.

The decrease in sensitivity of the financial assets portfolio to changes in the valuation of listed equity instruments at the end of 2011 compared with 2010 results from the lower exposure to equity instruments exposed to other price risk.

Stress tests

In connection with the obligation placed on insurance companies by the Polish Financial Supervision Authority, PZU and PZU Życie carried out stress tests relating to the financial data reported as of 31 December 2010, in line with the guidance obtained from the Polish Financial Supervision Authority and submitted the test results by the 31 July 2011 deadline. Additionally, the PZU Group participated in the European Stress Tests for the insurance sector carried out by EIOPA, whose results were submitted to the Polish Financial Supervision Authority (KNF). The stress tests showed that the PZU Group has sufficient capital to be able to continue its operations safely after strong turbulence in the business environment has abated.

17. REINSURANCE

Reinsurance activity of the PZU Group Companies in 2011

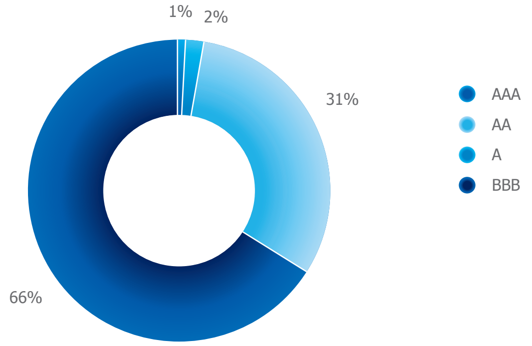
In 2011 the PZU Group's reinsurance cover is a safeguard for its insurance activity, curtailing the effects of catastrophic phenomena, which could adversely affect the financial position of insurance undertakings. This task is achieved using obligatory reinsurance treaties additionally coupled with facultative reinsurance.

Reinsurance treaties – PZU

On the basis of its reinsurance treaties PZU limits its risk, among others through a non-proportional excess of loss treaty protecting PZU's portfolio against catastrophic claims (e.g. flooding, hurricane), non-proportional excess of loss treaties protecting its portfolios of property insurance, technical insurance, marine insurance, aviation insurance, third person liability insurance and motor third person liability insurance against the effects of high individual claims. PZU's risk is also limited through a proportional treaty protecting its financial insurance portfolio.

The following reinsurers were the main partners providing obligatory reinsurance cover to PZU in 2011: Swiss Re, Hannover Re, Scor, Munich Re and Lloyd's. PZU's reinsurance partners hold high-grade investment ratings according to S&P, which affords the Company certainty of a reinsurer's good financial position.

Reinsurance premium under obligatory treaties in 2011 according to Standard & Poor's rating



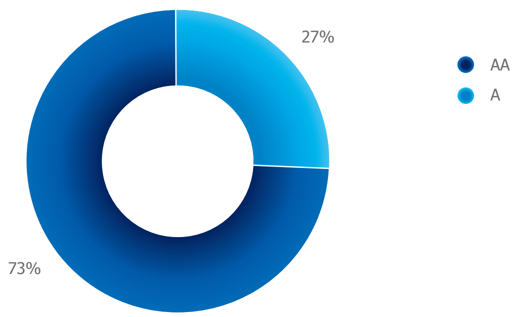
PZU's inward reinsurance activity is one of the elements of support provided to PZU Lietuva and PZU Ukraine. The Company participates in the obligatory and facultative reinsurance treaties of these companies. Moreover, PZU generates a gross reinsurance premium on inward reinsurance through its operations on domestic and international markets, primarily through facultative reinsurance.

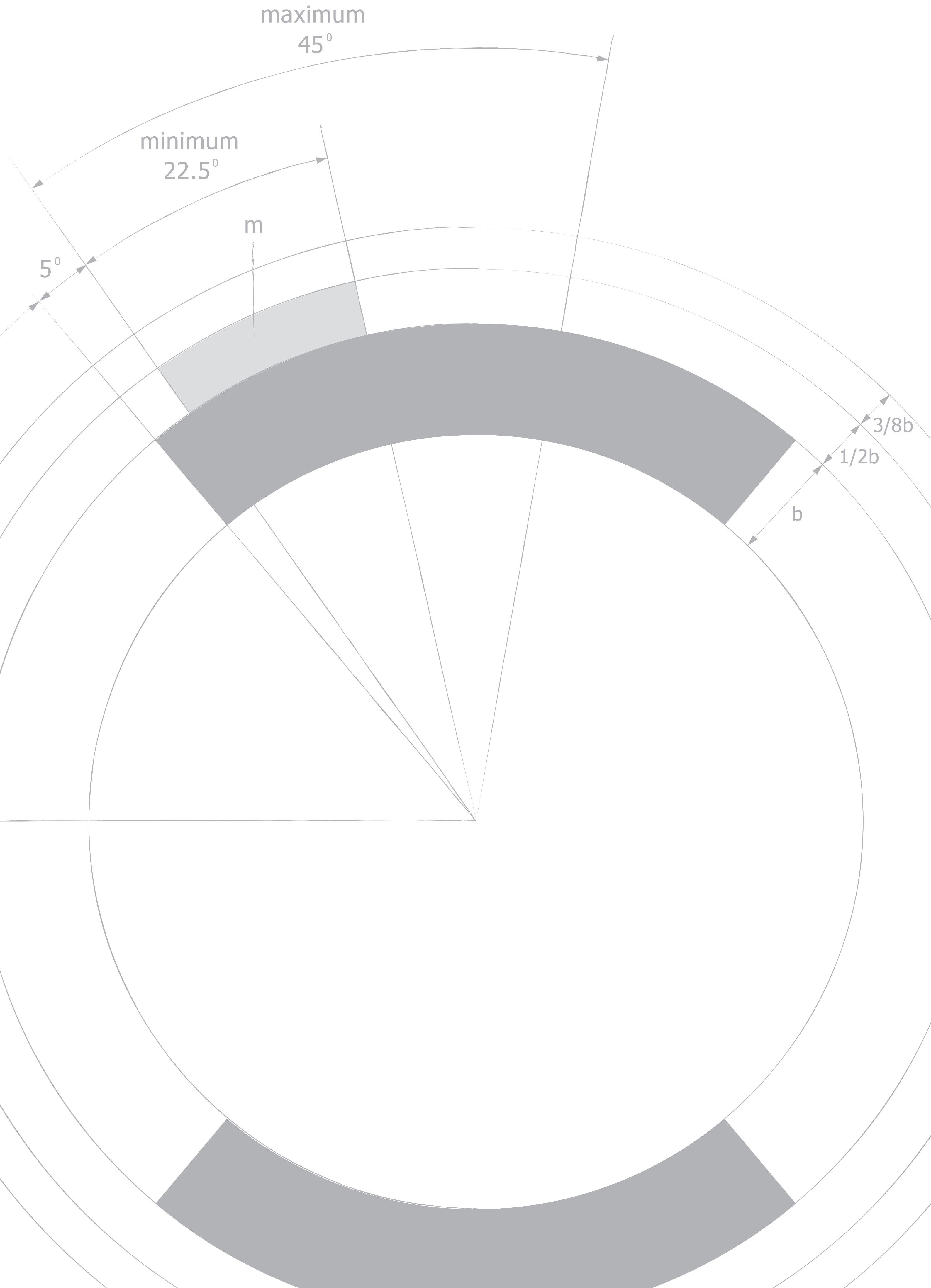
Reinsurance treaties – PZU Życie

Through its outward reinsurance treaties PZU Życie protects its portfolio against risk accumulation (catastrophic treaty), it protects individual policies with higher sums insured and it protects its children's critical illness group insurance portfolio.

The following reinsurers partner with PZU Życie to provide it reinsurance cover: RGA, Gen Re, Arch Re and Lloyd's. Reinsurance partners have high investment-grade ratings according to S&P, which affords the Company certainty of a reinsurer's good financial position.

Reinsurance premium in 2011 according to Standard & Poor's rating





maximum
45⁰
minimum
22.5⁰
m
5⁰
3/8b
1/2b
b

18. PURSUING THE STRATEGY AND DEVELOPMENT PROJECTS

Projects conducted in the previous year were directly related to the pursuit of the PZU Group strategy for the years 2009-2011 aimed at profitable growth and constructing a cost-effective organization aimed at satisfying client requirements.

In respect of profitable growth, the following actions were pursued

- a process for implementing a chain of modern outlets was launched according to the physical presence model developed in 2010 - clearly visible shared PZU Group and sales-focused branches;
- work was completed on revitalizing the corporate property insurance sales area aimed at improving the competencies of sales teams and optimizing their geographic location;
- a tool was implemented to enable deeper segmentation of clients, which will be used for cross-selling campaigns (analytical CRM enabling the creation of a standardized PZU client database).
- analytical work was started on the concept for developing healthcare-related business, including preparations for the potential reform of public health insurance.

Under actions aimed at building an effective organization, focused on satisfying client needs - in respect of claims handling and claims paid – the following project activities were pursued:

- a new model for cooperation with certifying physicians and simplified and remote accidental claims handling procedures were implemented;
- the „automatic payment" („autowypłata") process in respect of benefits was launched in PZU Życie;
- work was carried out related to expansion of Internet services in the area of claims and benefits – among other things, an application for Internet reporting of the claims for English speaking clients was launched (an innovation on the Polish market);
- a pilot program for directing clients to respective repair shops in a repair shop chain was conducted;
- work was carried out on creating a centralized model for managing the process of renting replacement vehicles during repairs;
- under the process of developing the PZU Assistance concept an auction platform was developed PZU Pomoc Online (trading salvaged vehicles on total loss vehicles), and as part of building brand awareness, replacement cars used by clients under door-to-door services were appropriately marked.

In customer service, apart from the project mentioned above related to the construction of a chain of modern outlets, the following activities were pursued:

- 110 PZU branches were marked according to a unified standard, so as to improve their visibility and facilitate clients finding the outlet;
- the process of unifying management structures in the current PZU Group outlets and of front-office employees was continued to enable comprehensive servicing of life and non-life clients in all outlets;
- IT tools were implemented to support office processes and handling correspondence from all channels and moreover a Central Office was opened which provides services to all PZU Group companies[1)];
- the functionality for servicing PZU Życie group insurance clients was expanded to include upselling or cross-selling other PZU products to clients, and sales network training was conducted - this will enable using the cross-selling potential of Group products.

Additionally, apart from the activities listed above, in 2011 several initiatives were conducted in the PZU Group aimed at improving process efficiency and cost optimization. They included, among others:

- a further stage of headcount restructuring as a result of which headcount dropped by approximately 1,050 full-time positions;
- analytical work on a project aimed at developing PZU's operating model and as a result the PZU policy system will be replaced;
- stage 1 of joint implementation of the PZU and PZU Życie

[1)] This does not concern the Armatura Capital Group companies.

ERP class system - in 2011 unified processes in financial accounting, procurement and a joint chart of accounts were implemented (start-up in 16 January 2012);
- starting analytical work related to the process of restructuring the real property portfolio necessary from the perspective of PZU's and PZU Życie's statutory operations;
- creating the HR and compensation service center for contractors and intermediaries of PZU and PZU Życie, by the end of 2011 the servicing of all the branches of both companies was taken over;
- launching the process of automatic policy population issued in the sales system to the policy administration system;
- further optimization of the costs of the functioning of the operational back-office;
- centralization and automation of claims and annuities payment process was conducted;
- continuing projects in progress related to the unification and centralization of the IT systems and IT servicing of the PZU Group in other areas, i.e. the Service Desk, user authentication systems, e-mail system and the data warehouse.

19. PZU'S OPERATIONS IN 2011

Sales

PZU offers a wide scope of non-life insurance products, in particular motor, personal, agricultural and general liability insurance. As at the end of 2011, PZU offered over 200 insurance products. Motor insurance is the most important group of products offered by PZU, both in terms of the number of binding insurance contracts and the percentage of written premium in PZU's total gross written premium.

In 2011 PZU's activities concentrated mainly on improving returns on the corporate insurance portfolio and proactive sales of insurance to mass clients.

Products – mass client

- In 2011 motor insurance tariffs for individual clients and SMEs changed several times to adjust them to market conditions, and specifically to growing claims.
- Introducing the Premium Security Option in motor insurance is a new option in PZU. Clients who buy this additional option to motor own damage and third party liability insurance will retain the bonus-malus deduction if an insured event occurs.
- Tools for quoting and servicing fleet insurance of small and medium enterprises were developed.
- Tools enabling verification of the declaration of the insurance history were implemented (submitted by new clients upon underwriting motor TPL or motor own damage insurance contract) using data provided by the Information Center of the Insurance Guarantee Fund.
- In respect of property insurance a new version of home insurance was implemented PZU DOM and PZU DOM Plus, covering among other things PZU Pomoc w domu (help at home) insurance. The prices of home insurance were also adjusted to incorporate the flood risk in particular parts of the country, and at the same time an option to eliminate flood cover from the standard insurance contract was eliminated.
- The basic offer for SME clients was modified – the PZU Doradca (advisor) package. These changes aimed at extending the availability of the product to all SME clients and improving the profitability of insurance. Depending on client needs, insurance may be expanded to include assistance services and insurance of risks specific to a given business (such as the PZU HOTEL clause addressing clients in the hospitality industry).
- Due to the high loss ratio in compulsory subsidized crop insurance, in the autumn of 2011, changes were made to this insurance offer to improve profitability.
- In accordance with amendments to legislation (package of health acts) a new offer was prepared for compulsory and voluntary insurance for healthcare facilities. Modifications to the insurance of payers of public benefits were introduced and the option to insure other professional groups was introduced in respect of financial losses arising in connection with performing the function.
- In accidental insurance PZU Pomoc w Podróży (travel assistance) was added to the offer, covering insurance of the costs of treatment and assistance for people travelling in Poland and abroad. Special insurance for Euro 2012 Football Cup fans was also created, offered with Polish Pass cards.

Products – corporate client

- In accordance with the adopted strategy, PZU continued actions to continue improving the profitability of motor insurance (own damage and TPL), among others through changing tariffs and modifying the general insurance terms and conditions for motor own damage insurance of corporate clients. The measures previously taken produced a noticeable and significant improvement in technical results.
- In non-life insurance as part of the activities related to improving profitability and portfolio quality, the essential role of underwriting was maintained through:
  - further limitation of sales to entities from high loss ratio industries;

- improving the efficiency of the selection process, classification and risk assessment (including flood risk);
- wider application of additional clauses and other technical insurance restrictions changing the scope of insurance.

- In general liability insurance, new risk assessment tools were applied and changes were introduced to the terms and conditions of insurance and quotation principles.

Products – financial insurance

- In 2011 two new products were added to the offer:
  - performance bond for removing and adjusting negative effects on the environment and environmental damage (referred to as an environmental performance bond);
  - an insurance guarantee for the user contract in respect of accounts with deferred payments (referred to as an e-toll guarantee).
- In respect of insuring monetary receivables and bank loans, a policy was pursued aimed at securing the portfolio held and earning a technical profit. This was realized by using restrictive risk assessment criteria, hedging the transactions concluded and maintaining safe legal regulations in the contracts concluded.

Products – bancassurance

- In 2011 cooperation was continued with its current Partners – leading banks on the Polish market – such as PKO BP SA, ING Bank Śląski SA, Bank Millennium SA and BGŻ SA. The offer was supplemented by new insurance being added to banking products, such as protection programs for payment cards and insurance of buildings and apartments added to mortgage loans and advances.
- Cooperation was continued and relations were established with partners with large client bases or partners handling mass payments such as telecoms, power companies and commercial chains. It comprised several new, specialized insurance products such as mobile phone and notebook insurance, insurance of loan repayment in case of unemployment.

Sales network

The organization of PZU's sales network aims at maintaining high sales effectiveness while simultaneously ensuring high quality services. This is achieved by organizing sales in two dimensions:
- division by distribution channels;
- client segmentation.

As at 31 December 2011, PZU offered products in the following distribution channels:
- tied agents – PZU's own agent network:
  - office agents (347; sales-support agents in PZU's own outlets);
  - agents operating locally exclusively on a mobile basis (5,686)[1];
  - Group Agencies (6; pilot program – agents managing stationary outlets);
- multiagencies – agents cooperating with several insurance companies (2,215)[2];
- insurance brokers (approximately 800);
- bancassurance – sales via banks and other partners for whom insurance sales are an auxiliary activity;
- direct – telephone and web-based sales;
- PZU employees – sales in own outlets (470 people).

General terms and conditions of insurance

The general terms and conditions of insurance are available on PZU's website (www.pzu.pl) and in PZU's outlets. In accordance with the Act on insurance activities, the general terms and conditions of insurance should be delivered to the policyholder before an insurance contract is concluded.

In accordance with the PZU Management Board's Regulations, tariffs for compulsory and voluntary insurance are passed in the form of a resolution.

Insurance contracts exceeding 25% of PZU's total technical provisions and equity

During the 12 months ended 31 December 2011, PZU did not conclude any insurance contracts for a sum of one net risk insured exceeding 25% of the total amount of technical reserves and equity.

Claims handling

In 2011 as part of the process of improving motor claims handling effectiveness, the following actions were taken:
- development of a Claims Communication Platform to provide full electronic communication with the PZU Repair Network's workshops through PZU's claims handling IT system;
- implementation of a procedure for simplified motor claims handling;
- cooperation with ControlExpert in respect of automating the verification of the motor claims valuation process;
- pilot rollout of a solution to improve management of PZU's Repair Network;
- launch of a telephone service „Proposed Vehicle Sales" in respect of partial damage to vehicles in motor TPL insurance;
- centralization of the process for renting replacement cars for motor TPL claims;
- launch of an auction platform to trade salvaged vehicle in total losses.

[1] Including dealers cooperating with PZU on the basis of exclusive contracts (182).

[2] Including dealers cooperating with PZU on the basis of multiagency contracts (964).

The following changes took place in respect of property claims handling in 2011:

- electronic claims document workflow was introduced;
- the claims handling system (SLS) was integrated with the expert claims valuation systems in buildings;
- a simplified system for valuing claims in buildings was implemented;
- new tools were used for property claims handling (among other things, Mini Mobile PZU Assistance Office).

In the area of casualty claims handling, the following actions were conducted:

- a new model for cooperation with certifying physicians was implemented – four entities providing medical services for the purpose of certifying claims in motor TPL and accidental insurance were selected and cooperation commenced;
- a program for mental rehabilitation groups for children injured in motor accidents was implemented (under cooperation with Dom Misia Ratownika);
- a system automating payment of annuities was implemented.

20. PZU ŻYCIE'S OPERATIONS IN 2011

Sales

PZU Życie offers a wide scope of life insurance products, and specifically group protection insurance, individual insurance and insurance offered in cooperation with banks. Group protection insurance constitute the most important group of products in terms of the percentage of gross written premium in the total gross written premium in PZU Życie.

Products – group insurance

In 2011, in the area of group insurance work was conducted related to the re-tariffication of group insurance, whose effects were implemented as of 1 January 2012:

- new tariffication levels will enable more price flexibility in offers and systemize discounts and the variability of commissions;
- new additional group insurance with rights to individual continuation of insurance and three types of continuation guarantees differentiated by premium for the right to continue in the group phase and in the continuation phase;
- changes in the offer for P Plus group employee insurance dedicated to the SME sector PZU Ochrona Plus (among other things: adding to the additional insurance offer a guarantee of continuation in all protection packages).

The Company also emphasized the need to develop the PZU Club „Pomoc w Życiu" (help in life), which as at the end of 2011 had 2 million members. At the same time PZU Życie continued work on expanding its offer for club members.

In 2011 PZU Życie continued to participate in the submission of tender offers for group insurance. In connection with the duty of applying the requirements resulting from the Act on Public Procurement to submitting orders for insurance services, there has been a visible increase in the number of public employers who have decided to apply tender procedures.

In 1 January 2012 in continued group and individual insurance with Karta Apteczna (Pharmacy Card) the general terms and conditions of insurance – „OWU" – and the Regulations were adapted to the amendments made to the Act of 6 September 2001 Pharmaceutical Law (Journal of Laws, No. 126 of 2001, Item 1381, as amended).

Products – individual insurance

In connection with the new legal regulations introducing the additional possibility of saving funds for retirement with financial relief, in 2011 PZU Życie conducted work on launching a new product – an individual retirement security account (Indywidualne Konto Zabezpieczenia Emerytalnego - „IKZE"). As a result, as of 2 January 2012, this product was launched to target current clients and prospectives. One uncontested benefit it offers is the current year tax relief afforded by deducting the premium from taxable income. The Individual Retirement Account (IKE) will still be offered in addition to IKZE.

In 2011 the sales of Plan na Życie insurance were continued, offering the possibility of investing and saving in unit-linked insurance which enjoys enormous client interest. Under the „Plan na Życie" product clients may regularly invest money in investment funds or may use model funds and additionally set protection at a selected level – which gives extensive freedom in managing a contract.

In 2011, in connection with the continued interest in structured products observed on the market, PZU Życie's objective is to maintain these products' presence on the market. Through „Świat Zysków" insurance PZU Życie offers its clients products that are an alternative or supplementary to other investment products. In 2011 six consecutive successful subscriptions of the product with different investment strategies were conducted. The insurance is still in the offer and in 2012 further subscriptions are planned. To adapt the investment strategies proposed as part of the product better to changing economic conditions and client needs, it was decided to increase the number of subscriptions and shorten their duration.

In January 2011, a new product was launched which expanded the protection offer of PZU Życie, under the name „PZU Ochrona Rodziny" (family protection). This insurance targets current clients who have unit-linked insurance, fixed term insurance and „Plan na Życie" insurance. The contract is constructed so as to ensure wide accident protection. Insurance also provides the possibility of giving coverage in a single agreement not just to the insured but to members of his or her closest family members, i.e. spouse and children, which greatly enhances its attractiveness. This product is supported by the service model for the Company's current customers as implemented in the agency network structures.

Products – individual insurance for the banking channel

In 2011 the product offer was further developed under cooperation with current business partners and new banks.

In connection with the observed volatility on the financial markets, investment products with attractive potential returns and full capital protection gained interest, mainly structured insurance. The offer of products distributed jointly with current partners was expanded. A new type of product was introduced in Bank Handlowy w Warszawie SA under consecutive subscriptions to structured insurance – autocall. In Bank Millennium SA a new, multicurrency unit-linked product was introduced, under which modern model funds and a guarantee fund were launched.

Single-premium endowment insurance garnered the largest share in written premium. In accordance with the adopted strategy, the possibility of offering this type of product depends on the scope of cooperation with a given partner in other product lines.

In protection insurance, cooperation with PKO BP SA was expanded by life insurance for mortgage loan borrowers. In other protection products, the Group concentrated on maintaining and developing the current insurance portfolio and on work related to the planned implementation of insurance for consumer finance and mortgage banking clients.

Products – health insurance

In 2011 the product offer in health insurance underwent further development, concentrating on group products targeting non-standard offers for corporate clients.
In Q3 2011 the group insurance offer was expanded to include products based on a „fee for service" model with a new medical service provider PZU Pomoc SA. Also in the second half of 2011, under the Healthcare (Opieka Medyczna) product line, a pilot comprehensive health insurance program was adopted in respect of refunding drugs, organized in cooperation with the Polish Pharmaceutical Group (Polska Grupa Farmaceutyczna).

Sales network

The Company engages in sales of insurance both via its proprietary network and an agency network. Additionally, distribution channels, which are modern and popular on the Polish market, are used such as the banking channel or direct mailing. The key distribution channels are as follows:

- corporate sales – employees of PZU Życie, whose fundamental task is to sell and maintain the group insurance portfolio;
- agency sales – a network of approximately 2.3 thousand exclusive agents and 181 Sales Team Managers, whose actions are aimed at selling group and individual insurance and maintaining and servicing the individual insurance portfolio;
- a network of proprietary outlets – a network of joint PZU and PZU Życie outlets, which apart from service functions also serve sales functions, in particular in individual insurance (including individually continued cover);
- direct sales – a distribution channel used to acquire individually continued insurance clients (including up-selling additional insurance);
- the banking channel – a network of banks in cooperation with which the Company distributes a wide range of investment and protection products.

General terms and conditions of insurance

The general terms and conditions of insurance are available on the PZU website (www.pzu.pl) and in PZU's various customer service points. In accordance with the Act on insurance activities, the general terms and conditions of insurance should be delivered to the policyholder before an insurance contract is concluded.

In accordance with the Regulations of the PZU Życie Management Board, tariffs for compulsory and voluntary insurance and general terms and conditions of insurance are passed in the form of a resolution.

Claims handling

In 2011, under the process of improving claims handling, the following actions were taken:

- a new claims handling system was implemented in further product groups (bank, individual protection, investment, other group protection and individually continued)

and exclusion from the use of the „old” distributed system of claims handling system;
- a new model of cooperation with certifying physicians was implemented – four entities providing medical services for the purpose of certifying benefit claims were selected and cooperation with them commenced;
- a new form of benefit payments was launched – Autowypłata;
- „old portfolio” benefit administration was centralized;
- paper applications were completely eliminated.

21. PTE PZU'S OPERATIONS OF PTE PZU IN 2011

The key initiative realized in the Company in 2011 was the IKZE project. As a result of statutory changes, universal pension fund management companies were included in the entities authorized to maintain individual retirement security accounts (IKZE) and offering respective financial services to clients, related to saving for future retirement as of 1 January 2012. Respective operations are conducted via the PZU Voluntary Pension Fund established by PTE PZU. PTE PZU was one of the first entities on the market was allowed to engage in these activities by the Polish Financial Supervision Authority (KNF) (decision of 22 November 2011 granting permission to establish Dobrowolny Fundusz Emerytalny PZU), thus approving the Articles of Association. The fund managed by PTE PZU was – as the first entity in this segment – entered in the Fund Register on 12 January 2012, thus having the possibility of commencing operations. The new product offered by PTE PZU under the 3rd pension insurance pillar enables those who make payments to IKZE to obtain personal income tax relief up to the amount of an annual limit specified by the regulator.

Acting in the interests of OFE PZU members, the Management Board of PTE PZU decided to change its custodian bank, to ING Bank Śląski SA, which on 18 November 2011 obtained a permit from the Polish Financial Supervision Authority. The first day on which ING Bank Śląski SA performed this function was 14 January 2012. The change – while maintaining the former standards of services and security of the funds entrusted by members of OFE PZU - will make it possible to cut significantly the fees paid to the Custodian for safekeeping OFE PZU assets.

22. KEY MARKETING ACTIVITIES

Advertising, media and the Internet

In 2011 the PZU Group conducted eight national advertising campaigns:

- in February and March a campaign was conducted on the fixed sum insured and door-to-door services, to build the perception of PZU's wide and comprehensive motor insurance offering;
- at the turn of May and June the „Young drivers" campaign was conducted in which PZU's offer addressed to drivers under 26 years of age was presented;
- in August and September the „PZU assistance at home" campaign was conducted to promote the PZU home insurance offer;
- in October and November the e-szkoda (e-claim) campaign was conducted to provide information on the possibility of complete claims handling via the Internet;
- in December the „ochrona zniżek" [deduction protection] campaign was carried out to present PZU's motor insurance offering;
- at the turn of February and March and of October and November two investment and protection campaigns were conducted in respect of insurance offered by PZU Życie, to bolster PZU brand awareness as a brand competent in savings and investments;
- at the turn of February and March and in October, group insurance campaigns were conducted to illustrate the option of insureds participating in the PZU Pomoc Club in work establishments.

All these campaigns were conducted on TV and in the Internet, and in selected media other than TV (such as radio and the press).

Marketing sales support

In 2011, PZU and PZU Życie's activities in sales support were focused mainly on the mass product segment. Apart from activities consisting of preparing advertising banners and leaflets the following were conducted:

- a test mini loyalty program for PZU clients purchasing motor TPL and own damage insurance as a bundle– thanks to this program clients may also make use of the Niezguba service (lost car keys are returned to the owner), and an additional assistance bundle and discount program;
- enhancing standard mass mailing sent to clients with marketing communication (e.g. in the form of the newspaper Moje PZU and Moje PZU Dobry Rolnik, or leaflets informing clients how a submitted claim may be easily monitored);
- issuing PZU Business Club cards – a program directed to corporate clients of PZU and PZU Życie;
- marking the best PZU EU branches to improve awareness of the location of branches among potential clients.

23. KEY HR ACTIVITIES

Restructuring process in PZU and PZU Życie

On 29 December 2009 the PZU and PZU Życie Management Boards announced a plan for implementing a restructuring program for the years 2010-2012.

The headcount restructuring process in 2011 was a continuation of the activities launched in 2010 and consisted of ongoing integration of teams carrying out similar tasks in PZU and PZU Życie, implementing IT tools and optimizing processes to grow productivity standards (ratios), and centralize some functions in organizational entities further.

The headcount restructuring processes in 2011 mainly covered the following areas: transactions, finance, administration, HR and payroll, claims handling and benefits, and the network, in all areas, in local and regional branches, in specialized units and in the PZU and PZU Życie Head Office.

Having regard for the extent of change on 11 May 2011 the Management Boards of PZU and PZU Życie adopted a resolution on the intention of conducting mass layoffs in 2011.
On 26 May 2011 an agreement was executed on mass layoffs between PZU and PZU Życie and the trade unions operating in these Companies. Accordingly, in the period from 13 June to 10 October 2011 the headcount restructuring and optimization process entailing mass layoffs was conducted.

In 2011 a maximum of 3,303 PZU and PZU Życie employees were to be affected by this program including net layoffs, this meant that the intended decrease in the number of employees was 1,199 people.

The people who were laid off or who did not accept the proposed change in the terms and conditions of employment were offered favorable terms of resignation, better than those offered in accordance with the law in similar situations [the Act of 13 March 2003 on specific principles for terminating employment contracts for reasons not related to employees (Journal of Laws, No. 90 of 2003, Item 844 as amended)].

The amount of additional severance payments depended on the level of compensation of individual employees and their years of service with the PZU Group.

In 2011, 1,943 employees were affected by layoff procedures. Contract termination was initiated with 1,276 employees as a result of severance agreements, termination notices and employee refusals to accept the new terms and conditions of employment not due to the fault of the employee. Moreover, employment contracts with 75 employees were terminated under individual layoff procedures, for reasons not related to the employees, and the costs of the layoffs were also charged to the restructuring provision.

An outplacement program was launched for the laid-off employees, one of the largest support programs for such employees realized in Poland in 2011.
Total restructuring expenses were PLN 58.2 million in 2011 (in 2010: 147.8 million).

As at 31 December 2011, the restructuring provision costs amounted to PLN 113.0 million (as at 31 December 2010: PLN 75.3 million), which signified movement of the provision of PLN 37.7 million in 2011.

Other HR activities

In 2011, a new HR project was conducted called „New Energy of PZU Leaders" – a development program for key PZU managers from the Mass Client department. The Project intends to bolster permanently the skills of key PZU sales managers and giving them a competitive edge on the market in respect of sales of non-life insurance to retail clients. 25 key managers are participating in the program.

24. ACTIVITIES RELATED TO CORPORATE SOCIAL RESPONSIBILITY

Business Ethics

The PZU Group adheres to the ethical principles of corporate social responsibility described in item 10.

Social commitment

As part of its educational activities, PZU maintains an Internet insurance-dedicated service – „JakieUbezpieczenie.pl". The character of the site is purely informative and educational. It explains the benefits of insurance products in a simple and easily comprehensible manner.

Just as in previous years, PZU conducted preventive activities aimed at improving public safety and limiting various risks. In this respect the following actions were taken in 2011:
- cooperation with TOPR, GOPR and selected WOPR groups was continued;
- cooperation with Stowarzyszenie Misie Ratują Dzieci (Teddy Bears Save Children Association) was initiated in therapeutic and psychological help for children injured in accidents;
- the Bezpieczna Flota (Safe Fleet) project was undertaken addressed to selected fleet drivers.

PZU also was the sponsor and patron of various nationwide and local cultural and sports events. Key activities in this area include:
- sponsoring the Royal Castle in Warsaw;
- the PZU zone during the Night of Museums at the Royal Castle in Warsaw;
- close cooperation with the Nowe Sukiennice National Museum Department in Kraków;
- patron of the Royal Łazienki Museum;
- sponsoring the Grand Theatre in Warsaw;
- sponsoring the „Rzeszów Carpathia Festiwal 2011";
- patron of Willa Decjusza in Kraków;
- sponsoring the „Droga na Harvard" (Way to Harvard) competition;
- sponsoring the Polish Presidency in 2011;
- sponsoring the educational program entitled Akcjonariat Obywatelski (Citizen Shareholdership).

The PZU Foundation

The PZU Foundation's mission is to act in the interests of the public in education, culture, art, healthcare and social security. The PZU Foundation pursues its goals by co-financing projects carried out by non-governmental organizations and other organizational entities in its operational areas.

In 2011, the PZU Foundation awarded subsidies under consecutive editions of competitions and projects outside the framework of competitions, and for individual aid.

In „Education" the following actions were taken:
- a grant competition entitled Expanding the educational offer in rural areas and in small towns;
- Partnership programs were introduced:
  - in cooperation with Fundacja Edukacyjna Przedsiębiorczości in Łódź – scholarships were set up for young people from rural areas and small towns;
  - two editions of historical workshops were co-financed organized by Fundacja Centrum im. prof. Bronisława Geremka in Warsaw;
  - financial support was offered for the project „Świetlica – Moje Miejsce" conducted in cooperation with Polska Fundacja Dzieci i Młodzieży in Warsaw;
  - three-year cooperation was established with the national children's fund (Krajowy Fundusz na rzecz Dzieci) in Warsaw under a program to help extremely- gifted persons ;
  - one-off subsidies were awarded to Fundacja Pomoc Polakom na Wschodzie in Warsaw, Fundacja ABC XXI – Cała Polska czyta dzieciom in Warsaw, Fundacja dla Uniwersytetu Jagiellońskiego in Kraków and Fundacja Młodzieżowej Przedsiębiorczości.

In the area of „Culture and Art", the PZU Foundation supports cultural institutions such as the National Museum in Kraków and the National Museum in Warsaw by acquiring new collections on their behalf.

In the area of „Social care and social aid" grants were awarded:
- in the competition entitled „Developing social activity in handicapped children and adolescents";
- to disadvantaged individuals, including PZU employees;
- to Stowarzyszenie Wspólnota Polska in Warsaw by financing insurance for children and adolescents from Poland's eastern neighbors during their stay in Poland;
- to the Holy Cross Mokotów Hospice in Warsaw;
- to organizations named in the PZU employees commitment survey.

In „Health Protection", initiatives aimed at widely-understood health prevention were financed. Grants were made to the organizations listed below:
- the Polish Community Association in Warsaw by financing insurance of the medical mission in Ukraine and Moldavia;
- Polish Union of Oncology in Warsaw.

25. MAIN ACTIVITIES IN IT

In 2011 the functioning of joint consolidated IT structures in the PZU Group stabilized. The following tasks were among the ones completed:

- the first stage of the project for a shared ERP class system for PZU and PZU Życie was implemented, which is to take over the systems currently in operation ultimately;
- the system for supporting the creation of standalone and consolidated financial statements was implemented (the Hyperion system);
- the process of automatic policy population in the sales system to the policy administration system was launched;
- tools were implemented to reduce the costs of technical IT infrastructure and to augment its reliability (such as the process of accelerating the wide area network, tools for monitoring the operations of critical systems, modernizing data maintenance and backup system).

Moreover, in 2011 several important initiatives were launched which could lead to implementing new IT tools, including commencing work on the project aimed at replacing PZU's key policy system.

26. PLANNED KEY DEVELOPMENT DIRECTIONS

The strategy for 2012-2014 will, to a large extent, be a continuation of the pursuit of the goals under the strategy in 2009-2011. The PZU Group's objective is to maintain profitable growth and its leading position on the Polish insurance services market.

In the foreseeable future, the PZU Group's operating model will be transformed from a product-oriented organization to a customer segment-oriented organization. These transformations will enable the Group to understand the needs of its clients better and to react appropriately to their needs. In later years, further optimization of the PZU Group's operations is planned.

A pro-client orientation coupled with high operating efficiency will allow the Group to maintain its leading position – the PZU Group will continue to be the largest and most profitable insurance company in Central and Eastern Europe.

These goals will be accomplished by focusing on the following actions:

- in the mass client segment:
  - maintaining the market share in the motor insurance and property insurance segment and introducing advanced principles for price-setting and reacting to market changes;
  - dynamic development of savings and investment products, and in particular long-term savings products;
  - further development in mass sales by developing basic distribution channels;
- in the group client segment:
  - maintaining the profitable leading position in life insurance;
  - creating a health insurance market to increase the scale of business in that area;
  - actively upselling products related to health and drug insurance to group clients;
  - strengthening direct relations with insureds through PZU Club's offer „Pomoc w Życiu" (help in life);
- in the corporate client segment:
  - transforming PZU into a business partner with a strong expert position that is not only an entity selling insurance but also a client advisor;
  - maintaining its market position in motor insurance and increasing its market share in non-motor insurance;
- in the operating model:
  - introducing a new product system in PZU which will enable an increase in operational efficiency;
  - implementing a new customer service model calling for an integrated contact channel structure, compliant with customer expectations, and specifically building a network of modern sales and service outlets;
  - further optimization in claims handling and operations.

Additionally actions are planned:

- continuing operations focused on transforming the PZU Group into a performance-oriented organization;
- increasing the PZU Group's scale of operations through international expansion on the Central and East European markets;
- refreshing the brand to enable modernization and communicating the changes that have already been implemented in the PZU Group;
- introducing changes in the investment policy covering, among other things, a change in investment structure prompting higher profitability while simultaneously curtailing the volatility of investment performance.

27. OTHER SELECTED PZU GROUP COMPANIES

PZU Lietuva

In 2011, PZU Lietuva improved its market position taking 3rd place. Despite the difficult situation on the insurance market, the Company grew sales by nearly 10%. The Company managed to reduce both the loss ratio and the ratio of operating expenses net of reinsurance, by consistently lowering the level of the combined ratio, while the forecasted profit was consumed by the loss on investing activity following the declared bankruptcy of one of the largest banks in Lithuania. The declared bankruptcy was an unexpected event according to the general opinion of the analysts.

There were no extraordinary single claims or catastrophic claims. A significant factor affecting the financial result was the bankruptcy of the bank AB Snoras, which cooperated with PZU Lietuva. The total amount of PZU Lietuva's accounts receivable from AB Snoras is LTL 8.6 million. The Company established a 100% provision for these accounts receivable, which caused the negative financial result in 2011. The consequence is that the Company's share capital fell to below one half of the share capital, which constitutes a breach of the Lithuanian regulations for the operation of a commercial law company. This implies the necessity of undertaking measures to rectify the breach in the first half of 2012 by covering the loss by PZU making a cash contribution and using future earnings. The impairment charge did not affect the Company's solvency – here the ratios remained at the level required by the regulations. It should be pointed out that had this event not been incorporated, the Company would have generated a net financial result higher than last year.

In 2011 PZU Lietuva concentrated on further enhancement of the profitability of its motor portfolios and strengthening its position on corporate non-life insurance.

In 2011, activities initiated in the previous year were continued aimed at full unification of non-life and life insurance in the PZU Lietuva Group. The objective of this process is to adapt the structure of PZU Lietuva to corporate governance guidance, among others, by reducing operating expenses.

PZU Ukraine

In 2011, PZU Ukraine recorded a high premium growth rate accompanied by small growth in the Ukrainian insurance market. After three quarters, the Company was number 10 on the traditional property and casualty insurance market (data as at the end of the third quarter of 2011).

The modifications in the approach to the tariffication of motor vehicle insurance products, constituting the bulk of the portfolio of PZU Ukraine, introduced in 2010, led to a considerable improvement in profitability in 2011. Despite the slight deterioration in the insurance activity expense ratio the technical result and the net financial result were considerably better than last year, while topping the targets. In 2011 company's attention was particularly focused on the profitability of the medical insurance portfolio under the continuation of actions launched in 2010.

In 2011 the capital restructuring process was initiated. The financial results of the two companies of the PZU Ukraine Group, the non-life and life companies, improved considerably compared to 2010 results.

TFI PZU

The key undertakings of TFI PZU in 2011 in sales and marketing include:
- actively acquiring employee pension schemes;
- actions aimed at organizing the distribution network;
- promoting the best TFI PZU funds in the media.

In 2011, TFI PZU introduced changes to its product offer:
- nine open investment funds with a diversified investment policy were transformed into PZU FIO Umbrella Fund with subfunds;
- PZU SFIO Ochrony Majątku was transformed into Fundusz PZU FIO Ochrony Majątku;
- two new closed-end investment funds were created: PZU FIZ Sektora Nieruchomości 2 and FIZ RE Income.

TFI PZU's significant achievements in 2011:
- honoring the Employee Pension Scheme run by TFI PZU with the Polish Promotion Emblem „Teraz Polska";
- acquiring and handling 15 new Employee Pension Schemes;
- recognizing PZU Energia Medycyna Ekologia investment fund as the „DISCOVERY OF THE YEAR 2011" during the 7th edition of the Consumer/Client Laurels conducted by Rzeczpospolita;
- awarding four stars to the PZU Papierów Dłużnych POLONEZ Subfund in the Online Analyses Rating;
- launching a new unit-linked product with Towarzystwo Ubezpieczeniowe Benefia na Życie SA;
- forming and launching, together with PZU Życie, the Millennium Prestige 2 Investment Scheme;
- commencing works on launching a service for distributing units of TFI PZU funds through remote channels: by the web and phone.

As at the end of 2011, the net asset value of the investment funds managed by TFI PZU was PLN 5,371.2 million (a 66.3% increase compared with the end of 2010). The increase in the net asset value resulted from the PZU Group companies' own investments in units of TFI PZU funds and in investment certificates of dedicated closed-end investment funds, the positive net balance of new investments and redemptions of fund participation units and the increase in the value of fund investments.

PZU AM

As planned, in 2011 PZU AM provided services solely to PZU Group companies, i.e. to PZU, PZU Życie, TFI PZU and MPTE PZU SA.

In accordance with the plans, in 2011 PZU AM began managing new investment portfolios (PZU FIZ Sektora Nieruchomości 2; FIZ RE Income; Model Funds for PZU Życie).

PZU Pomoc SA

In 2011, many new initiatives were launched, including:
- launching an auction platform „PZU Pomoc ONLINE" whose purpose is to sell damaged vehicles and property;
- purchase of cars for providing roadside assistance;
- implementing loyalty programs:
  - „Klub PZU Pomoc w Życiu" – for clients of PZU Życie holding life insurance in the group insurance sector;
  - „Karta Klienta PZU - Niezguba" – for clients of PZU holding a motor vehicle insurance package (at least motor TPL and own damage). The pilot scheme will end in December 2012;
  - „PZU Business Club" – for representatives of entrepreneurs having a business relation with PZU or PZU Życie, with a specified level of premium written or number of insured persons;
- launching operations in medical services.

In July 2011, the company ended its preparations for launching activities in offering and organizing medical services, with more than 600 medical facilities signed up throughout Poland and the launch of a medical hotline.

On 11 August 2011, the company signed a cooperation contract with PZU Życie for providing medical services to the PZU Group's health insurance clients. Therefore, on 1 September 2011, PZU Życie received its first group of Clients (employees of PZU and PZU Życie) – a total of 8,255 insureds.

PZU Centrum Operacji SA

In 2011, PZU Centrum Operacji (PZU CO) executed a number of undertakings, which included:
- incorporating the Insurance Services Center in Warsaw and a part of the Call Center within PZU CO's organizational structure
- carrying out the project to handle and distribute the Individual Retirement Security Account (IKZE) for PTE PZU SA and PZU Życie SA;
- creating the Internet Auction Platform - PZU Pomoc SA;
- optimizing service processes and resources utilized.

28. PZU TAX CAPITAL GROUP

On 5 September 2008 the Management Boards of PZU and PZU Życie adopted a resolution on PZU and PZU Życie forming a Tax Capital Group (hereinafter: „TCG") within the meaning of the Corporate Income Tax Act of 15 February 1992 (Journal of Laws, No. 74 of 2011, Item 397 as amended, „CIT Act"). PZU and PZU Życie formed the TCG and it was established for a period of 3 years – from 1 January 2009 to 31 December 2011.

On 27 September 2011 a new Tax Capital Group agreement was concluded by the PZU Group companies covering 9 companies: PZU, PZU Życie, TFI PZU, PZU AM, PZU CO, PZU Pomoc SA, Ipsilon BIS SA, Ogrodowa-Inwestycje Sp. z o.o. and Ipsilon Sp. z o.o. This TCG was established for a period of 3 years – from 1 January 2012 to 31 December 2014.

In both TCG agreements PZU was the parent company and the entity representing the TCG. According to art. 25 section 1 of the CIT Act, a TCG settles accounts with the tax office on a monthly basis. PZU remits advances to the tax office for corporate income tax due from all the companies in the TCG, and they transfer their advances toward the corporate income tax on their economic activity to PZU.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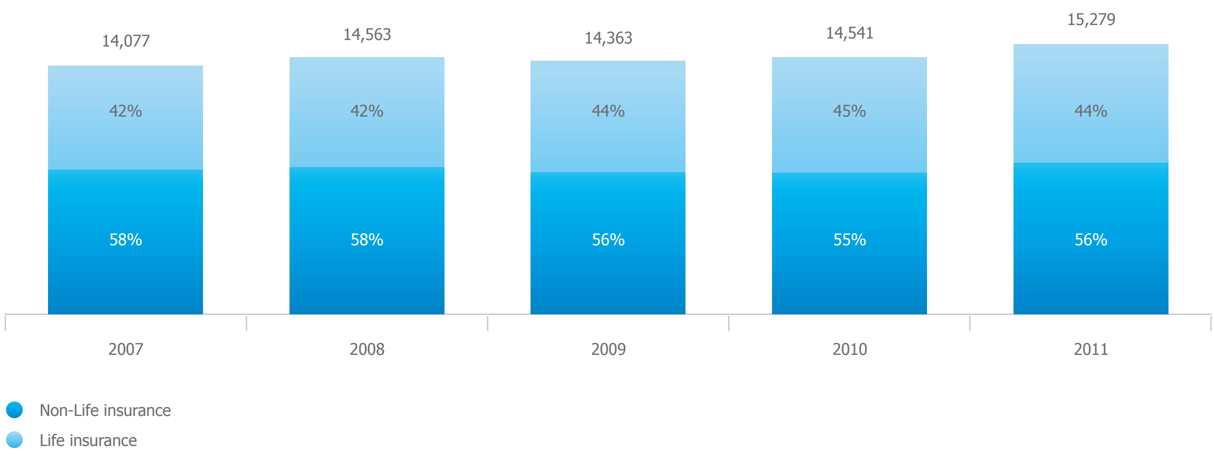
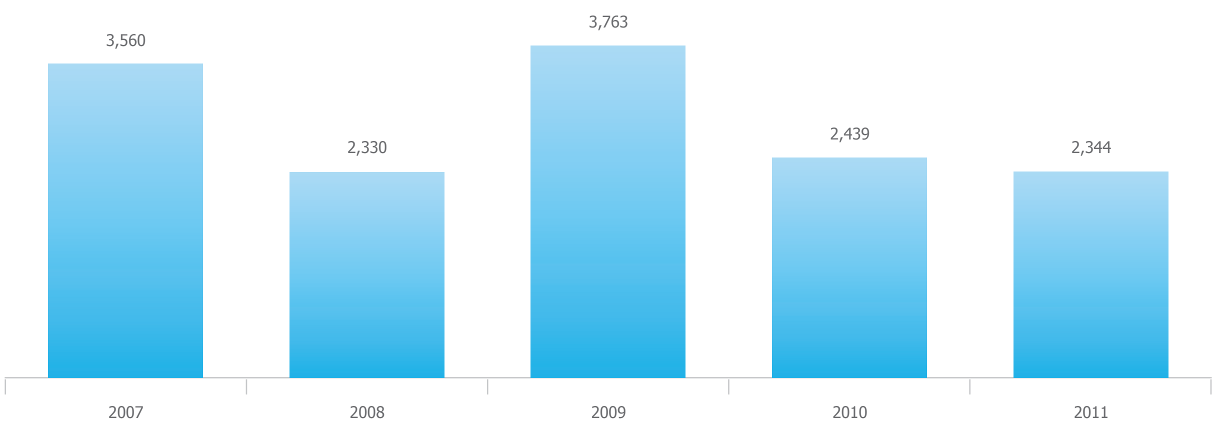
29. FINANCIAL SUMMARY OF 2011 – CONSOLIDATED DATA

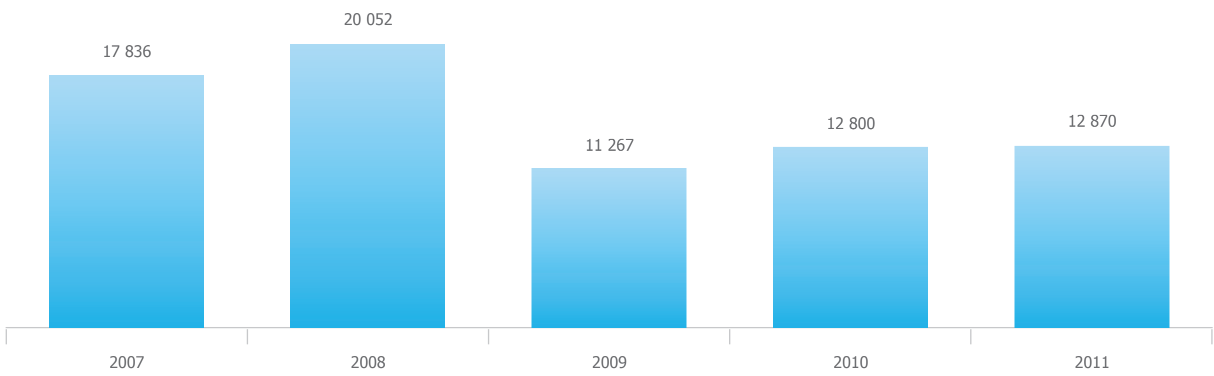
Gross written premium (PLN mn, %)



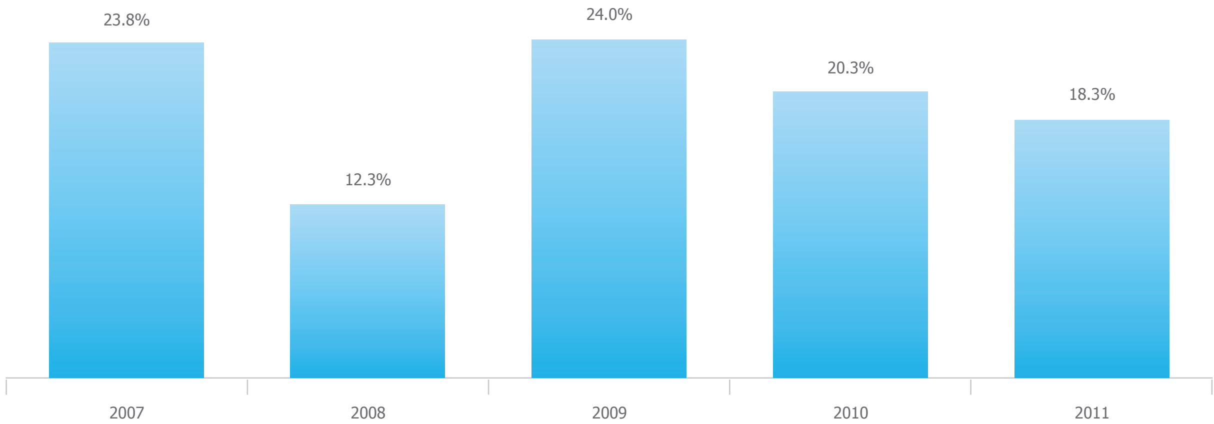
Net financial result (PLN mn)



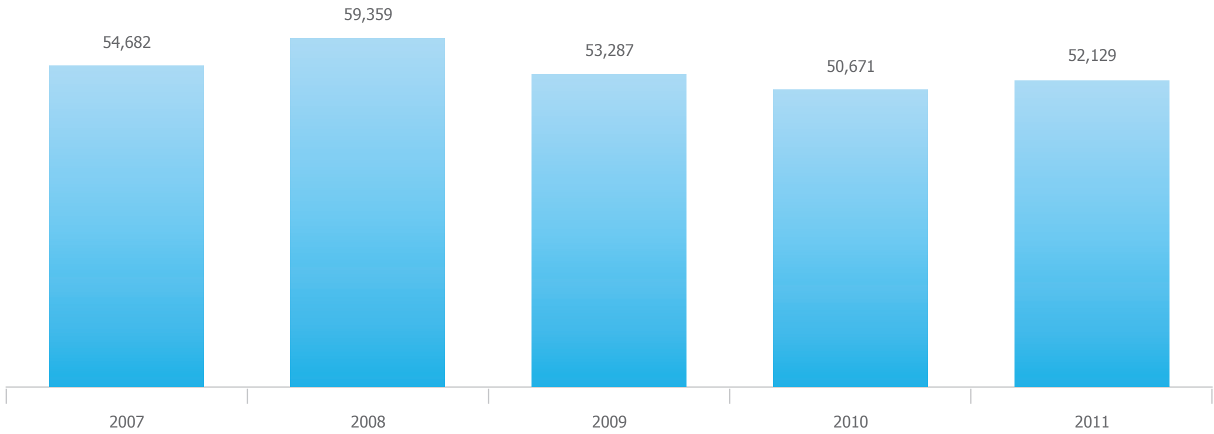
Equity (PLN mn)



Return on equity – ROE (%)[1)]

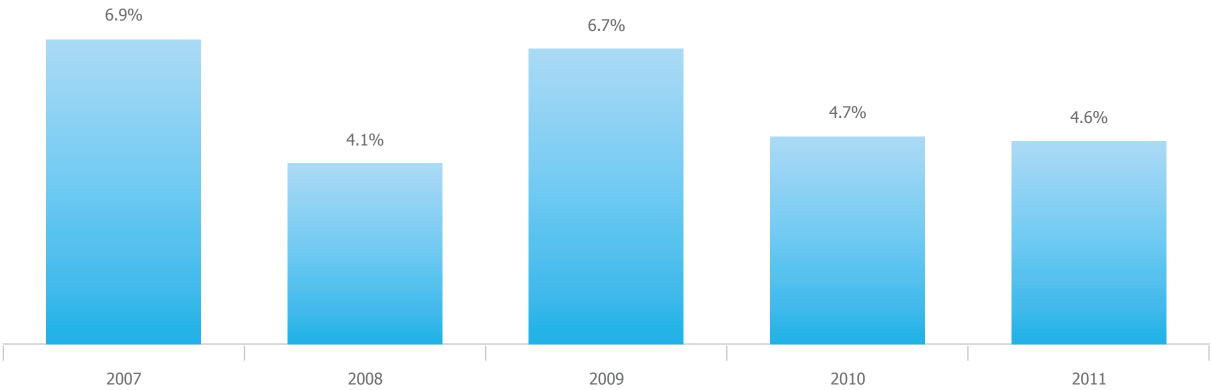


Total assets (PLN mn)

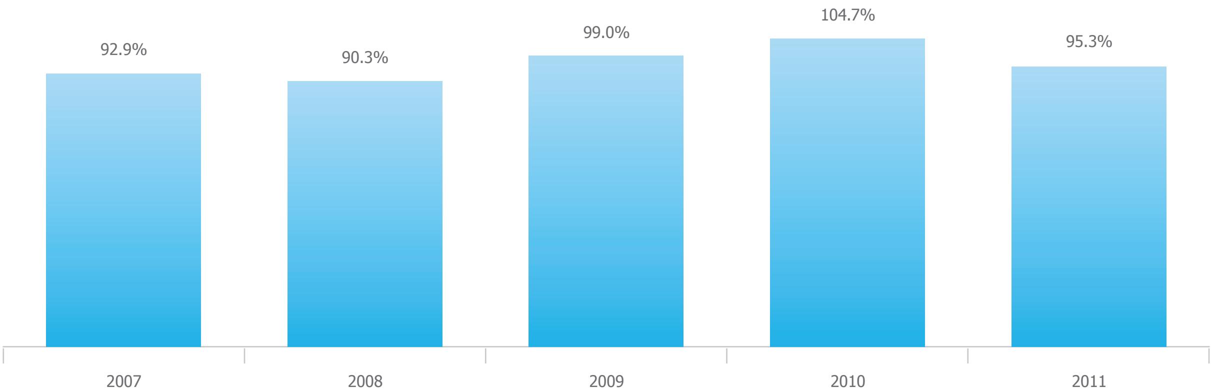


[1)] ROE – ratio calculated as the quotient of the net result and the average amount of equity at the end and beginning of the reporting period.

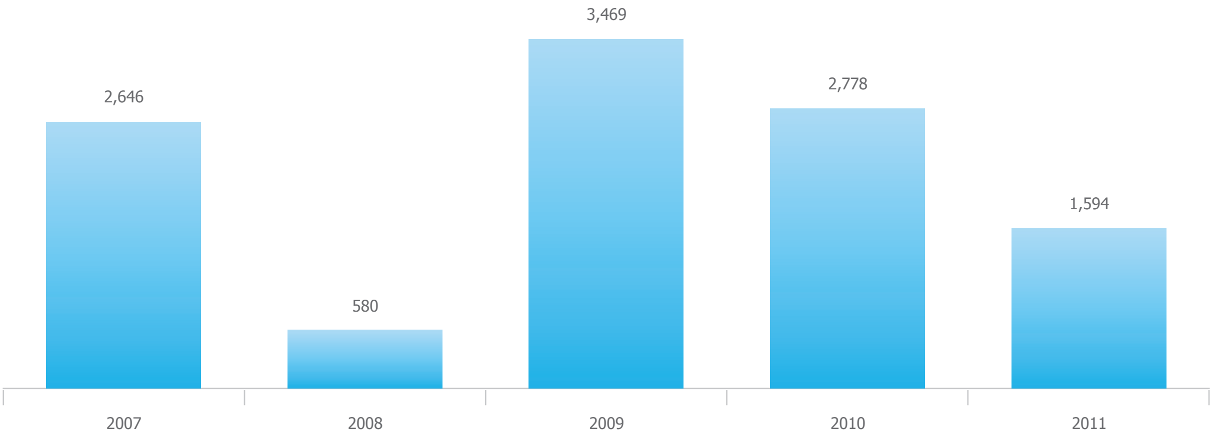
Return on assets – ROA (%)[2)]



Combined ratio – COR (%)[3)]



Investments results (PLN mn)



Source: PZU Group data, according to IFRS

[2)] ROA – ratio calculated as the quotient of the net result and the average amount of equity at the end and beginning of the reporting period.

[3)] COR – combined ratio in non-life insurance segment calculated as a sum of costs and claims ratios.

The PZU Group's net financial result in 2011 was PLN 2,343.9 million. The PZU Group's operating profit in 2011 was PLN 2,956.7 million, making it 4.3% lower than the previous year's result, stemming primarily from the lower results on investing activity (- 42.6%). This decline was compensated for to a considerable degree by the 4.8% growth in the net earned premium and the 1.6% decline in net claims paid. ROE[4)] at yearend 2011 was 18.3%.

PZU's 2011 net profit (the parent company of the PZU Group) was PLN 2,582.3 million, yielding PLN 29.90 per share. PZU's investments at yearend 2011 were PLN 24,882.9 million. Its equity was PLN 11,745.4 million. PZU's ROE in 2011 was 21.8%. The Company paid a gross dividend of PLN 26.00 per share.

[4)] ROE – ratio calculated as the quotient of the net result and the average amount of equity at the end and beginning of the reporting period.

30. MACROECONOMIC ENVIRONMENT IN 2011

Basic trends in the economy and pace of economic growth

In 2011 Poland's GDP increased by 4.3%, which exceeded expectations and the previous year's GDP growth (3.9%). In 2011 the rate of increase in domestic demand slowed slightly to 3.8% compared with 4.6% in 2010, and contrary to 2010, net exports contributed to GDP growth. Once again in 2011 retail consumption was the most important factor underpinning economic growth with a 3.1% increase compared to 3.2% in 2010. However, in the second half of the year, its growth rate started to decline significantly due to real income increasing at a slower pace. Moreover, domestic consumption was lower in 2010. In 2011 capital expenditures on fixed assets increased quarter on quarter, mainly as a result of public investments in infrastructure. In 2011 investments rose by 8.5%, compared to a 0.2% decline in the previous year, thereby becoming a factor almost as important to GDP growth as retail consumption. In 2011 the GDP input contributed by investments was significantly lower than in 2010, and in Q1 2011 it was negative for the first time since 2009.

On the supply side of economic growth, added value in the construction industry increased the most in 2011 (11.8% compared with 6.4% in 2010), thus confirming the important part played by infrastructural investments. Added value in the industrial sector increased at a slower pace in 2011 compared with 2010 (6.3% compared with 9.4%). The pace of growth of added value increased in trade and repairs of motor vehicles (4.6% compared with 2.6%).

Capital markets

In 2011, despite the good financial position of companies and the relatively high GDP increase, the key indices of the Polish equities market, namely WIG and WIG20 slumped by 20.8% and 21.9%, respectively. Until April, these rose in line with expectations of accelerated global economic growth. In Q2, the global growth outlook dampened, which translated into investors' increased risk aversion on the global financial markets. In Q3, the exacerbation of the global debt crisis in the Eurozone, fiscal problems in the USA coupled with rating agencies downgrading the highest financial credibility ratings, as well as revised data on the country's GDP, contributed to an enormous increase in risk aversion on the global financial markets which also resulted to a fall-off in the WIG and WIG20 indices.

The return on Polish debt remained relatively stable throughout the financial market turbulence in 2011. As the Eurozone debt crisis intensified and investors became increasingly risk averse in the global debt market, the yield on Polish ten- and five-year treasury bonds dropped by 16 and 17 basis points, respectively from the end of 2010 until 2011. The yield on two-year bonds, however, increased by 7 basis points. The average annual return on Polish debt was slightly higher than in 2010 with two- and five-year bonds edging up by 7 and 11 basis points, respectively and with 10-year bonds advancing by 19 basis points. The resilience of the Polish debt market to crisis events was the result of the relatively high economic growth, progress in reducing the budget deficit and efficient management of financing borrowing needs.

Monetary policy, interest rates, inflation

In 2011 the average annual inflation (CPI) was 4.3% compared to 2.6% in 2010, and at the end of the year the prices of consumer goods were 4.6% higher than in 2010 (3.1% y/y in 2010). The acceleration of inflation in the first half of 2011 resulted from global trends: higher food prices and other raw materials (including mainly fuels), and administrative price hikes (including household energy prices) and the VAT rate hike. In the second half of 2011, in turn, the Polish zloty's weakening against key currencies was a pro-inflationary factor. In 2011 net inflation grew steadily (CPI, net of food and energy prices) climbing to 3.1% at yearend. The Monetary Policy Council (RPP) increased interest rates four times during the first half of 2011, each time by 25 basis points. Since June 2011, in view of the escalation of the debt crisis in the Eurozone and increased uncertainty as to Poland's further economic growth, the Monetary Policy Council held interest rates at an unchanged level (with the NBP reference rate at 4.5%).

Labor market and consumption

In 2011 labor market conditions deteriorated steadily. Despite higher employment in the corporate sector by approximately 124 thousand people in December 2011 compared with December 2010 (2.3% y/y compared with 2.4% y/y in 2010), the demand for employees had been falling since Q2 2011. The slower pace of employment growth accompanied by an insignificantly higher number of active employees contributed to the recorded unemployment rate staying at a higher level (annual average unemployment figure of 12.4% compared with 12.1% in 2010, at yearend 12.5% compared with 12.4%). In these conditions, wage and salary growth remained moderate. Although the average monthly salary in the national economy increased in nominal terms by 5.4% in 2011 compared with 3.9% in the previous year, in the second half of the year, nominal and real wages and salaries fell in the corporate sector. At the end of 2011 the average monthly salary in the corporate sector after accounting for inflation was slightly lower than at the end of 2010. High inflation was a significant factor contributing to the constriction of real household income in 2011, in particular due to slower growth of social benefits. Therefore, individual consumption increased by 3.1% compared with 3.2% in 2010, but its growth rate fell noticeably in Q2. In Q4 2011 consumer satisfaction rates dropped yet again.

Foreign exchange rates

Increased risk aversion on the global financial markets related to the intensification of the debt crisis in the Eurozone in the second half of 2011 (especially in Q3) contributed to weakening the Polish zloty and greater volatility. The EUR to PLN exchange rate (NBP fixing) was 11.5% higher at the end of 2011 than at the end of 2010, and the USD to PLN rate increased by 15.3%. The changes in the PLN annual average exchange rate were lower: the EUR / PLN exchange rate increased by 3.1%, and the USD / PLN rate dropped by 1.7%. Faced with greater risk aversion, the CHF also strengthened against the PLN, and the CHF / PLN exchange rate was 14.8% higher at the end of 2011 than at the end of 2010.

Impact exerted by macroeconomic factors on the insurance sector

The macroeconomic conditions had an ambiguous impact on the sales of insurance. On one hand, relatively high GDP growth should contribute to higher demand for insurance services. However, on the other hand, especially in the second half of the year, real income growth fell and thus the conditions for an increase in consumer demand deteriorated. GDP growth was increasingly driven by investments, especially infrastructural investments.
In 2011 production, imports and sales of cars dropped, whereby the average age of cars in Poland rose and the demand for motor own damage insurance[1)] slackened. The sales growth of durable consumer goods also fell. On the other hand, in 2011 corporate capital expenditure increased after falling in 2010. The financial results of non-financial companies in 2011 improved compared with 2010, contributing to improvement in the conditions of sales of insurance products to corporate clients.

The weakening of the zloty against the EUR exerted an adverse impact on the loss ratio in motor insurance due to the impact exerted by imported spare parts (this phenomenon persisted over time as importers maintained certain inventories).

In 2011 the credit market revived somewhat which could have had a positive impact on sales and related financial insurance. This related mainly to corporate loans. The increase in mortgage loans was lower than in the previous year and the value of originated consumer loans dropped.

The equity price decline in 2011 following heightened global risk aversion exerted an unfavorable impact on investment income and on the demand for unit-linked insurance.

[1)] Automobile production data according to the Central Statistical Office, sales and import-related data according to Samar.

31. MARKET SHARES OF PZU, PZU ŻYCIE AND PTE PZU

Overall insurance market

The gross written premium in the Polish insurance sector according to Polish Accounting Standards („PAS") as at the end of September 2011[1)] was PLN 57,150 million, representing an 5.5% increase (+ PLN 2,987 million) compared with the first three quarters of the previous year.

[1)] Most current data published by the Polish Financial Supervision Authority („KNF") as at the moment of preparing the PZU Annual Report.

Property and casualty (non-life) insurance

Non-life premiums in the first three quarters of 2011 increased by 11.3% to PLN 25,301 million compared with the first three quarters of the previous year were many price hikes on the market in the period from Q2 2010 to Q1 2011.

The share of Powszechny Zakład Ubezpieczeń Spółka Akcyjna („PZU") measured by gross written premium in the Polish non-life insurance market was 32.6% as at the end of December 2011. PZU remains the leader on the Polish insurance market, specifically in the motor insurance sector.

Non-life insurance market – gross written premium

PLN million

Property insurance market – gross written premium	2011			2010		
	PZU	Market	Market without PZU	PZU	Market	Market without PZU
Motor own damage insurance	2,285	5,822	3,537	2,258	5,263	3,005
Motor TPL	2,891	8,725	6,101	2,591	7,674	5,083
Other products	3,071	10,754	7,416	2,935	9,804	6,869
TOTAL	**8,247**	**25,301**	**17,054**	**7,784**	**22,741**	**14,957**

Source: KNF (www.knf.gov.pl). Quarterly Bulletin. Insurance Market 4/2011, Insurance Market 4/2010, PZU data.

Non-life insurance market – analysis of gross written premium

Structure of written premium	2011			2010		
	PZU	Market	Market without PZU	PZU	Market	Market without PZU
Motor own damage insurance	27.7%	23.0%	20.7%	29.0%	23.1%	20.0%
Motor TPL	35.1%	34.5%	35.8%	33.3%	33.8%	34.0%
Other products	37.2%	42.5%	43.5%	37.7%	43.1%	46.0%
TOTAL	**100.0%**	**100.0%**	**100.0%**	**100.0%**	**100.0%**	**100.0%**

Source: KNF (www.knf.gov.pl). Quarterly Bulletin. Insurance Market 4/2011, Insurance Market 4/2010, PZU data

Non-life insurance market – PZU share in market premium

PZU SA share in market premium (in %)	2011	2010
Motor own damage insurance	39.3%	42.9%
Motor TPL	33.1%	33.8%
Other products	28.6%	29.9%
TOTAL	**32.6%**	**34.2%**

Source: KNF (www.knf.gov.pl). Quarterly Bulletin. Insurance Market 4/2011, Insurance Market 4/2010, PZU data

The main reason for the drop in PZU's market share in the non-life insurance market is its pursuit of the corporate insurance portfolio restructuring program, mainly in the area of motor insurance, aimed at lowering the loss ratio. Under this program a restrictive underwriting policy is pursued in respect of areas of operation with increased risk, where the key focus is on the security of the portfolio and earning a technical profit.

Non-life insurance market – technical result

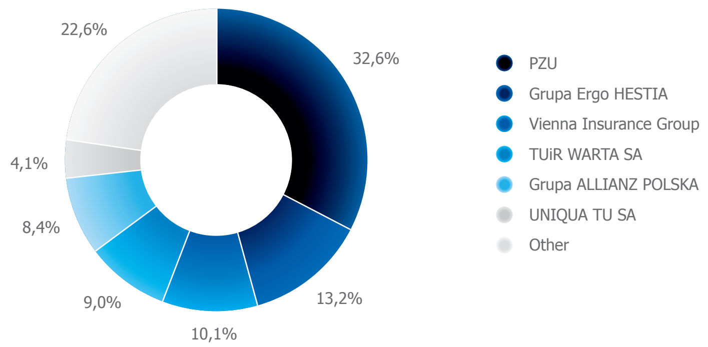
PLN million

Technical result	2011			2010		
	PZU	**Market**	**Market without PZU**	**PZU**	**Market**	**Market without PZU**
Motor own damage insurance	248	333	85	(6)	(315)	(309)
Motor TPL	(105)	(512)	(407)	(160)	(908)	(748)
Other products	189	608	419	(163)	(53)	110
TOTAL	**332**	**429**	**97**	**(329)**	**(1 276)**	**(947)**

Source: KNF (www.knf.gov.pl). Quarterly Bulletin. Insurance Market 4/2011, Insurance Market 4/2010, PZU data.

Due to the increase in rates and restructuring the quality of the motor insurance portfolio (specifically in the corporate client segment) and the absence of natural disasters which had such an impact on PZU's 2010 results, the Company achieved very good technical results compared with other companies on the market. This is specifically visible in motor insurance.

Market share held by the largest non-life insurers in Poland



Source: KNF (www.knf.gov.pl). Quarterly Bulletin. Insurance Market 4/2011, Insurance Market 4/2010, PZU data.

Life insurance

The gross written premium in life insurance has increased by +1.4% yoy, which implies deceleration compared to the growth rate in 2010, when it was +3.8%. Lower growth was visible in regular premiums (+1.9% growth in 2011 vs. 2010, as compared to a +8.3% increase in 2010 vs. 2009). Single premiums increased slightly (+0.9%, as compared to 2010 and 2009, when no growth was reported). Slower growth of regular premiums results from higher unemployment, entailing a gradual decrease in salary growth in the corporate sector. The stable level of single premiums results from reducing the supply of products combining the features of a life insurance policy and a bank deposit, caused by low profitability, significant capital requirements and lower demand for unit-linked insurance (unstable situation in the financial markets and investing funds in low-risk assets).

Life insurance market – gross written premium and technical result

PLN million

Life insurance market – gross written premium vs. technical result	2011			2010		
	PZU Życie	Market	Market without PZU Życie	PZU Życie	Market	Market without PZU Życie
Gross written premium	9,806	31,849	22,043	9,300	31,422	22,122
Technical result	2,015	3,345	1,330	2,145	3,601	1,456

Source: KNF (www.knf.gov.pl). Quarterly Bulletin. Insurance Market 4/2011, Insurance Market 4/2010, PZU data.

In 2011 the market share of PZU Życie increased to 30.8% (+1.2 p.p. compared with 2010). The Company sustained its dominant market share in the key segment of regular premiums at 43.4%. Thanks to the cooperation with PKO BP SA and Bank Millennium SA, PZU Życie's share of the single premium segment increased by 1.9 p.p. to 19.5%.

PZU Życie's technical result accounts for the majority of the results earned by all life insurance companies. It should be emphasized that despite the drop in technical result, in 2011 PZU Życie's technical profit margin on written premium still exceeds the margin earned by all the other life insurance companies by more than three times (20.6% vs. 6.0%).

Life insurance market – gross written premium

PLN million

Life insurance market – gross written premium	2011			2010		
	PZU Życie	Market	Market without PZU Życie	PZU Życie	Market	Market without PZU Życie
Regular premiums	6,530	15,040	8,510	6,363	14,758	8,395
Single premiums	3,276	16,808	13,532	2,937	16,664	13,727
TOTAL	**9,806**	**31,849**	**22,042**	**9,300**	**31,422**	**22,122**

Source: KNF (www.knf.gov.pl). Quarterly Bulletin. Insurance Market 4/2011, Insurance Market 4/2010, PZU data.

Pension insurance

Position of OFE PZU (open pension fund) on the pension market in Poland

Market for pension insurance	31 December 2011			31 December 2010		
	OFE PZU	OFE market	OFE market without PZU	OFE PZU	OFE market	OFE market without PZU
Number of fund members	2,214,995	15,493,373	13,278,378	2,193,502	14,930,991	12,737,489
Net assets under management in PLN million	30,523	224,720	194,197	30,660	221,251	190,592

Source: KNF (www.knf.gov.pl). Pension market. Monthly data.

Share of OFE PZU (open pension fund) in the pension market in Poland

Share of OFE PZU „Złota Jesień" in the market (in %)	31 December 2011	31 December 2010
Number of fund members	14.3%	14.7%
Net assets under management in PLN million	13.6%	13.9%

Source: KNF (www.knf.gov.pl). Pension market. Monthly data.

As at the end of 2011, Otwarty Fundusz Emerytalny PZU „Złota Jesień" („OFE PZU") had approximately 2,215 thousand members, which constituted 14.3% of the total number of open pension fund („OFE") members and ranks OFE PZU third on the market. Compared with the end of 2010, the number of OFE PZU members increased by 21.5 thousand people, i.e. 1.0%.

In 2011 the number of people signing contracts with open pension funds for the first time dropped by as much as 40% compared with 2010. The main reason for the drop was the limitation of acquisition activity by funds indirectly caused by the reduction in the contribution transferred to OFE, and an increase in the unemployment rate among graduates.

Moreover, the number of people who decided to change funds dropped (a drop of 5.0% compared with 2010). OFE PZU was one of the funds with a negative churn rate (12,962 people); however, it was still the best result among the three largest funds (ING OFE noted a net negative churn of 51 thousand people, and Aviva OFE 111 thousand people).

As at the end of 2011, the total value of net assets in all the open pension funds was PLN 224,720.1 million and had increased by 1.6% compared with the end of 2010. OFE PZU assets dropped by 0.4% during the period, to PLN 30,523 million, which placed OFE PZU third among all OFEs operating on the market in terms of assets.

Investment funds

According to data provided by the Chamber of Fund and Asset Managers „IZFA" as at the end of December 2011 the net asset value of investment funds in Poland amounted to approximately PLN 114.7 billion, and the drop in managed assets in 2011 amounted to approximately 4.8%. The net balance of new investments and redemptions was minus PLN 3.3 billion. Most new fund inflows were seen in debt funds, money market funds and cash funds (of approximately PLN 2.1 billion each). The largest outflows were noted in mixed funds (approximately PLN 5.8 billion) and equity funds (approximately PLN 2.9 billion).

The share of the five largest investment fund management companies in terms of the net asset value of the managed investment funds as at the end of December 2011 amounted to 41.3%.

In terms of the net asset value of funds, TFI PZU ranks tenth among the 33 investment fund management companies covered by the IZFA report. At the same time, TFI PZU remains the leader in the segment of employee pension funds among Polish investment funds, with assets exceeding PLN 1.3 billion.

Macroeconomic factors which will have an impact on PZU Group's operations in 2012

The expected slowdown in the pace of economic growth with the possible insignificant deterioration on the labor market may have a negative impact on the demand growth for insurance products.

The Eurozone debt crisis will continue to pose a risk to Poland's economic development in 2012. It may also contribute to sustained high volatility of financial asset prices and in the event of further exacerbation to decline, which would negatively impact investment income.

As of 1 April 2012, the tax exempt status of overnight term deposits will be liquidated. These term deposits were structured on a loophole in the Act of 29 August 1997 entitled the Tax Code (Journal of Laws, No. 8 of 2005, Item 60 as amended) which made it possible not to charge capital gains tax if the gain did not exceed PLN 0.50. These amendments were enacted in the Act of 22 December 2011 on amending some acts related to the performance of the Budget Act (Journal of Laws, No. 291 of 2011, Item 1707). When these amendments come into force, they will contribute to greater market interest in investment contracts based on insurance offered by life insurers, which poses an opportunity for PZU Życie to grow the sales of this type of insurance through the bancassurance channel and its own branch network.

32. PZU GROUP'S 2011 FINANCIAL RESULTS

Events with a significant impact on the operations and results of the PZU Group in 2011

The PZU Group's 2011 financial results were mainly shaped by:
- changes in the structure of written premium in the property and casualty (non-life) insurance, due to:
  - restructuring the corporate client portfolio;
  - retail tariff hikes (as of 2010);
- improved profitability in the non-life segment, mainly in motor and property insurance:
  - a significantly lower rate of natural disasters in the analyzed period, which in 2010 related mainly to snow and flood claims (PZU's net share in claims amounted to PLN 369.4 million);
- stable increase in gross written premium in group protection insurance;
- lower administrative expenses due to strict cost discipline and the implemented restructuring program, including group layoffs in regional branches and specialist units;
- lower investment profits compared with the previous year as a result of poor conditions on the capital markets, including the Warsaw Stock Exchange („WSE").

Commentary to the PZU Group's consolidated financial results

Premiums

Gross written premium on direct and indirect insurance for the year ended 31 December 2011 was PLN 15,279.3 million (PLN 14,541.0 million in 2010). The PLN 738.2 million (+5.1%) increase compared with the previous year resulted from higher sales in both segments: life and non-life. The main product lines recording growth in 2011 were motor TPL in the mass client segment (+PLN 287.3 million), fire and other property damage insurance (+PLN 102.0 million) and group insurance (+ PLN 179.5 million).

Changes in premiums are described in detail in the comments to segment results.

Analysis of gross written premium in the PZU Group

PLN' 000

Gross written premium	2011	2010	% change
Gross written premium in non-life insurance	8,527,492	8,028,481	6.2%
In direct insurance	8,491,093	7,991,069	6.3%
In indirect insurance	36,399	37,412	(2.7)%
Gross written premium in life insurance	6,751,770	6,512,541	3.7%
Individual premiums	2,401,961	2,342,210	2.6%
In direct insurance	2,401,961	2,342,210	2.6%
Group insurance premiums	4,349,809	4,170,331	4.3%
In direct insurance	4,349,809	4,170,331	4.3%
Gross written premium	**15,279,262**	**14,541,022**	**5.1%**

Investment result

Investment income for the 12 months ended 31 December 2011 and 31 December 2010 was PLN 1,593.8 million and PLN 2,777.8 million, respectively (including investment contracts, i.e. contracts which do not include significant risk insured).

Investment result

PLN' 000

Investment result	2011	2010	% change
Interest income	1,835,917	1,772,869	3.6%
Dividend income	122,148	77,655	57.3%
Income from investment properties	27,256	19,940	36.7%
Foreign exchange differences	28,610	(17,178)	-
Other	(43,677)	(28,768)	-
Total net investment income	**1,970,254**	**1,824,518**	**8.0%**
Net income on realized investments	(75,196)	303,152	-
Impairment allowance	(112,051)	(103,701)	-
Total net result on realized investments and impairment losses	**(187,247)**	**199,451**	**-**
Net change in fair value of assets and liabilities measured at fair value	**(189,181)**	**753,805**	**-**
Investment income	**1,593,826**	**2,777,774**	**(42.6)%**

The drop in the „net change in fair value of assets and liabilities measured at fair value" of PLN 943.0 million was caused mainly by a drop in prices of equity instruments on financial markets: the WIG index dropped by 20.8% in 2011, whereas in 2010 it grew by 18.8%.

Net income on realized investments was PLN 386.7 million lower than in the previous year, which was also due to a drop in the prices of equities on the financial markets in 2011.

The increase in new investment income of PLN 145.7 million was due to the impact of foreign exchange differences on financial instruments denominated in EUR: in 2011 the PLN weakened by 3.1% against the EUR on an annual average basis, contrary to the PLN's strengthening against the EUR by 1.7% in 2010. In 2011 interest income, dividend income and investment property income were also higher than in the previous year.

The PZU Group's investing activities are conducted by applying an appropriate degree of safety, liquidity and profitability. What is more, the PZU Group Companies don't apply hedge accounting.

Debt securities issued by sovereign governments as at 31 December 2011 and 31 December 2010 constituted approximately 75% of the investment portfolio and Polish government bonds dominated the portfolio. At the same time, the PZU Group had debt securities issued by other sovereigns in its portfolio (Germany – 1% share of its financial assets, Lithuania – 0.3%, Iceland – 0.1% and Ukraine and Hungary – 0.01% each).

The drop in the share and value of equities was mainly due to the drop in their market value in 2011.

Structure of the financial asset portfolio

PLN' 000

Portfolio structure	2011	2010	Structure 2011	Structure 2010
Debt securities, including:	**35,195,032**	**35,200,159**	**74.4%**	**76.9%**
issued by sovereign governments	34,716,308	34,291,519	73.4%	74.9%
Other	478,724	908,640	1.0%	2.0%
Equity instruments	**5,160,350**	**5,741,732**	**10.9%**	**12.5%**
quoted on regulated market	2,507,136	3,083,846	5.3%	6.7%
other (participation units, investment certificates, unquoted shares)	2,653,214	2,657,886	5.6%	5.8%
Debt, reverse repo transactions, term deposits with financial institutions	**6,334,782**	**4,296,170**	**13.4%**	**9.4%**
Investment property	**534,222**	**441,014**	**1.1%**	**1.0%**
Other	**85,195**	**106,971**	**0.2%**	**0.2%**
Total	**47,309,581**	**45,786,046**	**100.0%**	**100.0%**

Claims

A drop in net claims paid (PLN 162.9 million, i.e. 1.6%) was noted exclusively in the non-life segment. In the life insurance segment the following had an impact on the increase in net claims paid and on the movement in technical reserves of PLN 115.3 million (2.5%) in 2011:

- 6.6% higher claims paid;
- lower provisions where investment risk is borne by the policyholder in 2011 (a loss on investments in this group of investments) compared with a strong increase in 2010.

In the non-life insurance segment, the drop was related to a significant decrease in property insurance, and it resulted mainly from the absence of claims in respect of natural disasters which took place in 2010 (intense snowfall in Q1 2010 and flooding in the second quarter of 2010).

Acquisition and administrative expenses

In 2011 acquisition costs increased by PLN 50.7 million (+2.7%) compared with 2010. The increase resulted mainly from changes in sales in the non-life segment related to:

- higher written premium;
- changes in the structure of distribution channels (greater share of channels charging commissions offset by a drop in channels not charging commissions and automatic renewals);
- changes in sales in recent years by introducing additional bonuses to support the effectiveness of agents and making their compensation conditional on achieving goals (super commission; in 2011 their role increased and they were implemented in new channels).

The drop in administrative expenses of PLN 121.9 million (-8.1%) was to a large extent the effect of restructuring activities conducted in PZU Group companies, which covered the Head Office, regional branches and specialized entities in the PZU Group companies. In 2011 the headcount restructuring program started two years ago was continued; it aimed at improving operating efficiency in claims handling, centralizing day-to-day policy handling and creating new customer service standards (establishing an EU Group Network Department) which resulted in a significant decrease in the fixed costs of current operations. Moreover, the continuation of the fixed costs optimization program brought about positive effects and enabled expenses to be reduced in many areas, such as administration (office stationery, postal services), real property management (costs of cleaning) and IT costs.

Other operating income and expenses

The balance of other operating income and expenses deteriorated by PLN 62.4 million in 2011 compared with the previous year (movement from PLN -212.1 million to PLN -274.5 million). The main reasons for this movement were as follows:

- setting up a provision for reorganization and restructuring of PLN 96.8 million;
- adjusting the estimated settlements of reinsurers' commissions and profit sharing of PLN 91.8 million;
- setting up a provision for the costs of the penalty imposed by the Office for Competition and Consumer Protection („UOKiK") for applying the practice of limiting competition on the domestic market in selling group accidental insurance to children, adolescents and personnel in educational establishments of PLN 56.6 million; and
- starting the consolidation of the Armatura Capital Group under the full method in the consolidated financial statements of the PZU Group, which led to recognizing one-off revenue of PLN 118.9 million in 2011.

Results and business ratios of the PZU Group

In 2011 operating profit amounted to PLN 2,956.7 million and was 4.3% lower than in the previous year, which resulted mainly from the lower results on investing activity (- 42.6%). The drop was largely offset by a 4.8% increase in net premium earned and a drop in net insurance claims and benefits of 1.6%.

Data from the consolidated income statement of the PZU Group

PLN' 000

Data from the consolidated income statement	2011	2010	% change
Gross written premium	15,279,262	14,541,022	5.1%
Net premium earned	14,890,528	14,213,013	4.8%
Fee and commission income	281,351	288,037	(2.3)%
Net result on investing activities	1,593,826	2,777,774	(42.6)%
Net claims and benefits	(10,221,122)	(10,384,062)	(1.6)%
Acquisition costs	(1,961,986)	(1,911,255)	2.7%
Administrative expenses	(1,383 897)	(1,505,784)	(8.1)%
Operating profit/(loss)	2,956,727	3,088,085	(4.3)%
Profit/(loss) before tax	2,907,575	3,029,431	(4.0)%

PLN' 000

Data from the consolidated income statement – cont.	2011	2010	% change
Net profit	2,343,947	2,439,229	(3.9)%
Profits (losses) of minority interests	(1,477)	(2)	x
Basic and diluted weighted average number of ordinary shares outstanding	86,352,300	86,352,300	
Basic and diluted earnings per ordinary share (in PLN)	27,16	28,25	(3.8%)

Data from the consolidated cash flow statement of the PZU Group

PLN' 000

Data from the consolidated cash flow statement	2011	2010	% change
Net cash from operating activities	1,587,572	469,423	238.2%
Net cash from investing activities	(288,686)	5,329,478	(105.4)%
Net cash from financing activities	(1,485,832)	(5,727,985)	(74.1)%
Net increase/(decrease) in cash and cash equivalents	**(186,946)**	**70,916**	**(363.6)%**

Basic profitability ratios of the PZU Group

Gross written premium	2011	2010	% change
Return on equity (ROE) (net profit/loss /average equity*) x 100%	18.3%	20.3%	(2.0) p.p.
Return on assets (ROA) (net profit/loss /average assets*) x 100%	4.6%	4.7%	(0.1) p.p.
Administrative expense ratio (administrative expenses / net premium earned)	9.3%	10.6%	(1.3) p.p.
Sales margin (net profit (loss)/ gross written premium)x100%	15.3%	16.8%	(1.5) p.p.

Analysis of assets and liabilities

The main component of assets are investments (financial assets and investment property) comprising 90.8% of total assets. As at the end of 2011 they amounted to PLN 47,309.6 million, which is an increase of 3.3% compared with the balance as at the end of 2010. The increase in the balance of financial assets as at the end of 2011, despite the drop in the prices of shares quoted on the capital markets, was a consequence of business development.

Equity was 0.5% higher than in the previous year and amounted to PLN 12,869.5 million.

The key component of total liabilities and equity were technical provisions, which comprised approximately 62.4% of the total balance sheet value. As at the end of 2011 they amounted to PLN 32,522.7 million, which is an increase of 2.2% compared with the balance as at the end of 2010. The increase in these provisions as at the end of 2011 was due to an increase in gross written premium in motor TPL insurance in the mass client segment (+13.1%) and an increase in claims in this segment.

The increase in the balance compared with 31 December 2010 resulted mainly from liabilities to credit institutions of PLN 758.9 million in respect of sell-buy-back transactions.

Main balance sheet items of the PZU Group

PLN' 000

Main balance sheet items	2011	2010	% change
ASSETS, including	52,129,282	50,670,557	2.9%
Financial assets	47,309,581	45,786,046	3.3%
Receivables	1,734,636	1,734,274	0.0%
LIABILITIES AND EQUITY, including:	52,129,282	50,670,557	2.9%
Equity	12,869,505	12,799,926	0.5%
Technical reserves	32,522,729	31,822,990	2.2%
Investment contracts	3,471,772	3,544,515	(2.1)%
Liabilities	1,797,521	1,133,822	58.5%
Accruals and deferred income	686,957	482,143	42.5%

Material off-balance sheet items

As at 31 December 2011, the Group had PLN 86.0 million of disputed claims which were not approved by PZU Group companies and which are to be litigated by the creditors. As at 31 December 2010, disputed claims amounted to PLN 127.1 million.

Under a guarantee line agreement dated 26 September 2008 concluded by and between PZU and Bank Millennium SA, the bank grants bank guarantees (both in terms of bid bonds and performance bonds) to PZU in tenders for insurance services. The guarantee line is PLN 15.0 million and every year it is renewed for another year. As at 31 December 2011, 33 bank guarantees were in force under the guarantee line, for a total of PLN 6.4 million. Moreover, as at 31 December 2011 PZU had a warranty in respect of an agency agreement from Raiffeisen-Leasing Polska S.A. in the amount of PLN 11.0 million.

Solvency margin

In accordance with the Act on insurance activities, an insurer with its registered office in the territory of the Republic of Poland is obliged to have own funds no lower than the solvency margin and no lower than the guarantee capital. There are no regulations that would define the calculation of the solvency margin and the amount of own funds for a capital group and therefore these data are presented below separately for PZU and PZU Życie.

The solvency margin and the amount of own funds were calculated on the basis of Polish accounting standards and the requirements of the Regulation of 28 November 2003 on computing the solvency margin and the minimum guarantee capital for insurance sections and sub-sections (Journal of Laws, No. 211 of 2003, Item 2060 as amended).

Calculation of own funds to cover PZU's solvency margin (according to PAS)

Specification	2011	2010	Change
Coverage of technical reserves with assets ratio (Assets covering technical reserves / technical reserves) x 100%	127.0%	127.4%	(0.3) p.p.
Solvency margin (PLN '000)	1,338.8	1,338.8	-
Coverage of the solvency margin ratio	686.6%	716.6%	(30.0) p.p.
Guarantee capital (PLN '000)	446.3	446.3	-
Coverage of the guarantee capital ratio	2059.8%	2149.7%	(89.9) p.p.

Calculation of own funds to cover PZU Życie's solvency margin (according to PAS)

Specification	2011	2010	Change
Coverage of technical reserves with assets ratio (Assets covering technical reserves / technical reserves) x 100%	106.9%	112.4%	(5.5) p.p.
Solvency margin (PLN '000)	1,715.2	1,698.1	17.1
Coverage of the solvency margin ratio	332.5%	367.0%	(34.5) p.p.
Guarantee capital (PLN '000)	571.7	566.0	5.7
Coverage of the guarantee capital ratio	997.6%	1007.6%	(10.0) p.p.

Impact of one-off events on operating results

Consolidation of the Armatura Capital Group

As of 1 January 2011 the consolidated data of the Armatura Group („Armatura Group", covering the data of the following entities – Armatura Kraków SA, Armatoora SA, Armatoora i wspólnicy sp. k. and Armagora SA) are consolidated under the full consolidation method in the consolidated financial statements of the PZU Group. Consolidation of the Armatura Group is the effect of its exceeding materiality levels adopted by the PZU Group for the purpose of consolidated reporting.

In the table below, the key items of the consolidated statement of financial position of the Armatura Group with reconciliation to the consolidated net assets of the Armatura Group as at 1 January 2011 (measured according to the PZU Group accounting principles).

Structure of assets of the Armatura Group

PLN' 000

Reconciliation of net assets of the Armatura Group as at 1 January 2011	Value
Property, plant and equipment	159,199
Investment properties	23,767
Receivables	102,419

PLN' 000

Reconciliation of net assets of the Armatura Group as at 1 January 2011 – cont.	Value
Cash and cash equivalents	1,849
Assets held for sale (investment properties)	76,000
Other assets	123,895
Total assets	**487,129**
Liabilities	(236,582)
Minority interests	(75)
Net assets	**250,472**

The difference between the carrying amount of the shares of Armatura Kraków SA as at 1 January 2011 and the share of the PZU Group in the net assets of the Armatura Group of PLN 118.9 million was recognized in the financial results for 2011 and disclosed in „Other operating income" of the consolidated income statement.

Impact of the consolidation of the Armatura Group on the consolidated results of the PZU Group

PLN' 000

Impact of the consolidation of the Armatura Group on the consolidated results of the PZU Group	Value
Carrying amount of shares of Armatura Kraków SA (measurement at the historical purchase cost net of impairment)	42,952
Value of consolidated net assets of the Armatura Group as at 1 January 2011	250,472
Share of the PZU Group in consolidated net assets of the Armatura Group as at 1 January 2011 (64.6250%)	161,868
Effect on the consolidated financial results of the PZU Group	**118,916**

Changes in investments in subsidiaries

Capital restructuring of insurance companies in the Ukraine

In 2011 the capital restructuring of the Ukrainian companies of the PZU Group was completed. In connection with the resolution of the Extraordinary Shareholder Meeting of PrJSC IC PZU Ukraine and PrJSC IC PZU Ukraine Life Insurance, on 18 January 2011 PZU concluding the following:

- a sales agreement with PZU Ukraine of 29,207,233 shares of UAH 7.19 each, amounting to UAH 210,000 thousand (the equivalent of USD 26,448 thousand - PLN 75,380 thousand) was received on 31 January 2011);
- a sales agreement with PZU Ukraine Life Insurance of 139,991 shares of UAH 21.43 each, amounted to UAH 3,000 thousand (the equivalent of USD 378 thousand - PLN 1,077 thousand) was received on 31 January 2011);

On 2 February 2011, based on the above agreements, PZU transferred ownership rights to the shares to their acquirers.

The remaining 27,998 shares in PZU Ukraine Life Insurance, which were to be redeemed, were purchased from another shareholder - PZU Ukraine (based on an agreement concluded on 18 January 2011).

The decrease in share capital was registered by the Securities and Capital Markets Commission of Ukraine on 28 April 2011.

Moreover, in 2011, under the capital restructuring process, the additional capitalization of the Ukrainian PZU Group was done without the participation of PZU – shares in the life insurance company were taken up by the non-life insurance company increasing its previous interest and the shares in the non-life insurance company were taken up by the life insurance company, thus becoming its shareholder. The process was registered on 13 October 2011. As a result of the share issues, PZU's direct interest in the capital and voting rights of the Ukrainian companies of the PZU Group changed (interest in the share capital of the non-life insurance company is currently 89.9678%, and in the life insurance company – 53.4723%). Indirectly, PZU still controls 100% of the Ukrainian companies' capital and voting rights.

To simplify the ownership structure of PrJSC IC PZU Ukraine and to optimize the costs of the PZU Group, on 1 December 2011 a share sales agreement was concluded for the sale of shares in this company held by PZU CO to PrJSC IC PZU Ukraine Life Insurance. As a result of the transaction, PZU CO retracted its equity exposure from the Ukrainian market.

Capital deficit in PZU Ukraine Life Insurance

As a result of decreasing the share capital, and the consecutive significant increase in the EUR/UAH exchange rate, PZU Ukraine Life Insurance stopped meeting the minimum share capital requirement which the Ukrainian Insurance Act specifies for insurance companies, i.e. EUR 1,500 thousand (in accordance with the binding EUR/UAH exchange rate, as at 31 March 2011 the requirement amounted to UAH 16,823 thousand, which leads to a capital deficit of UAH 622 thousand as at that date).

On 18 April 2011, at the meeting of the Supervisory Boards of PZU Ukraine and PZU Ukraine Life Insurance, a plan of mutual additional capitalization of the companies was presented in the amount of approximately UAH 8,000 thousand each, in such manner that the shares of PZU Ukraine Life Insurance would be taken up by PZU Ukraine and vice versa. This transaction was intended to enable meeting the license requirements without the additional involvement of PZU funds.

On 30 June 2011, on the basis of the recommendation of their Supervisory Boards, the Extraordinary Shareholder Meeting of PZU Ukraine and PZU Ukraine Life Insurance passed resolutions on:

- increasing the share capital of PZU Ukraine Life Insurance by UAH 2,500 thousand, and equity of UAH 7,872 thousand by issuing 25,000 shares with a nominal value of UAH 100.00 per share and an issue price of UAH 314.88 per share,
- increasing the share capital of PZU Ukraine by UAH 1,800 thousand, and equity of UAH 7,517 thousand by issuing 180,000 shares with a nominal value of UAH 10.00 per share and an issue price of UAH 41.76 per share.

On 16 September 2011 the PZU Group's Ukrainian companies concluded share purchase agreements in accordance with the terms and conditions described above. The respective Articles of Association accounting for the capital increases were registered on 26 September 2011, and on 13 October 2011 share registration certificates were issued. The increased share capital of PZU Ukraine is UAH 17,954 thousand, and of PZU Ukraine Life Insurance - UAH 18,701 thousand.

Commentary to segment reporting

Property and casualty (non-life) insurance

Income statement data – non-life insurance

PLN' 000

Income statement data – non-life insurance	2011	2010	% change
Gross written premium, including:	8,529,156	8,029,327	6.2%
External	8,527,492	8,028,481	6.2%
Intrasegmental	1,664	846	96.7%
Net premium earned	8,138,989	7,700,289	5.7%
Net result on investing activities*	2,650,750	4,086,694	(35.1)%
Net claims and benefits	(5,507,572)	(5,779,968)	(4.7)%
Acquisition costs	(1,539,194)	(1,510,903)	1.9%
Administrative expenses	(696,851)	(748,725)	(6.9)%
Operating profit/(loss)	**2,726,518**	**3,613,184**	**(24.5)%**

* including dividend from PZU Życie of PLN 1,987,282 thousand in 2011 and PLN 3,120,000 thousand in 2010, respectively.

In the non-life sector, 96.7% of gross written premium (excluding intrasegmental adjustments) constituted premium collected by PZU. The remaining share comprised premium written by PZU Ukraine and PZU Lietuva.

As of 1 January 2011, PZU introduced a change consisting of recognizing revenue from premium written on the date of concluding the insurance contract instead of on the date of commencement of insurance cover. Additionally, the date of recognizing commission expense relating to the underwritten contracts was changed in an identical manner.

The change had no impact on the consolidated results or on the consolidated net assets of the PZU Group as it was offset by changes in the principles for calculating unearned premium reserves and for deferring acquisition costs.

Gross written premium in the non-life segment (after intrasegmental adjustments) for the year ended 31 December 2011 and 31 December 2010 amounted to PLN 8,527.5 million and PLN 8,028.5 million, respectively. Motor insurance constituted 62.8% of the premium collected by PZU, i.e. 0.5 p.p. more than in 2010. Sales of motor TPL insurance increased by PLN 295.0 million – in the mass client segment +13.1%, and in the corporate client segment +2.0% - mainly due to the increases in tariffs effected in 2010. In motor own damage insurance, written premium increased by PLN 36.8 million – in the mass client segment, premiums increased by 3.8%, and in the corporate client segment dropped by 3.4% in connection with the profitability improvement policy (verification of unprofitable clients).

Written premium recognized by date of underwriting the policy – non-life segment

PLN' 000

Gross written premium by product groups	2011	2010	% change
Motor TPL insurance, including:	2,890,917	2,595,912	11.4%
– individual*	2,485,857	2,198,602	13.1%
– corporate	405,060	397,310	2.0%
Motor own damage insurance, including:	2,285,214	2,248,430	1.6%
– individual*	1,640,540	1,581,230	3.8%
– corporate	644,674	667,200	(3.4)%
Total motor insurance	5,176,131	4,844,342	6.8%
Fire and other property damage insurance	1,723,671	1,621,623	6.3%
Other TPL insurance (cat. 11, 12, 13)	518,258	493,874	4.9%
Accident insurance and others**	829,181	820,662	1.0%
Total non-life insurance net of motor insurance	3,071,110	2,936,159	4.6%
Total PZU	**8,247,241**	**7,780,501**	**6.0%**
Foreign operations***	281,915	248,826	13.3%
Total non-life	**8,529,156**	**8,029,327**	**6.2%**

* Including SMEs.
** This item includes loan guarantees and other financial insurance, travel insurance, assistance insurance, maritime, rail and air transport insurance.
*** Gross written premium recognized by date of assuming liability by PZU Ukraine and PZU Lietuva.

Written premium recognized by date of assuming insurance liability – non-life segment

PLN' 000

Gross written premium by product groups	2011	2010	% change
Motor TPL insurance, including:	2,928,946	2,590,946	13.0%
– individual*	2,505,077	2,208,286	13.4%
– corporate	423,869	382,659	10.8%
Motor own damage insurance, including:	2,338,058	2,257,857	3.6%
– individual*	1,669,860	1,582,082	5.5%
– corporate	668,198	675,776	(1.1)%
Total motor insurance	5,267,004	4,848,803	8.6%
Fire and other property damage insurance	1,712,046	1,625,210	5.3%
Other TPL insurance (cat. 11, 12, 13)	525,274	488,051	7.6%
Accident insurance and others**	766,051	821,872	(6.8)%
Total non-life insurance net of motor insurance	3,003,370	2,935,133	2.3%
Total PZU	**8,270,374**	**7,783,936**	**6.2%**
Foreign operations	281,915	248,826	13.3%
Total non-life	**8,552,290**	**8,032,762**	**6.5%**

* Including SMEs.
** This item includes loan guarantees and other financial insurance, travel insurance, assistance insurance, maritime, rail and air transport insurance.

The drop in claims in the non-life sector of PLN 272.4 million resulted mainly from the absence of large natural disaster claims (in particular compared with the snow and flood claims in 2010). In the first half of the year the number of claims related to the effects of the poor condition of crops after winter increased, but had an insignificant effect on the results.

Income from investing activities in the non-life segment, adjusted by the dividend received from PZU Życie in 2011 and in 2010 amounted to PLN 663.5 million and PLN 966.7 million, respectively. The drop in the „net change in fair value of assets and liabilities measured at fair value" was caused mainly by the bear conditions on the financial markets in 2011 (in 2011 the WIG index dropped by 20.8% in 2011, whereas in 2010 it grew by 18.8%). This drop was partly offset by an increase in „Net investment income" net of the dividend from PZU Życie (an increase of PLN 95.4 million) – the effect of the positive impact of foreign exchange differences on interest income on financial instruments denominated in EUR (in 2011 the PLN weakened against the EUR by 3.1% on an annual average basis contrary to its strengthening against the EUR of 1.7% in 2010).
In 2011 acquisition costs in the non-life segment increased by PLN 28.3 million (+1.9%) compared with the previous year as a result of an increase in sales, changes in the structure of distribution channels (an increase in the share of channels charging commissions compared with automatic renewals without charging commissions) and an increase in supercommissions (supercommissions supporting agent effectiveness and multi-agents conditioning their compensation on the achievement of assumed goals and sales profitability).

In 2011 a model for allocating indirect costs to particular insurance products according to activity based costing (ABC method) was implemented in PZU, which led to transfers of particular costs between cost categories such as acquisition, administration, claims handling and investing activities. This has no impact on the overall volume of the indirect costs.

The purpose of implementing ABC cost allocation is as follows:
- to determine more precisely the actual costs of the products offered by PZU;
- to determine more precisely the actual overhead cost markups (and the rules for their allocation) charged to various products.

In the non-life segment the ABC method led to changes in the cost structure in 2011 and 2010:

- administrative expenses dropped by PLN 245.6 million and PLN 221.7 million, respectively;
- acquisition costs increased by PLN 133.5 million and PLN 125.3 million, respectively;
- claims handling costs increased by PLN 103.4 million and PLN 89.1 million, respectively;
- other costs increased by PLN 8.7 million and PLN 7.3 million, respectively.

The deterioration in the balance of other operating income and expenses of PLN 185.4 million was mainly due to:

- adjusting the estimated settlements of reinsurers' commissions and profit sharing of PLN 91.8 million;
- setting up restructuring provisions of PLN 73.3 million;
- setting up provisions for the costs of the penalty imposed by the Office for Competition and Consumer Protection („UOKiK") for applying the practice of limiting competition on the domestic market for sales of group accidental insurance to children, adolescents and personnel in educational establishments Note 52.1.2 of PLN 56.6 million.

Operating profit in the non-life insurance segment in 2011 and in 2010 amounted to PLN 2,726.5 million and PLN 3,613.2 million, respectively. The PLN 886.7 million (24.5%) drop resulting from deteriorated results on investing activities (mainly lower dividend received from PZU Życie and a drop in prices of financial instruments on the capital markets) and higher other operating expenses was partly offset by an increase in net premium earned and lower claims.

Impact of one-off events on operating results

In 2011, in the property insurance segment, no one-off events were noted which would have an impact comparable to those in the previous year (flood and snow claims). The events with a significant impact on the results for the period comprised.

- payment of claims in crop insurance – frost and poor crop conditions after winter of PLN 128.4 million;
- setting up a provision for disputed settlements in respect of reinsurers' commissions and profit sharing of PLN 91.8 million;
- setting up provisions for the costs of the penalty imposed by the Office for Competition and Consumer Protection for applying a practice of limiting competition on the domestic market for sales of group accidental insurance to children, adolescents and personnel in educational establishments of PLN 56.6 million.

Assets covering technical reserves according to PAS - PZU

The list of PZU's assets covering technical provisions according to PAS as at 31 December 2011 is presented below. The requirements for covering technical provisions with assets are specified in art. 154 and 155 of the Act on insurance activities. As at the end of 2011, the degree of coverage of the technical provisions with assets amounted to 127.0% (130.4% as at the end of 2010).

The increase in gross written premium of PLN 239.2 million (3.7%) resulted mainly from the development of group protection insurance (an increase in average premiums and in the number of insureds) and from the growing sales of endow-

Assets covering technical provisions in PZU

PLN' 000

Description	Total at yearend 2011	% of provisions	Maximum limit %
A. Technical provisions	**14,572,028**	**100.0%**	
B. Total assets	**18,510,626**	**127.0%**	
1. Securities and bonds issued, backed or guaranteed by the State Treasury, local authorities or associations of local authorities	14,717,777	101.3%	no restrictions
2. Other fixed-income securities	191,904	1.3%	10%
3. Shares	817,691	5.6%	40%
4. Properties or their parts, with the exclusion of properties or their parts used for internal purposes	68,672	0.5%	25%
5. Bank deposits	1,022,963	7.0%	no restrictions
6. Receivables	695,034	4.8%	25%

Assets covering technical provisions in PZU – cont.

PLN' 000

Description	Total at yearend 2011	% of provisions	Maximum limit %
7. receivables from the State	5,476	0.0%	no restrictions
8. fixed assets other than properties, if they are depreciated at rates determined according to the prudence principle	86,693	0.6%	5%
9. Cash and cash equivalents	72,895	0.5%	3%
10. Deferred acquisition costs	493,180	3.4%	no restrictions
11. Ceded technical reserves	338,341	2.3%	25%
C. Excess/(shortage) of assets for covering the technical provisions	**3,938,598**	**27.0%**	

* The given maximum limit is the maximum limit for covering technical provisions in receivables from assignors, reinsurers, insurants, insurance intermediaries and the ceded share of technical reserves, in total.

Life insurance

Income statement data – life insurance

PLN' 000

Income statement data – life insurance	2011	2010	% change
Gross written premium	6,751,770	6,512,541	3.7%
Net premium earned	6,752,929	6,514,124	3.7%
Net result on investing activities	876,400	1,689,026	(48.1)%
Net claims and benefits	(4,719,185)	(4,603,935)	2.5%
Acquisition costs	(333,984)	(295,695)	12.9%
Administrative expenses	(609,106)	(653,399)	(6.8)%
Operating profit/(loss)	**1,880,259**	**2,591,639**	**(27.4)%**

Written premium by product group – life insurance segment

PLN' 000

Written premium by product group – life insurance segment	2011	2010	% change
Group insurance	4,349,809	4,170,331	4.3%
Retail insurance, including:	2,401,961	2,342,210	2.6%
– continued individual insurance	1,829,243	1,797,331	1.8%
– other individual insurance	572,718	544,879	5.1%
Total life insurance segment	**6,751,770**	**6,512,541**	**3.7%**

Written premium by type of payment – life insurance segment

PLN' 000

Written premium by type of payment – life insurance segment	2011	2010	% change
Regular premium	6,522,780	6,356,029	2.6%
Single premium	228,990	156,512	46.3%
Total life insurance segment	**6,751,770**	**6,512,541**	**3.7%**

ment insurance with a single premium in the bancassurance channel. An increase was also noted in premiums collected on Employee Pension Funds and health insurance underwritten in group form. In individually continued insurance premium, growth was achieved mainly due to upselling additional insurance (the number of insureds dropped, mainly in type D, a closed portfolio of continued insurance). The significant premium growth rate in individual insurance was the result of:

- developing a protection-linked savings and investment product with a regular premium „PZU Plan na Życie" launched in 2010;
- conducting six subscriptions of structured insurance with a single premium PZU „Świat Zysków";
- introducing, in cooperation with Bank Millennium SA, a new individual unit-linked product with a single premium;
- an increase in interest in the IKE (individual pension account) product;
- introducing an additional insurance package „PZU Ochrona Rodziny" (family protection) to the offer.

These changes were partly offset by the expiry of the endowment insurance portfolio underwritten in the 1990s.
The increase in net claims and benefits paid and the change in technical provisions of PLN 115.3 million (2.5%) was due to an increase in payments of endowment benefits of PLN 171.7 million (+55.5%) with a significant drop in provisions in insurance where the investment risk is borne by the policyholder in 2011 (a technical loss in this group of investments) compared with strong growth in 2010.

Gross claims and benefits with a change in gross technical provisions increased by PLN 290.2 million mainly as a result of higher benefits in group protection insurance (limited controlled growth in loss ratio), an increase in endowment benefits in short-term investment products, partly offset by a change in the actuarial provision, higher endowment benefits from insurance underwritten in the 1990s, a drop in benefits in the continued portfolio and a lower value of insurance benefits in the „old portfolio" – benefits in individual juvenile, life and annuity insurance taken over in 1992 from PZU.

The difference in the change in technical provisions (PLN -174.9 million) results mainly from a drop in the balance of provisions where the investment risk in borne by the policyholder in 2011 as a result of a loss on investing activities compared with a significant increase in 2010. This effect was partly offset by a slowing in the rate of conversion of long-term policies into yearly-renewable term insurance in group protection insurance (the conversion effect on technical provisions in group protection insurance in 2011 translated into releasing provisions worth PLN 406.1 million, whereas in the prior year it was PLN 520.3 million), and a faster pace of increase in the actuarial provision in continued insurance due to the ageing of the portfolio.

Income from investing activities in the life segment, adjusted by the dividend received from PTE PZU in 2011 and in 2010 amounted to PLN 876.4 million and PLN 1,689.0 million respectively. The drop in the „net change in the fair value of assets and liabilities measured at fair value" was caused mainly by the bear conditions on the financial markets in 2011 (in 2011 the WIG index dropped by 20.8% in 2011, whereas in 2010 it grew by 18.8%).

Acquisition costs in the life insurance segment in 2011 and 2010 amounted to PLN 334.0 million and PLN 295.7 million, respectively. The 38.3 million (12.9%) change results mainly from:

- an increase in commission paid in respect of group protection insurance as a result of an increase in the portfolio and a growing share of premium underwritten through the brokerage channel, where the growth trend in the share of premium underwritten through this channel in the total gross written premium slowed significantly compared with prior years;
- an increase in commission in protection insurance distributed through the bancassurance channel due to the payment of their share in profits;
- an increase in commission in the savings and investment product with a protection element and regular premium „Plan na Życie" – the commission is prepaid.

Administrative expenses in the life insurance segment dropped by PLN 44.3 million (-6.8%), which was the effect of economizing, including headcount downsizing and the fixed costs optimization program conducted in the PZU Group.

Other net operating income and expenses in the life insurance segment amounted to PLN -86.8 million and PLN -58.5 million in 2011 and 2010, respectively. The net change in the balance of other operating income and expenses of PLN 28.3 million resulted, among other things, from implementing the statutory ban on open pension fund acquisition on the primary and secondary markets, which was connected with discontinuing the distribution (acquisition) agreement with PTE PZU and a loss of part of the income in this respect. Additionally, as at 31 December 2011 the value of the provision for restructuring amounted to PLN 26.0 million, which meant an increase in the said provision of PLN 3.4 million in 2011 (when in 2010 it dropped by PLN 13.4 million).

In 2011 operating profit in the life insurance segment dropped by PLN 711.4 million (27.4%), mainly as a result of losses incurred on the equity part of the investment portfolio.

Impact of one-off events on operating results

In the life insurance segment no one-off events were noted which would have a significant impact on the operating results of the life insurance segment either in 2011 or in 2010.

Assets covering technical provisions according to PAS – PZU Życie

The table below presents a statement of assets covering the technical provisions according to Polish accounting standards in PZU Życie as at 31 December 2011.

The requirements defining the coverage of technical provisions with assets are specified in art. 154 and 155 of the Act on insurance activities. As at the end of 2011, the degree of coverage of the technical provisions with assets amounted to 106.9% (112.4% as at the end of 2010).

Assets covering technical provisions in PZU Życie

PLN' 000

Description	Total at yearend 2011	% of provisions	Maximum limit %
A. Technical provisions	**22,059,093**	**100.0%**	
B. Total assets	**23,570,734**	**106.9%**	
1. Securities and bonds issued, backed or guaranteed by the State Treasury, local authorities or associations of local authorities	17,121,571	0.4%	no restrictions
2. Other fixed-income securities	112,764	0.4%	10%
3. Participation units or investment certificates in investment funds	3,559,863	11.3%	40%
4. Borrowings	60,964	0.3%	5%

Assets covering technical provisions in PZU Życie – cont.

PLN' 000

Description	Total at yearend 2011	% of provisions	Maximum limit %
5. Bank deposits	2,146,588	10.6%	no restrictions
6. Receivables from insurants following from insurance contracts concluded with the exception of receivables which matured more than 3 months ago	46,053	0.2%	25%
7. Cash and cash equivalents	116,926	0.6%	3%
8. Liabilities in respect of transactions concluded on the financial market	(34,735)	(1.0)%	no restrictions
C. Excess/(shortage) of assets for covering the technical provisions	**1,511,641**	**6.9%**	

Investment contracts

Investment contracts concluded by PZU Życie are shown in the segment „Unallocated (consolidation eliminations and other)". Investment contracts are accounted for under the deposit method; consequently, the transaction volumes from investment contracts do not constitute revenues according to IFRS.

Transaction volumes from investment contracts by product group

PLN' 000

Transaction volumes from investment contracts by product group	2011	2010	% change
Group	2,293,916	1,897,092	20.9%
Individual, including:	760,434	890,566	(14.6)%
Individual, continued	-	-	-
Other individual	760,434	890,566	(14.6)%
Total	**3,054,350**	**2,787,658**	**9.6%**

Transaction volumes obtained from investment contracts

PLN' 000

Transaction volumes obtained from investment contracts	2011	2010	% change
Regular payments	7,446	7,136	4.3%
Single payments	3,046,904	2,780,522	9.6%
Total	**3,054,350**	**2,787,658**	**9.6%**

Transaction volumes obtained from investment contracts in 2011 and in 2010 amounted to PLN 3,054.4 million and PLN 2,787.7 million respectively. The PLN 266.7 million (9.6%) increase resulted mainly from higher sales of short-term endowment products both in the banking channel and in the proprietary channel. This change was partly offset by a drop in sales of unit-linked investment products distributed via the banking channel.

Activities in the area of pension funds

Selected results – the pension segment

PLN' 000

Data from the consolidated income statement – pension insurance	2011	2010	% change
Fee and commission income	231,638	246,915	(6.2)%
Net result on investing activities	12,563	16,121	(22.1)%
Acquisition costs	(81,559)	(48,738)	67.3%
Administrative expenses	(73,091)	(93,119)	(21.5)%
Operating profit/(loss)	90,447	122,446	(26.1)%
Net profit/(loss)	**73,735**	**99,571**	**(25.9)%**

Fee and commission income in the pension segment in 2011 and 2010 amounted to PLN 231.6 million and PLN 246.9 million. The PLN 15.3 million (-6.2%) drop resulted mainly from a drop in the level of contributions transferred from ZUS (Social Insurance Institution) to OFE PZU from 7.3% to 2.3% of base pension insurance contributions (as of May 2011).

The increase in acquisition costs of PLN 32.8 million (67.3%) resulted mainly from changes in settling the commission expense and the asset impairment charge made in 2011 in connection with the permanent loss of value resulting from the decrease in contributions transferred by ZUS to OFE PZU. Administrative expenses of PTE PZU dropped by PLN 20.0 million (-21.5%), which was mainly the effect of lower costs of the ZUS fee collected on contributions transferred to OFE PZU, and lower payments to the Guarantee Fund.

Operating profit dropped by PLN 32.0 million (-26.1%) and reflected the drop in fee and commission income and increase in operating expenses.

Risk factors which may have an impact on financial results in future periods

Property and personal (non-life) insurance

The risk factors which could have an impact on non-life insurance segment results in 2012 comprise mainly:

- the economic slowdown or stagnation which could give rise to an increased loss ratio on the financial insurance portfolio;
- the possible increase in the unemployment rate in 2012 and lower growth rate of retail consumption translating into a change in demand for insurance products;
- price pressure from competitors;
- higher loss ratios, and specifically the loss frequency;
- an increase in the insurance brokers' role which could lead to higher acquisition costs;
- fluctuations in the return on Treasury securities dependent on the economic position of Poland and European Union countries - a drop in returns on securities could lead to lower investment returns and the potential need to change the technical rates applied by the company;
- the behavior of the capital markets in 2012, and specifically of the WSE – part of the Company's investment income depends on the trends on this market;
- absence of a precisely defined scope of exemptions relating to e.g. medical insurance services in the amended Act of 11 March 2004 on Value Added Tax (Journal of Laws No. 54 of 2004, item 535 as amended);
- possible changes (amended regulations) in the principles of valuation of provisions for the capitalized value of annuities – this could lead to the need to increase the level of prudence and higher provisions;
- the growing average cost of casualty claims resulting from the growing share of non-public healthcare and the impact of monetary compensation on behalf of members of the deceased's family (art. 446 § 4 of the Act of 23 April 1964 the Civil Code (Journal of Laws No. 16 of 1964, item 93 as

amended, „Civil Code")), which could lead to the need to increase provisions in motor TPL insurance;
- the risk of an increase in the number and value of claims from clients and injured parties in connection with the Act of 17 December 2009 on pursuing claims in class action suits (Journal of Laws, No. 7 of 2010, Item 44 as amended);
- changes in bank regulations which may have an impact on the reduction in the number of mortgage loans granted and borrowers' insurance.

Life insurance

The factors which could have an impact on PZU Życie's results in 2012 comprise mainly:
- the possible increase in the unemployment rate in 2012 and lower retail consumption growth rate translating into a change in the demand for insurance products;
- potential increase in competition in group insurance due to an increase in the role of brokers in this segment and the requirement to conduct tender procedures for group insurance by entities subject to the Act of 29 January 2004 on Public Procurement (Journal of Laws, No. 223 of 2007, Item 1655 „Act on Public Procurement");
- changes in the financial intermediation market, slowdown in the growth of popularity of independent financial advisory services thus limiting the number of channels for selling insurance products;
- fluctuations in the return on Treasury securities dependent on the economic position of Poland and European Union countries - a drop in returns on the securities could lead to a drop in investment returns and the potential need to change the technical rates applied by PZU Życie and the amount of European Embedded Value;
- the behavior of the capital markets in 2012, and specifically of the WSE – part of the Company's investment income depends on the trends on this market;
- all changes in universally binding legal regulations or their interpretation in the area of the technical servicing of group insurance by people designated for the task by policyholders;
- changes in the current level of mortality and morbidity.

Pension funds

The risk factors which could have an impact on PTE PZU's results in 2012 comprise mainly:
- possible changes in the pension insurance system leading to a drop in the amount of pension contribution transferred by ZUS to OFE, creating sub-funds and acquisition principles on the market;
- possible increase in the unemployment rate in 2012 translating into a lower number of members joining OFE;
- a low rate of salary growth leading to a lower growth rate in the contributions paid by members of pension funds;
- changes in the financial intermediation market, slowdown in the growth of popularity of independent financial advisory services thus limiting the number of sales channels;
- fluctuations in the return on Treasury securities dependent on the economic position of Poland and European Union countries - a drop in the returns on securities could lead to a drop in the returns on OFE PZU investments and management fees collected by PTE PZU;
- the behavior of the capital markets in 2012, and specifically of the WSE – part of the OFE PZU investment income depends on the trends on this market which translates into the value of assets and amount of management fees collected by PTE PZU.

33. MAIN TABLES FROM THE CONSOLIDATED FINANCIAL STATEMENT

Consolidated statement of financial position

PLN '000

Assets	2011	2010	2009
Intangible assets	166,038	109,067	85,069
Goodwill	8,716	8,381	19,631
Property, plant and equipment	1,055,381	990,411	1,043,811
Investment property	534,222	441,014	346,552
Entities measured using the equity method	-	-	-
Financial assets			
Financial instruments held to maturity	21,659,505	20,305,758	23,327,568
Financial instruments available for sale	7,851,903	8,623,082	10,027,845
Financial instruments measured at fair value through profit or loss	10,814,619	12,118,252	10,213,631
Loans	6,449,332	4,297,940	4,668,549
Receivables, including receivables from insurance contracts	1,734,636	1,734,274	1,495,207
Reinsurers' share in technical provisions	700,713	771,850	748,313
Estimated recoveries and recourses	83,117	77,812	82,330
Deferred tax assets	8,600	16,645	24,913
Current income tax receivables	8,582	9,958	87,599
Deferred acquisition costs	569,843	540,729	518,279
Prepayments	125,890	194,226	215,804
Other assets	120,461	7,455	15,781

PLN '000

Assets – cont.	2011	2010	2009
Cash and cash equivalents	237,724	423,703	366,556
Assets used in continuing operations	**52,129,282**	**50,670,557**	**53,287,438**
Non-current assets held for sale and disposal groups	-	-	-
Total assets	**52,129,282**	**50,670,557**	**53,287,438**

PLN '000

Equity and liabilities	2011	2010	2009
Equity			
Issued share capital and other equity attributable to the shareholders of the parent			
Share capital	86,352	86,352	86,352
Other capitals	7,948,386	6,649,782	5,802,568
Supplementary capital	7,711,818	6,296,313	5,485,014
Revaluation reserve	268,831	392,268	340,970
Exchange differences from translation of controlled entities	(32,263)	(38,799)	(23,416)
Undistributed profit / uncovered loss	4,748,424	6,063,666	5,377,826
Previous year profit (loss)	2,403,000	3,624,435	2,365,282
Net profit (loss)	2,345,424	2,439,231	3,762,945
Appropriations on net profit during the financial year	-	-	(750,401)
Minority interest	86,343	126	133
Total equity	**12,869,505**	**12,799,926**	**11,266,879**
Liabilities			
Technical provisions			
Provision for unearned premiums and for unexpired risks	4,521,396	4,315,675	4,189,849
Life insurance provision	14,595,112	14,570,725	14,582,590
Provisions for outstanding claims	5,429,481	5,157,080	4,456,464
Provision for capitalized value of annuity claims	5,088,626	4,862,552	4,874,653
Provisions for bonuses and rebates for the insured	7,192	6,177	5,071
Other technical provisions	581,155	614,692	698,918

PLN '000

Equity and liabilities – cont.	2011	2010	2009
Unit linked technical provisions	2,299,767	2,296,089	2,017,501
Investment contracts			
– with guaranteed and fixed terms and conditions	2,330,870	2,270,568	2,632,054
– for the client and at the client's risk	1,140,902	1,273,947	1,094,475
Provisions for employee benefits	255,576	257,916	260,946
Other provisions	322,063	212,559	314,595
Provision for deferred income tax	109,716	404,956	444,053
Current income tax liabilities	7,570	1,743	3,056
Derivatives	93,443	11,730	3,533
Other liabilities	1,789,951	1,132,079	5,974,052
Accruals and deferred income			
Cost accruals	669,048	474,272	464,126
Deferred income	17,909	7,871	4,623
Liabilities related to continuing operations	**39,259,777**	**37,870,631**	**42,020,559**
Liabilities directly related to non-current assets classified as held for sale	-	-	-
Total liabilities	**39,259,777**	**37,870,631**	**42,020,559**
Total equity and liabilities	**52,129,282**	**50,670,557**	**53,287,438**

Consolidated income statement

PLN '000

Consolidated income statement	2011	2010
Gross written premiums	15,279,262	14,541,022
Reinsurer's share in the written premium	(285,386)	(200,853)
Net written premium	**14,993,876**	**14,340,169**
Change in net provision for unearned premium	(103,348)	(127,156)
Net earned premiums	**14,890,528**	**14,213,013**
Revenue from commissions and fees	281,351	288,037
Net investment income	1,970,254	1,824,518

PLN '000

Consolidated income statement – cont.	2011	2010
Net profit or loss on realization and impairment loss on investments	(187,247)	199,451
Net change in the fair value of assets and liabilities plus equity measured at fair value	(189,181)	753,805
Other operating revenue	485,481	89,297
Claims and change in technical provisions	(10,373,521)	(10,939,234)
Reinsurers' share in claims and change in technical provisions	152,399	555,172
Net insurance claims	**(10,221,122)**	**(10,384,062)**
Claims and change in measurement of investment contracts	32,512	(177,549)
Acquisition expense	(1,961,986)	(1,911,255)
Administrative expense	(1,383,897)	(1,505,784)
Other operating expense	(759,966)	(301,386)
Operating profit (loss)	**2,956,727**	**3,088,085**
Financial expense	(49,152)	(58,654)
Share in net profit (loss) of entities measured using the equity method	-	-
Gross profit (loss)	**2,907,575**	**3,029,431**
Income tax		
– current portion	(826,397)	(639,298)
– deferred portion	262,769	49,096
Net profit (loss) from continuing operations	2,343,947	2,439,229
Net profit (loss), including:	**2,343,947**	**2,439,229**
– profit (loss) attributable to equity holders of the parent	2,345,424	2,439,231
– minority profits (loss)	(1,477)	(2)
Net profit (loss) from continuing operations	2,345,424	2,439,231
Net profit (loss) from discontinued operations	-	-
Weighted average basic and diluted number of ordinary shares	86,352,300	86,352,300
Basic and diluted profit (loss) on continuing operations per ordinary share (in PLN)	27,16	28,25
Basic and diluted profit (loss) on discontinued operations per ordinary share (in PLN)	-	-
Basic and diluted profit (loss) per ordinary share (in PLN)	27,16	28,25

Consolidated statement of comprehensive income

PLN '000

Consolidated statement of comprehensive income	2011	2010
Net profit (loss)	2,343,947	2,439,229
Other comprehensive income:	(116,887)	35,910
Financial assets available for sale	(162,649)	641
Exchange differences from translation of controlled entities	6,550	(15,388)
Real property reclassified from property, plant and equipment to investment property	39,212	50,657
Net comprehensive income total	**2,227,060**	**2,475,139**
– comprehensive income attributable to holders of the parent's equity	2,228,523	2,475,146
– comprehensive income attributable to equity under discretionary participation features contracts	-	-
– comprehensive income attributable to non-controlling interests	(1,463)	(7)

Consolidated statement of comprehensive income

PLN '000

Statement of changes in consolidated Equity	Equity and provisions attributable to owners of the parent's share capital							Minority interest	Total equity
		Other capitals			Undistributed profit / uncovered loss				
	Share capital	Supplementary capital	Revaluation reserve	Exchange differences from translation	Previous year profit (loss)	Net profit (loss)	Total		
Balance as at 1 January 2011	**86,352**	**6,296,313**	**392,268**	**(38,799)**	**6,063,666**	**-**	**12,799,800**	**126**	**12,799,926**
Change in measurement of AFS financial assets	-	-	(162,649)	-	-	-	(162,649)	-	(162,649)
Exchange differences from translation	-	-	-	6,536	-	-	6,536	14	6,550
Real property reclassified from property, plant and equipment to investment property	-	-	39,212	-	-	-	39,212	-	39,212

PLN '000

Statement of changes in consolidated Equity – cont.	Equity and provisions attributable to owners of the parent's share capital							Minority interest	Total equity
		Other capitals			Undistributed profit / uncovered loss				
Total increases (decreases) recognized directly in net capital (including income tax)	**-**	**-**	**(123,437)**	**6,536**	**-**	**-**	**(116,901)**	**14**	**(116,887)**
Net profit (loss) for the financial year	-	-	-	-	-	2,345,424	2,345,424	(1,477)	2,343,947
Total increases (decreases)	**-**	**-**	**(123,437)**	**6,536**	**-**	**2,345,424**	**2,228,523**	**(1,463)**	**2,227,060**
Other changes, including:	**-**	**1,415,505**	**-**	**-**	**(3,660,666)**	**-**	**(2,245,161)**	**87,680**	**(2,157,481)**
Financial profit distribution/ loss coverage	-	1,415,325	-	-	(3,660,485)	-	(2,245,160)	(2,830)	(2,247,990)
Consolidation of the Armatura Capital Group	-	-	-	-	-	-	-	88,679	88,679
Other	-	180	-	-	(181)	-	(1)	1,831	1,830
Balance as at 31 December 2011	**86,352**	**7,711,818**	**268,831**	**(32,263)**	**2,403,000**	**2,345,424**	**12,783,162**	**86,343**	**12,869,505**

Consolidated statement of cash flows

PLN '000

Consolidated statement of cash flows	2011	2010
Cash flows from operating activities		
Inflows	19,725,868	18,470,571
– gross inflows from insurance premiums	14,929,349	14,521,524
– inflows from investment contracts	3,054,350	2,787,658
– inflows from reinsurance commissions and share in reinsurers' profits	20,513	10,779
– reinsurers' payments due to share in claims	385,775	466,219
– other inflows from operating activities	1,335,881	684,391
Outflows	(18,138,296)	(18,001,148)
– insurance premiums paid due to reinsurance	(174,369)	(154,254)
– paid commissions and profit sharing due to outward reinsurance	(4,679)	(4,152)

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Consolidated statement of cash flows – cont.	2011	2010
– gross claims paid	(9,026,567)	(9,295,988)
– claims paid due to investment contracts	(3,068,852)	(3,026,424)
– outflows due to acquisition	(1,483,488)	(1,450,351)
– administrative outflows	(2,073,279)	(2,135,292)
– interest payments	(146)	(225)
– income tax payments	(904,071)	(110,228)
– other operating outflows	(1,402,845)	(1,824,234)
Net cash flows generated by operating activities	**1,587,572**	**469,423**
Cash flows from investment activities		
Inflows	259,765,786	270,016,909
– disposal of investment property	13,282	-
– inflows from investment property	8,763	5,628
– disposal of intangible assets and property, plant and equipment	27,905	7,859
– disposal of shares	4,372,949	4,416,405
– redemption of debt securities	65,465,651	31,510,882
– withdrawal of term deposits at credit institutions	130,812,922	129,179,172
– cash from other investments	58,512,745	103,641,528
– interest received	450,899	1,191,346
– dividends received	98,101	64,089
– other inflows from investments	2,569	-
Outflows	(260,054,472)	(264,687,431)
– acquisition of investment property	-	(1,329)
– payments for maintenance of investment property	(11,581)	(8,152)
– acquisition of intangible assets and property, plant and equipment	(168,435)	(155,850)
– acquisition of shares	(4,561,634)	(4,561,101)
– decrease in cash balance due to discontinued investment funds consolidation	-	(201)
– acquisition of debt securities	(63,630,331)	(27,390,996)
– acquisition of term deposits at credit institutions	(132,934,922)	(127,601,087)

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Consolidated statement of cash flows – cont.	2011	2010
– acquisition of other investments	(58,733,953)	(104,929,875)
– other payments for investments	(13,616)	(38,840)
Net cash used in/generated by investment activities	**(288,686)**	**5,329,478**
Cash flows from financing activities		
Inflows	39,242,376	578
– loans and borrowings and issues of debt securities	39,242,376	578
Outflows	(40,728,208)	(5,728,563)
– dividends paid to holders of the parent's equity	(2,163,206)	(921,239)
– dividends paid to non-controlling interest	(2,830)	-
– repayment of loans and borrowings and redemption of debt securities	(38,556,267)	(4,807,324)
– interest on credit facilities, loans and issued debt securities	(5,905)	-
Net cash used in financing activities	**(1,485,832)**	**(5,727,985)**
Total net cash flows	**(186,946)**	**70,916**
Cash and cash equivalents at the beginning of the financial year	423,703	366,556
Change in cash due to exchange differences	967	(13,769)
Cash and cash equivalents at the end of the financial year, including:	237,724	423,703
– of limited disposability	26,841	22,426

34. PZU GROUP'S CONTACT INFORMATION

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