



**Consolidated Annual Report of  
Kredyt Bank S.A. Capital Group  
prepared for the year ended  
December 31, 2005**

**(Submitted to the Polish Securities and Exchange Commission on February 28, 2006  
translated from Polish language)**

# THE SECURITIES AND EXCHANGE COMMISSION

## The consolidated annual report RS 2005

(pursuant to &86 item 2 of the Decree of the Council of Ministers dated October 19, 2005 – Journal of Laws No. 209, item 1744)

(for banks)

for the financial year 2005 comprising the period from 2005-01-01 to 2005-12-31  
containing the consolidated financial statement according to the International Standards of Financial Reporting  
Currency: PLN

Date of submitting: 2006-02-28

### KREDYT BANK S.A.

(full name of the issuer)

KREDYTB

(abbreviated name of the issuer)

Finance, Banks

(sector according to the Warsaw Stock Exchange classification)

01-211

(postal code)

Warszawa

(city or town)

Kasprzaka 2/8

(street) (number)

022 634-50-10

(telephone)

022 634-56-77

(fax)

ir@kredytbank.pl

(e-mail)

527-020-40-57

(Tax identification number)

006228968

(Statistical identification number)

[www.kredytbank.pl](http://www.kredytbank.pl)

(www)

	PLN thousand		EURO thousand	
SELECTED FINANCIAL DATA	31.12.2005	31.12.2004	31.12.2005	31.12.2004
I. Net interest	753 447	633 927	187 271	140 305
II. Net commissions and fees	314 890	513 641	78 267	113 683
III. Result on operating activity	320 121	178 773	79 567	39 567
IV. Gross profit (or loss)	321 368	178 774	79 877	39 568
V. Net profit (or loss) falling to the Bank's shareholders	415 878	156 840	103 367	34 713
VI. Minority shares in net profit	0	1 902	0	421
VII. Net total cash flows	-1 673 252	1 788 201	-415 890	395 777
VIII. Total assets	20 841 344	20 946 084	5 399 592	5 135 103
IX. Liabilities due to banks	2 562 167	3 007 090	663 808	737 213
X. Liabilities due to customers	14 533 624	14 061 105	3 765 383	3 447 194
XI. Equity	1 681 595	1 517 088	435 669	371 926
XII. Share capital	1 358 294	1 358 294	351 908	332 997
XIII. Number of shares	271 658 880	271 658 880		
XIV. Book value per 1 share (in PLN/EURO)	6,19	5,58	1,54	1,24
XV. Capital adequacy ratio	16,42	14,72		
XVI. Profit (loss) per 1 ordinary share (in PLN/EURO)	1,53	0,64	0,38	0,14

## **Letter of the President of Kredyt Bank S.A. Management Board**

### **To Shareholders, Customers and Employees,**

In 2005, Kredyt Bank S.A. generated a historically high, consolidated financial result amounting to PLN 415.9 million.

Launched in 2003 process of thorough review of the credit risk management and non-performing loans portfolio recovery, combined with the implementation of a new credit policies, enabled us to minimize the cost of risk impact upon the Group's financial performance.

Reorganized in 2004 support and cost management functions allowed us to reduce the operating costs and generate substantial savings.

The restructuring of sales, completed in 2005, was the third step and a key element allowing for an improvement in revenue generation and having impact on net result. It has enabled us to consolidate positive trends, particularly visible through the results on selected, strategic products, such as investment funds and insurance policies distribution or the sale of mortgage and retail loans.

All the above allowed for an ROE improvement, which if compared to 2004 figures, increased by 11.5%, up to 26%. Also the cost/income ratio decreased by 3.5% and at the end of 2005 amounted to 73%. The high, clearly unsatisfactory level of the latter ratio illustrates the magnitude of effort in efficiency improvement, which is still ahead of us.

The change of the Bank's corporate visualization, which together with the other companies of KBC Group operating in Poland was launched in September 2005, was a very crucial moment, both in business and symbolic terms. The launch marked the first phase of the new Kredyt Bank strategy implementation, which builds on establishing, in cooperation with WARTA insurance group, assuring the maximum advantage of the synergy effect resulting also from the cooperation of all KBC Group companies in Poland.

The objective of Kredyt Bank in the year 2006 is to fully implement opportunities resulting from the cooperation with WARTA S.A., Żagiel S.A. and Kredyt Lease S.A. Expansion of the Bank's network by 120 new units planned for the next three-year period will improve the access to products offered by the Bank and its partners.

I am convinced that the implementation of this strategy will enable us to increase our share in the Polish financial services market and develop our potential to a greater extent. We plan to achieve it with respect of our values being a partnership, understanding and responsibility.

I would like to thank all our employees and of our subsidiaries for their commitment and contribution to our performance in 2005. They were essential for the achievement of our business objectives.

*Ronnie Richardson*

*President of the Management Board  
of Kredyt Bank S.A.*

**In accordance with the Principle no. 18 of “The corporate governance principles” the Supervisory Board of Kredyt Bank S.A. makes publicly known a brief assessment of financial situation of Kredyt Bank S.A.**

2005 was the second year in a row, when Kredyt Bank S.A. generated the best result in its history since the Bank's net result amounted to PLN 410.5 million. The measurable effects were brought by a process of restructuring of the Bank's basic areas of activity that started in 2004. It primarily comprised the following areas: credit risk, the functioning costs management and organization of sales. It proceeded in close co-operation with and using the experience of KBC Group – the Bank's major shareholder.

The implementation of a new credit policy and a reorganization of credit process as well as credit risk management process allowed to minimize the impact of the risk cost on the Bank's results. The net write-offs by the reason of financial assets impairment and other assets as well as provisions were positive and amounted to PLN 29,623 thousand in 2005. The intensification and improvement in efficiency of vindication and restructuring activities conducted by the separate Irregular Loans Portfolio Management Division isolated from the business area, had a positive impact on the overall Bank's activity. The basic ratios that describe this area, had improved: the share of credits (for which individual circumstances of impairment were identified) in total customers' receivables dropped from 28.0% to 26.0%, the coverage ratio of these receivables by provisions increased from 60.8% to 70.8%.

The control of costs was the second basic factor conditioning the improvement of the results generated. The reorganization and centralization of costs management function carried out in 2004, implementation of new principles of making procurement decisions and investments as well as the re-negotiation of the significant contracts allowed to substantially decrease the costs of the Bank's functioning for the second time in a row. This item (i.e. costs of functioning) decreased by 7.5% as compared with the year of 2004. As a result the cost/income ratio further improved, falling from 80.9% to 74.2%.

On April 25, 2005 the General Assembly of Kredyt Bank S.A. decided to cover a last portion of the loss incurred over the years 2002 – 2003 disclosed in 2004 financial statement and amounting to PLN 588.9 million, which was a significant event of 2005. The positive tendencies with respect to operating results generated by the Bank affirm a high probability of settlement of the tax losses that have cumulated over the previous years. Due to that reason, as of December 31, 2005, the Bank recognized a surplus of assets over the provision by the reason of deferred income tax amounting to PLN 102.2 million, which had a material impact on the Bank's 2005 net result. High values of capital adequacy ratio, which over the quarters from I to IV were equal to 13.3%, 14.4%, 16.2% and 16.2%, respectively, affirm the Bank's stable situation as well as the existence of a solid base for the further development of activity.

The restructuring activities in the years of 2004 and 2005 conducted in the area of sales organization, consisting in the separation of administration functions from

business functions as well as the implementation of segmentation, brought positive results in the area of attracting customers' funds in 2005. In comparison with 2004 a significant growth was observed in the sale of the selected, strategic deposit products. Attention should be also drawn to a very dynamic growth of investment funds assets offered jointly with KBC TFI and WARTA, being an alternative for the customers' traditional deposits.

A summary of processes that were taking place in 2005 is a formulation of the Bank's new strategy. Its main assumption is the development of bancassurance and the establishment of the banking and insurance group in co-operation with WARTA S.A., applying the knowledge and experience of their major shareholder, i.e. KBC Group. The first step was a process of visualization of the Bank's logo that started in September 2005. Kredyt Bank S.A., WARTA S.A. and other entities from KBC Group in Poland introduced similar logotypes with the colouring and graphics similar to those of KBC logo. At the same time a process has been started to make uniform the décor of units and changes in the product offer aimed at the improvement of logo identification and securing for the customers an access "under one roof" to all products offered by the companies from KBC Group operating in Poland.

The improvement of the Bank's condition was affirmed by upgrading the ratings assigned by the rating agencies – Moody's Investors Service and Fitch Ratings. The changes in the basic ratios and financial figures obtained in 2005 justify a positive assessment of the Bank's financial situation as well as the activities conducted in order to assure the stable and safe foundations to generate profits and stimulate a further growth.

The Supervisory Board

## **Independent Auditor's Opinion**

### **To the Supervisory Board of Kredyt Bank S.A.**

1. We have audited the attached consolidated financial statements for the year ended 31 December 2005 of Kredyt Bank S.A. Capital Group ("Group"), for which the holding company is Kredyt Bank S.A. located at Warsaw, Kasprzaka 2/8 street, including:
  - the consolidated profit and loss account for the period from 1 January 2005 to 31 December 2005 with a net profit amounting to 415,878 thousand zlotys,
  - the consolidated balance sheet as at 31 December 2005 with total assets amounting to 20,841,344 thousand zlotys,
  - the consolidated statement of changes in shareholders' equity for the period from 1 January 2005 to 31 December 2005 with a net increase in shareholders' equity amounting to 423,395 thousand zlotys,
  - the consolidated cash flow statement for the period from 1 January 2005 to 31 December 2005 with a net cash outflow amounting to 1,673,252 thousand zlotys, and
  - the additional notes and explanations ("the attached consolidated financial statements").
2. The truth and fairness<sup>1</sup> of the attached consolidated financial statements and the proper maintenance of the consolidation documentation are the responsibility of the Bank's Management Board. Our responsibility was to audit the consolidated financial statements and to express an opinion whether, based on our audit, these consolidated financial statements are, in all material respects, true and fair<sup>2</sup>.
3. We conducted our audit of the attached consolidated financial statements in accordance with the following regulations in force in Poland:
  - chapter 7 of the Accounting Act, dated 29 September 1994 ('the Accounting Act'),
  - the auditing standards issued by the National Chamber of Auditors,

in order to obtain reasonable assurance whether these consolidated financial statements are free of material misstatement. In particular, the audit included examining, to a large extent on a test basis, documentation supporting the amounts and disclosures in the attached consolidated financial statements. The audit also included assessing the accounting principles adopted and used and significant estimates made by Management Board, as well as evaluating the overall presentation of the attached consolidated financial statements. We believe our audit has provided a reasonable basis to express our opinion on the attached consolidated financial statements treated as a whole.

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<sup>1</sup> Translation of the following expression in Polish: "rzetelność, prawidłowość i jasność"

<sup>2</sup> Translation of the following expression in Polish: "prawidłowe, rzetelne i jasne"

4. In our opinion, the attached consolidated financial statements, in all material respects:
- present truly and fairly all information material for the assessment of the results of the Group's operations for the period from 1 January 2005 to 31 December 2005, as well as its financial position<sup>3</sup> as at 31 December 2005;
  - have been prepared, in all material aspects, in accordance with International Financial Reporting Standards approved by the European Union;
  - are in accordance with the provisions of laws affecting the content of the attached financial statements.
5. We have read the Directors' Report for the period from 1 January 2005 to 31 December 2005 and the rules of preparation of consolidated annual statements ('the Directors' Report') and concluded that the information derived from the attached consolidated financial statements reconciles with these financial statements. The information included in the Directors' Report corresponds with the relevant regulations of the Decree of the Minister of Finance as at 19 October 2005, on current and periodic information published by issuers of securities (Journal of Law No. 209, item 1744 – "The Decree on current and periodic information").

on behalf of  
Ernst & Young Audit Sp. z o.o.  
ul. Emilii Plater 53  
00-113 Warszawa  
License no. 130

Dorota Snarska-Kuman  
Certified Auditor No. 9667/7232  
Warsaw, 28 February 2006

Dominik Januszewski  
Certified Auditor No. 9707/7255

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<sup>3</sup> Translation of the following expression in Polish: "sytuacja majątkowa i finansowa"

*Capital Group*  
**KREDYT BANK S.A.**

**LONG-FORM REPORT  
SUPPLEMENTING THE INDEPENDENT AUDITORS' OPINION  
ON THE CONSOLIDATED FINANCIAL STATEMENTS FOR THE  
YEAR ENDED 31 DECEMBER 2005**



## **I. GENERAL NOTES**

### **1. Background**

The holding company of the Capital Group Kredyt Bank S.A (hereinafter “the Group”) is Kredyt Bank S.A. (“the holding company”, “the Bank”). The holding company was incorporated on the basis of a Notarial Deed dated 4 September 1990. The Bank’s registered office is located in Warsaw at Kasprzaka 2/8 Street.

The holding company is an issuer of securities described in Art. 4 of European Parliament and European Union Council Decree on application of international accounting standards (Journal of Laws WE L 243 of 11.09.2002, item 1; Journal of Laws UE Polish special edition, chapter 13, t. 29, item 609) and based on Art. 55.6a of Accounting Act dated 29 September 1994 prepares the consolidated financial statements of the Group according to International Financial Reporting Standards which were authorized by EU. This obligation regards consolidated financial statements for the financial year beginning in 2005.

The holding company was entered in the Register of Entrepreneurs of the National Court Register under no. KRS 0000019597 on 12<sup>th</sup> June 2001.

The Bank was issued with tax identification number (NIP) 527-02-04-057 on 14<sup>th</sup> June 1993 and statistical number (REGON) 006228968 on 15<sup>th</sup> 1999.

The holding company belongs to capital group KBC Bank N.V.

The principal activities of the holding company are as follows:

- accepting call (demand) or term deposits and keeping deposit accounts,
- keeping other types of bank accounts,
- extending loans,
- extending bank guarantees and sureties,
- issuing bank securities,
- performing bank settlements in the form recognized in both domestic and foreign banking environment,
- operations including cheques and bills of exchange,
- issuing payment cards and performing operations using such cards,
- performing term financial operations,
- purchase and disposal of debt,
- storing valuable items and securities and renting safe deposit box,
- purchase and sale of foreign exchange,
- intermediation in money transfers and settlements in foreign exchange trade,
- taking over or purchasing shares and rights arising from banks’ shares and other rights from shares from other legal entities or participation units investment funds,
- purchasing securities on own account or third parties, dealing with those securities and keeping securities accounts,
- performing brokerage activities,
- raising liabilities relating to the issue of securities,
- acting as a trustee in dealing with securities, exercising rights arising from these papers on behalf of Banks’ clients,
- performing lease operations, factoring, underwriting, forfaiting,

- managing investments and pension funds, acting as depositary for investment and pension funds, keeping accounting books and members registers for funds,
- insurance agency activities for individuals and corporations,
- acquisition for open pension funds,
- performing ,with compliance to an agreement made with debtor, conversion liabilities to parts of debtor assets taking into account Banking Law,
- acquire and dispose of real property,
- financial consulting and advisory services,
- issuing electronic money instruments.

The operations of the Group's subsidiaries, jointly controlled entities and associates include the following activities:

- Żagiel S.A. – intermediary financial services including sales of goods and services, renting properties and selling materials and goods,
- Kredyt Lease S.A – lease services, renting and leasing of intangibles and fixed assets, real estate trading and acting as an intermediary in selling goods and services,
- Kredyt-Trade Sp. z o.o. – providing developers' services, substitute investments, brokerage services related to real estate, managing and administrating a real estate and technical objects, advisory services and economic and financial expertises, preparing business plans, performing due diligence, organizing and performing trainings,
- Kredyt International Finance B.V. – acquiring capital for the needs of Capital Group Kredyt Bank S.A. on foreign markets,
- PTE KB S.A. – managing Open Pension Fund and represent its action to third parties. On 1 October 2004 the Extraordinary Shareholders' Meeting of PTE KB S.A made a resolution about termination of business activities of the company (opening liquidation),
- Victoria Development Sp. z o. o. – building and administration of real estate.

As at 31 December 2005, the holding company's issued share capital amounted to 1.358.294 thousand zlotys. Group's equity as at that date amounted to 1.659.718 thousand zlotys.

In accordance with Bank's Share Book as at 28 February 2006, the ownership structure of the Bank's issued share capital was as follows:

	Number of shares	Number of votes	Par value of shares	% of issued share capital
KBC Bank N.V. (Brussels)	232.341.875	232.341.875	1.161.709.375	85,53%
Others	39.317.005	39.317.005	196.585.025	14,47%
<b>Total</b>	<b>271.658.880</b>	<b>271.658.880</b>	<b>1.358.294.400</b>	<b>100,00%</b>

According to Banking Supervisory Commission resolution No. 81/KNB/01 taken on 17 September 2001 KBC Bank N.V. has a right to execute not more than 75% of votes during the General Meeting of Shareholders of Kredyt Bank S.A.

There were no movements in the share capital in the reporting period.

As of 28 February 2006, the holding company's Management Board was composed of:

Ronald Richardson	- President
Krzysztof Kokot	- Vice-president
Małgorzata Kroker-Jachiewicz	- Vice-president
Guy Libot	- Vice-president
Bohdan Mierzwiński	- Vice-president

On 9 February 2005 the Supervisory Board appointed from 1 March 2005 Mr. Ronald Richardson as a Member of the Management Board and then as the President of the Management Board after Banking Supervisory Commission agreed with this decision on 8 June 2005. Mrs. Małgorzata Kroker-Jachiewicz who was the President of the Board till 8 June 2005 stayed in the Board as a Vice-president.

On 9 February 2005 the Supervisory Board appointed Mr. Krzysztof Kokot as Vice President of the Management Board from 1 March 2005.

On 31 March 2005 the Supervisory Board accepted Mr. Fedele Di Maggio resignation who was a Member of the Management Board.

## 2. Group Structure

As at 31 December 2005 the Capital Group Kredyt Bank S.A. consisted of the following subsidiaries (direct or indirect) and jointly controlled entities which are not commercial companies:

<u>Entity name</u>	<u>Consolidation method</u>	<u>Type of opinion</u>	<u>Name of authorised entity that audited financial statements</u>	<u>Balance sheet date</u>
Żagiel S.A.	<i>Full</i>	<i>Audit in progress</i>	Ernst & Young Audit Sp. z o.o.	31.12.2005
Kredyt Lease S.A.	<i>Full</i>	<i>Audit in progress</i>	Ernst & Young Audit Sp. z o.o.	31.12.2005
Kredyt Trade Sp. z o.o.	<i>Full</i>	<i>Audit in progress</i>	Ernst & Young Audit Sp. z o.o.	31.12.2005
Kredyt International Finance B.V.	<i>Full</i>	<i>Audit in progress</i>	Ernst & Young Audit Sp. z o.o.	31.12.2005
PTE Kredyt Banku S.A. w likwidacji *	<i>Full</i>	<i>Qualified</i>	Ernst & Young Audit Sp. z o.o.	30.11.2005
Victoria Development Sp. z o.o.	<i>Full</i>	<i>Audit in progress</i>	Janina Linka, Grupa Audytorsko-Konsultingowa Sp. z o.o.	31.12.2005

\* - on 22 December 2005 the Extraordinary Meeting of Shareholders PTE Kredyt Bank S.A. endorsed liquidation financial statements of the company. On 23 December financial statements and ESM's resolution was forwarded to the Registration Court with application to cross out the company from the National Court Register. As of 31 December 2005 the company was not erased from the National Court Register.

As at 31 December 2005 shares in the following associates (direct and indirect) were recognised in the Group's consolidated financial statements using the equity pick-up method:

<i>Name and registered office</i>	<i>Type of activity</i>
KBC Towarzystwo Funduszy Inwestycyjnych S.A.	Managing investment funds

Details of the type and impact of changes in the scope of entities included in the consolidation as compared to the prior year are described in Note 5 of the additional notes and explanations to the consolidated financial statements of the Group for the year ended 31 December 2005.

### **3. Consolidated Financial Statements**

#### **3.1. Auditors' opinion and audit of consolidated financial statements**

Ernst & Young Audit Sp. z o.o. with its registered office in Warsaw, at Rondo ONZ 1, is registered on the list of entities authorised to audit financial statements under no. 130.

Ernst & Young Audit Sp. z o.o. was appointed by the Supervisory Board on 11 May 2005 to audit the Group's financial statements.

Ernst & Young Audit Sp. z o.o. and the certified auditor in charge of the audit meet the conditions required to express an impartial and independent opinion on the financial statements, as defined in Art. 66, clause 2 and 3 of the Accounting Act dated 29 September 1994 (uniform text: Journal of Laws of 2002, No. 76 with subsequent amendments – 'the Accounting Act').

Under the contract executed on 26 July 2005 with the Bank's Management Board, we have audited the financial statements for the year ended 31 December 2005.

Our responsibility was to express an opinion on the financial statements based on our audit. The auditing procedures applied to the financial statements were designed to enable us to express an opinion on the financial statements taken as a whole. Our procedures did not extend to supplementary information that does not have an impact on the financial statements taken as a whole.

Our procedures did not comprise additional information which has no influence on consolidated financial statement mean as a whole.

Based on our audit, we issued an auditors' opinion without qualification dated 28 February 2006, stating the following:

#### **“To the Supervisory Board of Kredyt Bank S.A.**

1. We have audited the attached consolidated financial statements for the year ended 31 December 2005 of Kredyt Bank S.A. Capital Group (“Group”), for which the holding company is Kredyt Bank S.A. located at Warsaw, Kasprzaka 2/8 street, including:

- the consolidated profit and loss account for the period from 1 January 2005 to 31 December 2005 with a net profit amounting to 415,878 thousand zlotys,
  - the consolidated balance sheet as at 31 December 2005 with total assets amounting to 20,841,344 thousand zlotys,
  - the consolidated statement of changes in shareholders' equity for the period from 1 January 2005 to 31 December 2005 with a net increase in shareholders' equity amounting to 423,395 thousand zlotys,
  - the consolidated cash flow statement for the period from 1 January 2005 to 31 December 2005 with a net cash outflow amounting to 1,673,252 thousand zlotys, and
  - the additional notes and explanations ("the attached consolidated financial statements").
2. The truth and fairness<sup>1</sup> of the attached consolidated financial statements and the proper maintenance of the consolidation documentation are the responsibility of the Bank's Management Board. Our responsibility was to audit the consolidated financial statements and to express an opinion whether, based on our audit, these consolidated financial statements are, in all material respects, true and fair<sup>2</sup>.
3. We conducted our audit of the attached consolidated financial statements in accordance with the following regulations in force in Poland:
- chapter 7 of the Accounting Act, dated 29 September 1994 ('the Accounting Act'),
  - the auditing standards issued by the National Chamber of Auditors,
- in order to obtain reasonable assurance whether these consolidated financial statements are free of material misstatement. In particular, the audit included examining, to a large extent on a test basis, documentation supporting the amounts and disclosures in the attached consolidated financial statements. The audit also included assessing the accounting principles adopted and used and significant estimates made by Management Board, as well as evaluating the overall presentation of the attached consolidated financial statements. We believe our audit has provided a reasonable basis to express our opinion on the attached consolidated financial statements treated as a whole.
4. In our opinion, the attached consolidated financial statements, in all material respects:
- present truly and fairly all information material for the assessment of the results of the Group's operations for the period from 1 January 2005 to 31 December 2005, as well as its financial position<sup>3</sup> as at 31 December 2005;
  - have been prepared, in all material aspects, in accordance with International Financial Reporting Standards approved by the European Union;
  - are in accordance with the provisions of laws affecting the content of the attached financial statements.
5. We have read the Directors' Report for the period from 1 January 2005 to 31 December 2005 and the rules of preparation of consolidated annual statements ('the Directors' Report') and concluded that the information derived from the attached consolidated financial statements reconciles with these financial statements. The information included in the Directors' Report corresponds with the relevant regulations of the Decree of the Minister of Finance as at 19 October 2005, on current and periodic information published by issuers of securities (Journal of Law No. 209, item 1744 – "The Decree on current and periodic information")."

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<sup>1</sup> Translation of the following expression in Polish: "rzetelność, prawidłowość i jasność"

<sup>2</sup> Translation of the following expression in Polish: "prawidłowe, rzetelne i jasne"

<sup>3</sup> Translation of the following expression in Polish: "sytuacja majątkowa i finansowa"

We conducted the audit of the consolidated financial statements during the period from 7 November 2005 to 28 February 2006. We were present at the Bank's head office from 7 November 2005 to 22 November 2005 and from 4 January 2006 to 28 February 2006.

### **3.2. Representations provided and data availability**

The Management Board confirmed its responsibility for the truth and fairness<sup>4</sup> of the financial statements and stated that it had provided us with all financial information, accounting records and other required documents as well as all necessary explanations. The Management Board also provided a letter of representations dated 28 February 2006, confirming that:

- the information included in the books of account was complete,
- all contingent liabilities had been disclosed in the financial statements, and
- all material events from the balance sheet date to the date of the representation letter had been disclosed in the financial statements,

and confirmed that the information provided to us was true and fair to the best of the Management Board's knowledge and belief, and included all events that could have had an effect on the financial statements.

### **3.3. Consolidated financial statements for prior financial year**

The consolidated financial statements of the Group for the year ended 31 December 2004 prepared in accordance with Polish Accounting Standards were audited by Dominik Januszewski, Certified Auditor No. 9707/7255, acting on behalf of Ernst & Young Audit Sp. z o.o., with a register office at Emilii Plater 53 Street in Warsaw No. 130.

The certified auditor issued an opinion without qualification with emphasis of matter on the financial statements for the year ended 31 December 2004. Emphasis of matter related to verification of estimations conducted in 2003 regarding to amounts recoverable from collaterals associated with its corporate loan portfolio. In the second half of 2004, the Bank updated its analysis of collaterals discount factors taking into account additional vindication results arising in 2004. In financial statement as of 31 December 2004 these analysis were taken into account. Moreover emphasis of matter defines that the above estimates of the recoverable value may be subject to change in the future, and also the vindication results may significantly differ from the above estimates due to possible changes in the vindication process and obtaining by the Bank data from the completed vindication processes in the future. The above issue has no influence on financial statement as of 31 December 2005 prepared in accordance with International Financial Report Standards approved by EU.

The consolidated financial statement as of 31 December 2004 was approved by the General Shareholders' Meeting on 25 April 2005 at which shareholders made a resolution that net profit for the year 2004 amounting to 185.176 thousand zloty will be assigned in full amount to cover the loss from the previous years.

The consolidated financial statements for the financial year ended 31 December 2004, together with the auditors' opinion, a copy of the resolution approving the financial statements, a copy of the resolution on the appropriation of profit and the Directors' Report, were filed on 25<sup>th</sup> May 2005 with the National Court Register.

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<sup>4</sup> Translation of the following expression in Polish: "*prawidłowość, rzetelność, i jasność*"

The introduction to the financial statements, the balance sheet as at 31 December 2004, the profit and loss account, statement of changes in equity and cash flow statement for the year ended 31 December 2004 together with the auditors' opinion, a copy of the resolution approving the financial statements and a copy of the resolution on the appropriation of coverage of loss were published in the Polish Official Journal B No.1237 on 10 August 2005.

## 4. Analytical Review

### 4.1. Basic data and financial ratios

Presented below are selected financial ratios indicating the economic or financial performance of the Group for the years 2004 - 2005. The ratios for the years 2004 and 2005 were calculated on the basis of financial information included in the consolidated financial statements for the year ended 31 December 2005. The selected financial information and data for 2003 were not presented as the Group has changed in 2005 the accounting policies to International Reporting Standards as adopted by the EU and the comparable data for earlier periods are not available.

	2005	2004*
<b>Total assets</b>	20.841.344	20.946.084
<b>Shareholders' equity</b>	1.681.595	1.517.088
<b>Gross profit</b>	321.368	178.774
<b>Net profit</b>	415.878	158.742
<b>Solvency ratio</b>	16,42%	14,72%**
<b>Profitability ratio</b>	36,08%	16,94%
<hr/>		
<b>Cost income ratio</b>	73,01%	76,48%
<hr/>		
<b>Return on capital</b>	26,00%	14,13%
<hr/>		
<b>Return on assets (%)</b>	1,99%	0,71%***
<hr/>		

\* Comparable data

\*\* Solvency ratio as of 31 December 2004 was based on the approved consolidated financial statements as of 31 December 2004

\*\*\* Average assets as of 2004 was calculated on the basis of the sum of assets as of 31 December 2003 presented in consolidated financial statements for the year ended 31 December 2004 prepared in accordance with Polish Accounting Standards

Rate of inflation:

Yearly average	2.1%	3.5%
December to December	0.7%	4.4%



#### **4.2. Comments**

The following trends may be observed based on the above financial ratios:

- In the year 2005 the Group generated a net profit amounting to 415.878 thousand zloty in comparison with the net profit 158.742 thousand zloty in the previous year (according to comparable data presented in Group's consolidated financial statements as of 31 December 2005).
- In 2005 in comparison with 2004 total assets decreased and amount to 20.841.344 thousand zloty as of 31 December 2005.
- Profitability ratio increased from the level of 16,94% in 2004 to 36,08% in 2005.
- Cost income ratio decreased from 76,48% in 2004 to 73,01% in 2005.
- Return on capital increased from 14,13% in 2004 to the level of 26,00% in 2005.
- Return on assets increased from 0,71% in 2004 to 1,99% in 2005.
- As of 31 December 2005 solvency ratio calculated in compliance with NBP methodology amounted for 16,42% in comparison with 14,72% in 2004.

#### **4.3. Going concern**

Nothing came to our attention during the audit that caused us to believe that the Bank is unable to continue as a going concern for at least twelve months subsequent to 31 December 2005 as a result of an intended or compulsory withdrawal from or a substantial limitation in its current operations.

The audited consolidated financial statements for the year ended 31 December 2005 were prepared by the Management Board on the assumption that the Bank will continue as a going concern for a period of at least twelve months subsequent to 31 December 2005 and the Management Board has not indicated any circumstances that would indicate a threat to the Bank's continued activity.

## **II. DETAILED REPORT**

### **1. Completeness and accuracy of consolidation documentation**

During the audit no material irregularities were noted in the consolidation documentation which could have a material effect on the audited consolidated financial statements, and which were not subsequently adjusted. These would include matters related to the requirements applicable to the consolidation documentation (and in particular eliminations relating to consolidation adjustments).

### **2. Accounting policies for the valuation of assets and liabilities**

The Group's accounting policies and rules for the presentation of data are detailed in Note 6 of the additional information to the Group's consolidated financial statements for the year ended 31 December 2005. During the audited reporting period according to article 55.6a. of the Accounting Act as of 29 September 1994 the Group in order to present the consolidated

financial statements has switched from Polish accounting standards to International Financial Reporting Standards approved by EU. Results of changing accounting policy are presented in the Note 65 and 66 of additional notes in the Group's consolidated financial statements as of 31 December 2005.

### **3. Structure of assets, liabilities and equity**

The structure of the Group's assets and equity and liabilities is presented in the audited consolidated financial statements for the year 31 December 2005. The data disclosed in the consolidated financial statements reconcile with the consolidation documentation.

#### **3.1. Goodwill on consolidation and amortisation**

The method of determining goodwill on consolidation, basis of amortisation, amortisation charged in the financial year and accumulated amortisation up to the balance sheet date were presented in Note 37 of additional notes and explanations to the consolidated financial statements.

#### **3.2. Shareholders' funds**

The amount of shareholders' funds is consistent with the amount stated in the consolidation documentation and appropriate legal documentation. Minority shareholders' interest as of 31 December did not appear.

Information on shareholders' funds has been presented in Note 48 of the Additional Notes and Explanations.

#### **3.3 Financial year**

The financial statements of all Group companies forming the basis for the preparation of the consolidated financial statements were prepared as at 31 December 2005 and include the financial data for the period from 1 January 2005 to 31 December 2005 with exemption of financial statements of PTE Kredyt Bank S.A., which financial statements comprise 11 month period ended as of 30 November 2005.

### **4. Consolidation adjustments**

#### **4.1. Elimination of inter-company balances (receivables and liabilities) and inter-company transactions (revenues and expenses) of consolidated entities.**

All eliminations of inter-company balances (receivables and liabilities) and inter-company transactions (revenues and expenses) of the consolidated companies reconcile with the consolidation documentation.

#### **4.2. Elimination of unrealised gains/losses of the consolidated companies, included in the value of assets, as well as relating to dividends**

All eliminations of unrealised gains/losses of the consolidated companies, included in the value of assets, as well as relating to dividends reconcile with the consolidation documentation.

**5. Disposal of all or part of shares in a subordinated entity**

During the financial year the Group did not sell any shares in subordinated entities.

**6. Items which have an impact on the group's result for the year**

Details of the items which have an impact on the Group's result for the year have been included in the audited consolidated financial statements for the year ended 31 December 2005.

**7. The appropriateness of the departures from the consolidation methods and application of the equity accounting as defined in the Accounting Act and the regulations issued based thereon**

During the process of preparation of the consolidated financial statements there were no departures from the consolidation methods or application of the equity accounting

**8. Application of regulations mitigating banking risk**

To the issue of obeying concentration of credit risk and accuracy in calculating solvency ratio by the Bank assumed an attitude in the report as of 28 February which supplement auditing financial statements of the Bank as of 31 December 2005.

**9. Work of Experts**

During our audit we have taken into account the results of the work of the following independent experts:

- property appraisers - in the calculation regarding the level of impairment for loan receivables we took into consideration the value of collaterals established in valuations performed by property appraisers engaged by the Bank;
- actuary – actuarial calculation of provision for retirement benefits.

on behalf of  
Ernst & Young Audit Sp. z o.o.  
Rondo ONZ 1,  
00-124 Warsaw  
Reg. No. 130

Dorota Snarska-Kuman  
Certified Auditor No. 9667/7232

Dominik Januszewski  
Certified Auditor No. 9707/7255

Warsaw, 28 February 2006.



**Consolidated financial statements  
of Kredyt Bank S.A. Capital Group  
for the year  
ended 31.12.2005**

## TABLE OF CONTENTS

1.	Consolidated income statement .....	4
2.	Consolidated balance sheet .....	5
3.	Statement of changes in equity .....	8
4.	Consolidated cash flow statement.....	10
5.	General information .....	12
6.	The description of major accounting principles applied for the purpose of preparing this financial statement.....	14
7.	Accounting estimates .....	34
8.	Segment reporting .....	37
9.	Interest income .....	43
10.	Interest expense .....	44
11.	Fee and commission income.....	44
12.	Fee and commission expense.....	45
13.	Dividend income .....	45
14.	Net trading income .....	45
15.	Profit/(loss) on investment activity .....	46
16.	Other operating income .....	46
17.	General and administrative expenses .....	47
18.	Change in impairment charges and provisions .....	49
19.	Other operating expenses .....	50
20.	Income tax expense in the income statement.....	50
21.	Earnings per Bank's shareholders .....	53
22.	Earnings per share (EPS).....	54
23.	Cash and balances with Central Bank .....	54
24.	Amounts due from banks.....	55
25.	Allowance for impairment losses for receivables due from banks .....	56
26.	Financial assets at fair value through profit and loss .....	57
27.	Loans and advances to customers.....	59
28.	Allowances for impairment losses for loans and advances to customers.....	62
29.	Finance lease receivables and change in charges for leasing receivables .....	62
30.	Investment securities.....	63
31.	Equity investments in subsidiaries and associates .....	66
32.	Investments in associates measured with the equity method.....	69
33.	Tangible fixed assets.....	69
34.	Movement of fixed assets.....	70
35.	Intangible assets.....	74
36.	Movement of intangible assets.....	74
37.	Goodwill on subordinated companies .....	76
38.	Deferred tax assets .....	77
39.	Other assets .....	78
40.	Amounts due to banks.....	78
41.	Amounts due to customers.....	79
42.	Issued debt securities.....	81

43.	Securities sold under repurchase agreements .....	81
44.	Provisions .....	81
45.	Deferred tax liability .....	83
46.	Other liabilities .....	83
47.	Subordinated liabilities.....	84
48.	Equity.....	85
49.	Contingent liabilities granted .....	87
50.	Capital adequacy ratio.....	88
51.	Discontinued operations .....	89
52.	Related party transactions.....	90
53.	Remuneration of the Members of the Supervisory Board and the Management Board of Kredyt Bank S.A.....	93
55.	Consolidated cash flow statement – additional information .....	95
57.	Asset pledged as collateral.....	99
58.	Changes in the Management and Supervisory Boards of Kredyt Bank S.A in 2005 .....	100
59.	Restructing program .....	101
60.	Seasonality or cyclical nature of operations .....	102
61.	Non-typical factors and events .....	102
62.	Issue, redemption and repayments of debt or equity instruments .....	102
63.	Dividends paid .....	103
64.	Post-balance sheet events .....	103
65.	First time adoption of IAS/IFRS .....	103
66.	Clarifications related to the adoption of IFRS and the related adjustments in the opening balance .....	104
67.	Fair value of financial assets and liabilities not recognized at fair value in the balance sheet .....	111
68.	Information on proceedings before courts or public administration authority.....	113
69.	Custodian services .....	116
70.	Risk management at Kredyt Bank S.A. Capital Group.....	116

## 1. Consolidated income statement

in '000' PLN	Note	01.01.2005- 31.12.2005	01.01.2004- 31.12.2004
Interest income	9	1 408 504	1 302 973
Interest expense	10	-655 057	-669 046
<b>Net interest income</b>		<b>753 447</b>	<b>633 927</b>
Fee and commission income	11	334 581	537 518
Fee and commission expense	12	-19 691	-23 877
<b>Net fee and commission income</b>		<b>314 890</b>	<b>513 641</b>
Dividend income	13	780	817
Net trading income	14	143 812	138 611
Profit/(loss) from investment activity	15	-4 054	43 517
Other operating income	16	66 072	111 842
<b>Total operating income</b>		<b>1 274 947</b>	<b>1 442 355</b>
General and administrative expenses	17	-890 825	-1 055 175
Net impairment charges for financial assets, other assets and provisions	18	-9 167	-145 663
Other operating expenses	19	-54 834	-62 744
<b>Total operating expenses</b>		<b>-954 826</b>	<b>-1 263 582</b>
<b>Net operating income</b>		<b>320 121</b>	<b>178 773</b>
Share of profit of associates		1 247	1
<b>Profit before tax</b>		<b>321 368</b>	<b>178 774</b>
Income tax expense	20	93 536	-20 032
<b>Net profit from business activities</b>		<b>414 904</b>	<b>158 742</b>
Net profit (loss) from discontinued operations		974	0
Net profit		<b>415 878</b>	<b>158 742</b>
Including:			
<b>Per the Bank's shareholders</b>	<b>21</b>	<b>415 878</b>	<b>156 840</b>
Per minority interests		0	1 902
<b>Earnings per share per the Bank's shareholders (in PLN per share)</b>			
- basic	22	1,53	0,64

Income statement should be analyzed together with the notes which constitute an integral part of this financial statements

## 2. Consolidated balance sheet

in '000' PLN	Note	31.12.2005	31.12.2004
<b>Assets</b>			
Cash and balances with Central Banks	23	607 090	1 512 591
Amounts due from banks	24	2 229 615	2 699 852
Allowances for impairment losses for receivables due from banks	25	-2 894	-3 194
Financial assets at fair value through profit and loss account, including held-for-trading assets	26	703 888	557 760
Loans and advances to customers	27	12 306 286	14 105 952
Allowances for impairment losses for loans and advances to customers	28	-2 604 206	-2 740 428
Investments in securities	30	6 709 711	3 912 871
- available-for-sale		4 417 879	2 450 200
- held-to- maturity		2 291 832	1 462 671
Equity investments classified as available-for-sale	31	35 690	35 267
Investment in associates	31, 32	8 929	0
Tangible fixed assets	33, 34	416 400	469 371
Intangible assets	35, 36	111 475	140 187
Goodwill	37	36 052	36 052
Deferred tax assets	38	112 968	10 435
Current tax receivables		13 412	5 107
Other assets	39	156 928	204 261
<b>Total assets</b>		<b>20 841 344</b>	<b>20 946 084</b>
<b>Liabilities</b>			
Amounts due to banks	40	2 562 167	3 007 090
Held-for-trading financial liabilities	26	220 155	233 932
Amounts due to customers	41	14 533 624	14 061 105
Debt securities issued	42	402 435	418 150
Securities sold under repurchase agreements	43	368 701	718 772
Income tax liability		4	5 778
Provisions	44	77 847	37 439
Deferred tax liabilities	45	864	2 060
Other liabilities	46	404 371	345 384
Subordinated liabilities	47	589 581	599 286
<b>Total liabilities</b>		<b>19 159 749</b>	<b>19 428 996</b>

Balance sheet should be analyzed together with the notes which constitute an integral part of this financial statements



**Balance sheet (cont.)**

<b>Equity</b>		<b>31.12.2005</b>	<b>31.12.2004</b>
Share capital		1 358 294	1 358 294
Share premium	48	0	350 910
Revaluation reserve	48	15 928	-20 247
Reserve capital	48	120 942	173 779
Currency translation differences from the translation of subordinated companies and foreign branches		-637	-285
Retained earnings/(loss)		-228 810	-502 203
Current net profit (loss) per Bank's shareholders		415 878	156 840
<b>Total equity attributable to shareholders of the Bank</b>		<b>1 681 595</b>	<b>1 517 088</b>
<b>Minority shareholders</b>		<b>0</b>	<b>0</b>
<b>Total equity and liabilities</b>		<b>20 841 344</b>	<b>20 946 084</b>
Capital adequacy ratio	50	16,42	14,72

Balance sheet should be analyzed together with the notes which constitute an integral part of this financial statements

Off-balance sheet items		31.12.2005	31.12.2004
Contingent liabilities, granted and received		4 089 190	5 771 653
Liabilities granted, including:		3 577 985	5 256 655
- financial	49	2 451 828	2 085 879
- guarantees	49	1 126 157	3 170 776
Liabilities received, including:		511 205	514 998
- financial		11 831	51 707
- guarantees		499 374	463 291
Amounts due under sale/purchase transactions		79 905 636	31 099 032
Other:		3 057 287	3 649 245
- received collateral and guarantees		3 057 191	3 649 150
- other		96	95
<b>Total off-balance sheet items</b>		<b>87 052 113</b>	<b>40 519 930</b>

Off-balance sheet items should be analyzed together with the notes which constitute an integral part of this financial statements

### 3. Statement of changes in equity

#### Shareholders' equity per Bank shareholders

Changes in the period 01.01.2005-31.12.2005

	Share capital	Share premium	Revaluation reserve	Currency translation differences from the translation of subordinated companies and foreign branches	Reserve capital	Retained earnings/loss	Net profit for the period	Total equity
in '000' PLN								
<b>Equity balance as at 01.01.2005</b>	<b>1 358 294</b>	<b>350 910</b>	<b>8 059</b>	<b>-285</b>	<b>173 779</b>	<b>-632 557</b>	<b>0</b>	<b>1 258 200</b>
Changes in equity:	0	-350 910	7 869	-352	-52 837	403 747	0	7 517
- covering retained loss	0	-350 910	0	0	-52 837	403 747	0	0
- valuation of financial assets	0	0	11 377	0	0	0	0	11 377
- currency translation differences	0	0	0	-352	0	0	0	-352
- other changes	0	0	-41	0	0	0	0	-41
- deferred tax	0	0	-3 467	0	0	0	0	-3 467
<b>Net profit/loss for the period</b>	<b>0</b>	<b>0</b>	<b>0</b>	<b>0</b>	<b>0</b>	<b>0</b>	<b>415 878</b>	<b>415 878</b>
<b>Equity balance as at 31.12.2005</b>	<b>1 358 294</b>	<b>0</b>	<b>15 928</b>	<b>-637</b>	<b>120 942</b>	<b>-228 810</b>	<b>415 878</b>	<b>1 681 595</b>

\*Equity reconciliation under PAS and IFRS has been explained in note 65 and 66.

## Changes in the period 01.01.2004-31.12.2004

	Share capital	Supplementary capital	Revaluation reserve	Currency translation subordinated companies and foreign branches	Reserve capital	Other reserve capitals	Retained earnings/loss	Net profit/loss for the period	Total shareholders' equity
in '000' PLN									
<b>Equity balance as at 01.01.2004</b>	<b>1 056 451</b>	<b>1 020 023</b>	<b>-53 426</b>	<b>5 319</b>	<b>173 779</b>	<b>62 000</b>	<b>-1 534 191</b>	<b>0</b>	<b>729 955</b>
Changes in shareholders' equity:	301 843	-669 113	33 179	-5 604	0	-62 000	1 031 988	0	<b>630 293</b>
- issue of series W shares	301 843	0	0	0	0	0	0	0	<b>301 843</b>
- share issue above share nominal value	0	301 843	0	0	0	0	0	0	<b>301 843</b>
- costs of share issue	0	-989	0	0	0	0	0	0	<b>-989</b>
- covering retained loss	0	-969 988	0	0	0	-62 000	1 031 988	0	<b>0</b>
- valuation of financial assets	0	0	33 318	0	0	0	0	0	<b>33 318</b>
- decrease in currency translation differences	0	0	0	-5 604		0	0	0	<b>-5 604</b>
- other changes	0	21	-139	0	0	0	0	0	<b>-118</b>
- sale of KBU shares	0	0	0	0	0	0	0	0	<b>0</b>
<b>Net profit/loss for the period</b>	<b>0</b>	<b>0</b>	<b>0</b>	<b>0</b>	<b>0</b>	<b>0</b>	<b>0</b>	<b>156 840</b>	<b>156 840</b>
<b>Shareholder's equity at period end - balance as at 31.12.2004</b>	<b>1 358 294</b>	<b>350 910</b>	<b>-20 247</b>	<b>-285</b>	<b>173 779</b>	<b>0</b>	<b>-502 203</b>	<b>156 840</b>	<b>1 517 088</b>

\*Equity reconciliation under PAS and IFRS has been explained in note 65 and 66.

#### 4. Consolidated cash flow statement

in '000' PLN	Note	01.01.2005- 31.12.2005	01.01.2004- 31.12.2004
<b>A NET CASH FLOW FROM OPERATING ACTIVITIES (I+/-II)</b>		<b>1 713 031</b>	<b>1 733 789</b>
– indirect method			
<b>I. Net profit (loss)</b>		<b>415 878</b>	<b>156 840</b>
<b>II. Total adjustments:</b>		<b>1 297 153</b>	<b>1 576 949</b>
1 Minority profit (loss)		0	1 902
2 Share in (profit) loss of subordinated companies measured with the equity method		-1 247	-1
3 Depreciation		135 483	166 612
4 Gains/losses on currency translation differences		-62 442	-193 217
5 Interest		-161 591	-9 731
6 Share in profits (dividends)		-780	-817
7 Profit (loss) from investment activity		20 841	-1 758
8 Net increase/decrease in provisions		43 772	-1 018
9 Net increase/decrease in inventories		-90	500
10 Net increase/decrease in debt securities		628 682	186 162
11 Net increase/decrease in amounts due from banks	54 b	-297 814	-158 938
12 Net increase/decrease in loans and advances to customers	54 c	1 415 832	2 576 857
13 Net increase/decrease in shares, other securities and other financial assets		11 341	131 473
14 Net increase/decrease in amounts due to banks	54 d	-504 234	-871 580
15 Net increase/decrease in amounts due to customers	54 e	487 552	-608 105
16 Net increase/decrease in liabilities related to securities sold under repurchase agreements		-349 008	716 664
17 Net increase/decrease in other liabilities		60 627	-422 355
18 Net increase/decrease in prepaid expenses and accruals		-3 221	761
19 Income tax paid		8 016	7 649
20 Other adjustments		-134 566	55 889
<b>III. Net cash flow from operating activities (I+/-II) – indirect method</b>		<b>1 713 031</b>	<b>1 733 789</b>

Cash flow statement should be analyzed together with the notes which constitute an integral part of this financial statements

**Consolidated cash flow statement (cont.)**

in '000' PLN	Note	01.01.2005- 31.12.2005	01.01.2004- 31.12.2004
<b>B NET CASH FLOW FROM INVESTING ACTIVITIES (I+/-II)</b>		<b>-3 407 301</b>	<b>496 426</b>
<b>I. Inflows</b>		<b>43 645 888</b>	<b>10 630 672</b>
1 Disposal of shares in subsidiaries		0	116 747
2 Disposal of shares in associates		2 495	271
3 Disposal of other shares, other securities and other financial assets		43 600 669	10 348 882
- including Treasury debt securities		43 508 706	10 218 157
4 Disposal of intangible assets and tangible fixed assets		5 104	163 955
5 Dividends received		780	817
6 Other inflows from investment activity		36 840	0
<b>II. Outflows</b>		<b>47 053 189</b>	<b>10 134 246</b>
1 Acquisition of shares in associates		10 317	0
2 Acquisition of other shares in other securities and other financial assets		46 965 215	10 067 462
- including Treasury debt securities		46 965 120	10 067 217
3 Acquisition of intangible assets and tangible fixed assets		77 657	66 784
<b>III. Net cash flow from investing activities (I-II)</b>		<b>-3 407 301</b>	<b>496 426</b>
<b>C NET CASH FLOW FROM FINANCING ACTIVITIES (I+/-II)</b>		<b>21 018</b>	<b>-442 014</b>
<b>I. Inflows</b>		<b>996 140</b>	<b>672 697</b>
1 Long-term loans from banks		996 140	0
2 Issued debt securities		0	70 000
3 Net cash inflows from the shares issue and additional contributions to share capital		0	602 697
<b>II. Outflows</b>		<b>975 122</b>	<b>1 114 711</b>
1 Repayments of long-term loans to banks		886 286	281 390
2 Redemption of issued debt securities		0	707 700
3 Financial lease rentals		1 583	144
4 Repayment of subordinated liabilities		0	60 000
5 Other financial outflows		87 253	65 477
<b>III. Net cash flow from financing activities (I-II)</b>		<b>21 018</b>	<b>-442 014</b>
<b>D TOTAL NET CASH FLOW (A+/-B+/-C)</b>		<b>-1 673 252</b>	<b>1 788 201</b>
E BALANCE SHEET CHANGE IN CASH		-1 673 252	1 788 201
F. CASH AT PERIOD BEGINNING		3 922 141	2 133 940
G. CASH AT PERIOD END (F+/-D), including:	54 a	2 248 889	3 922 141
Restricted cash		509 457	571 363

Cash flow statement should be analyzed together with the notes which constitute an integral part of this financial statements

The Management Board of Kredyt Bank S.A. approved this consolidated financial statement of the Kredyt Bank S.A. Capital Group for publication on 28 February 2006.

This financial statement was audited by Ernst & Young Audit Sp. z o.o., an independent licensed certified auditor. The audit was performed in line with the certified auditors' professional standards issued by the National Council of Auditors in Poland.

## 5. General information

Kredyt Bank Spółka Akcyjna ('Kredyt Bank S.A.', 'Bank') with its registered office in Warsaw, (Poland), in ul. Kasprzaka 2/8 was established in 1990 and entered into the register of entrepreneurs maintained by the District Court for the Capital City of Warsaw under No. 0000019597. The financial statement of Kredyt Bank S.A. Capital Group as at 31 December 2005 comprises the financial statement of Kredyt Bank S.A. and its subsidiaries (referred to as 'Capital Group' or 'Group') as well as investment in associates.

Kredyt Bank S.A. is a universal bank, ranked among top 10 Polish banks in terms of total assets. It provides a wide range of banking services addressed and tailored to the needs of all customer groups: business entities, individual customers and local authorities. The Bank provides convenient access to its services via an extended network of outlets and ATMs. In cooperation with TUiR Warta, the Bank was the first to offer banc assurance services.

Below we present subsidiaries, which along with its parent company, Kredyt Bank S.A., form Kredyt Bank S.A. Capital Group ('Group') as at 31.12.2005

Parent company		Seat		
Kredyt Bank S.A.		Warsaw		
No.	Subsidiary	Seat	Share (%) in votes at GMS as at 31.12.2005	Share (%) in votes at GMS as at 31.12.2004
1.	BFI Serwis Sp. z o.o.	Warsaw	100,00	100,00
2.	Inwestia Sp. z o.o.	Warsaw	100,00	100,00
3.	KB Zarządzanie Aktywami S.A.	Warsaw	100,00	100,00
4.	Kredyt International Finance B.V. *	Amsterdam	100,00	100,00
5.	Kredyt Lease S.A. *	Warsaw	100,00	100,00
6.	Kredyt Trade Sp. z o.o.*	Warsaw	100,00	100,00
7.	Lizar Sp. z o.o.	Warsaw	100,00	100,00
8.	Net Banking Sp.z o.o.	Warsaw	100,00	100,00

No.	Subsidiary	Seat	Share (%) in votes at GMS as at 31.12.2005	Share (%) in votes at GMS as at 31.12.2004
9.	KBC Towarzystwo Funduszy Inwestycyjnych S.A. **	Warsaw	30,00	100,00
10.	PTE Kredyt Banku S.A. * (w likwidacji)	Warsaw	100,00	100,00
11.	Victoria Development Sp. z o.o. *	Warsaw	100,00	100,00
12.	Żagiel S.A. *	Lublin	100,00	100,00

(\*) companies consolidated using full method

(\*\*) company valued using the equity method

On 22 December 2005, the Extraordinary General Meeting of Shareholders of PTE Kredyt Bank S.A. approved the company's liquidation report and on 23 December 2005 the financial statement was submitted, along with the resolution of the Extraordinary General Meeting of Shareholders, to the Registry Court for the capital city of Warsaw, with a request to delete the company from the National Court Register.

As the financial data and scope of the operating activity of BFI Service Sp.z o.o. is immaterial for the Group financial statements the Bank has changed the scope of the consolidation as compared to financial statements for the year 2004 and does not consolidate this entity in presented consolidated financial statements.

### KBC Banking and Insurance Capital Group

Kredyt Bank S.A. is a part of the KBC Banking and Insurance Capital Group ('KBC Group') established in 1998 as a result of a merger of ABB Insurance Group, Almanij-Kreditbank Group and CERA Bank Group. KBC Group has been operating in the present structure since 2005, i.e. the merger of KBC Bank and Insurance Holding Company with Almanij. The KBC Group is listed on Euronext Stock Exchange in Brussels.

The KBC Group focuses on banc assurance-type operations for individual customers, provides services for businesses, is involved in assets management and other types of market activities. It is one of the three largest banking and insurance companies on its home market in Belgium. Moreover, it is one of the leading financial groups in Europe – geographically, its operations are focused in Central Europe which is regarded as the second home market; the KBC Group is also present in many other countries worldwide. Market capitalization of the KBC Group amounts to approximately EUR 30 billion.

In Poland the KBC Group is also a majority shareholder of TUIR WARTA S.A.



## 6. The description of major accounting principles applied for the purpose of preparing this financial statement

### 6.1. Declaration of compliance with IFRS

Under Article 55 clause 6a of the Accounting Act of 29 September 1994 (unified text) Journal of Laws of 2002 No. 76 item 694 as amended/ ('Act'), from 1 January 2005, consolidated financial statements of the Group have been prepared in accordance with IAS/IFRS.

Under Article 45 clause 1c of the Act and under the decision of the General Meeting of Shareholders of Kredyt Bank S.A. of 25 April 2005, from 1 January 2005, individual financial statements of Kredyt Bank S.A. have been prepared in accordance with the International Accounting Standards (IAS) and the International Financial Reporting Standards (IFRS).

The consolidated financial statement of the Group for the financial year 2005 ended on 31 December 2005 has been prepared in accordance with the International Accounting Standards (IAS) and the International Financial Reporting Standards (IFRS) in force as at 31 December 2005 and approved by the European Commission. Matters not governed by the above-mentioned standards are regulated by the Accounting Act of 29 September 1994 (Journal of Laws of 2002 No. 76 item 694 as amended) and executive regulations thereto, and the Ordinance of the Minister of Finance of 19 October 2005 on current and interim information provided by issuers of securities (Journal of Laws of 2005, No. 209, item 1744).

This statement is the first full annual consolidated financial statement of the Group prepared in line with IFRS.

As at 31 December 2005, the European Commission adopted, with the same effective date, new standards and amendments to certain existing standards and their interpretations in force. The most significant changes are as follows:

- Adoption of IFRS 7 *Financial Instruments: Disclosure* this standard is effective since 1 January 2006; however earlier application is permitted. IFRS 7 replaces IAS 30 *Disclosures in the Financial Statements of Banks and Similar Financial Institutions* effective as at the date of preparing this financial statement and the disclosure requirements under IAS 32 *Financial Instruments: Disclosure and Presentation* and extends the scope of disclosures for financial instruments. IFRS 7 extends the requirements for quantitative and qualitative disclosures related to the risk management resulting from financial instruments, including credit risk, liquidity risk and market risk. The Group expects that disclosures related to the sensitivity analysis in the market risk management process will require certain additional information.
- Amendments to IAS 1 *Presentation of Financial Statements* – these amendments to the standard are effective from 1 January 2006; however earlier application is permitted. IAS 1 requires additional disclosures related to shareholders' equity management. The Group expects that disclosures related to shareholders' equity management would require certain additional information.

- Amendments to IAS 39 *Financial Instruments: Recognition and Measurement – Fair Value Option* with resulting amendments in IFRS 1-1 January 2006 is the effective date of these amendments, however earlier application is permitted. However, if the Group had applied the amendments earlier, i.e. before 31 December 2005, it would not be able to apply the option of measurement at fair value of assets and liabilities other than those measured at fair value on this date.

The explanation of the impact of the transition from Polish Accounting Standards (PAS) applied earlier to IFRS upon the financial standing and results of the Group presented in previous periods has been described in detail in Note 66.

## **6.2. Basis of preparing this financial statement**

The figures in this financial statement have been presented in PLN thousands (thousand PLN), unless stated otherwise.

This financial statement was prepared according to the historical cost concept, except for financial assets and financial liabilities which are measured at fair value through profit or loss, and available-for-sale securities which are carried at fair value through revaluation reserve.

The preparation of financial statements for the first time, and next ones, in line with IFRS requires a professional judgment of an entity's Management Board on the adopted accounting principles and accounting estimates applied with respect to balance sheet items and income statement items. Estimates are made basing on historical data and a number of assumptions based on the facts available at the time, resulting from internal and external conditions. The actual results of business operations may differ from the current accounting estimates.

Accounting estimates are verified on a regular basis. Changes in estimates are recognized in the financial statement in the period they were made. If such changes are also related to future periods, the assumptions being the basis for the estimates for future periods are also adjusted. The essential accounting estimates, which affect this financial statement, have been presented in Note 7.

The date of 1 January 2004 is the date of adopting IFRS by the Group and by the Bank, i.e. of the opening balance prepared according to IAS/IFRS.

The accounting principles adopted for preparing financial statements are applied on a continuous basis in all presented periods, starting from the opening balance, except for the exemptions from specific IAS/IFRS, which are permitted under IFRS 1, as described in Note 65. Clarifications of the transition to IFRS and the related adjustments in opening balance have been presented in Note 66.

### **6.3. Consolidation of financial statements**

#### **6.3.1. Subsidiaries**

Subsidiaries are all entities, in relation to which the Bank may, directly or indirectly, exert control and govern their financial and operating policy in order to gain benefits from their business. Financial statements of subsidiaries, which are material for the consolidated financial statement, are subject to consolidation with the full consolidation method from the date of taking over the control by the Bank. As a result of conversion to IFRS the Group applies the methodology for materiality assessment for consolidation purposes used by the Bank major shareholder. On a quarterly basis the Group performs tests for materiality based on which decision is made whether the subsidiary is material and whether the entity is consolidated. The consolidation is ceased on the day such control ceases.

The acquisition of subsidiaries by the Group is settled with the acquisition method. The acquisition cost is the aggregate of the fair value of acquired assets, issued equity instruments and liabilities contracted or acquired as at the exchange date, increased with the costs related directly to the business combination. Identifiable assets and liabilities, including contingent liabilities, acquired under the business combination, are initially measured at fair value as at the acquisition date, irrespective of the volume of any possible minority interests. The surplus of the acquisition cost over the fair value of the Group's interest in identifiable net assets is recognized as goodwill. If the acquisition cost is lower than fair value of net assets of the acquired subsidiary, the difference is recognized directly in the profit and loss account following re-analysis.

Intercompany receivables and liabilities, unrealized gains and losses and income and expense on account of intercompany transactions are excluded from this financial statement.

#### **6.3.2. Associates**

Associates are entities not controlled by the Group in terms of their financial or operational policies, but the Group exerts significant influence upon them, which is often accompanied by 20%-50% stake in the total number of votes within their decision making bodies. Investments in shares in associates are initially recognized in the balance sheet at cost, which includes goodwill, and further on, they are measured with the equity method. From the acquisition date, the Group's share in the financial result of associates is recognized in the income statement, and its share in net increase/decrease in shareholders' equity of associates is recognized in respective items of consolidated equity.

Unrealized gains from transactions between the Group and associates are excluded in proportion to the Group's share. Unrealized losses are eliminated in a similar manner, if there is no evidence of the impairment of assets.

The accounting principles applied by subsidiaries and associates were changed if such changes were necessary in order to ensure the compliance with the accounting principles applied by the Bank

#### 6.4. Transactions in foreign currencies

The items included in the financial statements of particular Group members are recognized in the currency in which a given business operates.

Transactions in foreign currencies are translated into PLN at the exchange rate as at the transaction date. Monetary assets and liabilities expressed in foreign currencies, recognized at historical cost, are translated into PLN at the average exchange rate of the National Bank of Poland as of the balance sheet date. Gains/losses from the translation of the resulting FX differences are recognized in profit and loss account.

Non-monetary assets and liabilities expressed in foreign currencies, recognized at historical cost, are translated into PLN at an exchange rate as at the transaction date, and items measured at fair value are translated at the average exchange rate of the National Bank of Poland as of the measurement date. Currency translation differences on non-monetary items measured at fair value through profit or loss are recognized in gains and losses on the change in fair value. Currency translation differences on non-monetary items, such as available-for-sale financial assets, are presented in revaluation reserve.

As at 31 December 2005 the only foreign entity of the Bank is the Bank's subsidiary KIF BV. The functional currency for this entity is EUR. The company's balance sheet figures are translated at the NBP average exchange rate and the income statement and the cash flow statement figures are translated at the arithmetic mean of NBP average rates of exchange.

Below, we present NBP average rates of exchange applied by the Group to translate balance sheet items

	31.12.2005	31.12.2004
EUR	3,8598	4,0790
USD	3,2613	2,9904
CHF	2,4788	2,6421

#### 6.5. Recognition of financial assets and liabilities in the balance sheet

The Group recognizes financial assets and liabilities in the balance sheet only when it is a party to a transaction.

Sale/purchase transactions related to financial assets valued at fair value through profit and loss, held-to-maturity investments and available-for-sale financial assets are recognized in the balance sheet always on the date of transaction. Loans and receivables are recognized at the time of the payment of cash to the borrower.

Financial assets are excluded from the balance sheet when contractual rights to cash flows from a financial asset expire, or at the time when the Group assigns contractual rights to receive cash flows.

## **6.6. Classification and measurement of financial assets and liabilities**

### **6.6.1. Financial assets and liabilities at fair value through profit and loss**

This category includes:

- held-for-trading assets or liabilities, i.e. those acquired or contracted with the intention of selling or repurchasing them in the nearest future. This category also comprises portions of the financial assets and liabilities portfolios managed jointly in order to generate profits in a short time horizon. This category also included derivatives;
- financial assets and liabilities which, at the time of their initial recognition, were designated by the Group to be measured at fair value through profit or loss.

Assets and liabilities are recognized at fair value from the date of the transaction. Fair value is determined on the basis of quotations on active markets, including prices of the latest transactions and generally adopted measurement models based on variables that can be observed in the market environment.

Interest and acquired discount or premium on securities is settled over time in net interest income based on the effective interest rate method. Securities are carried at fair value, and its change is recognized in the profit/loss on financial operations.

Gains/losses from assets disposal are calculated using the FIFO method.

Financial derivatives are recognized, from the transaction date, at fair value, without deductions of transaction expenses that can be incurred at the disposal. The transaction price is the best indicator of fair value at the initial recognition of a derivative. Following the transaction, for the purpose of the balance sheet measurement, fair value is determined on the basis of quotations on active markets, including prices of the latest transactions and generally adopted measurement models based on variables that can be observed in the market environment.

Derivatives with positive valuation as at the date of measurement are recognized in the balance sheet as assets, and derivatives with negative valuation from measurement – in liabilities.

Certain embedded derivatives are treated as separate derivatives, if the risks related to them and their features are not closely associated with the economic features and the risk characteristics of the host contract, and the host contract is not carried at fair value through profit or loss. Such types of derivatives are measured at fair value, and changes in fair value are recognized in the profit and loss account.

## **Held-to-maturity investments**

Held-to-maturity investments are non-derivative financial assets with fixed or determinable payments and fixed maturity that the Group intends and is able to hold to maturity.

Held-to-maturity investments are measured at amortized cost based on the effective interest method, taking account of impairment loss. Accrued interest and settled discount or premium is recognized in net interest income.

## **Loans and receivables**

Loans and receivables are non-derivative financial assets, with fixed or determinable payments that are not quoted in an active market. Loans and receivables arise when the Group's disburse cash to customers for purposes other than generating short-term trading gains. This category includes amounts due from banks and customers, including purchased debt and investments in debt financial instruments, if they are not quoted on the active market.

Loans are measured in the balance sheet at amortized cost based on the effective interest rate method, taking account of impairment losses.

Accrued interest with net commission settled over time based on the effective interest method is recognized in interest income; the commission settled on a straight-line basis is recognized in fee and commission income. Impairment charges are recognized in the income statement as impairment charges for financial assets.

### **6.6.2. Available-for-sale financial assets**

Available-for-sale financial assets are non-derivative financial assets designated as available for sale or not classified as financial assets valued at fair value through profit and loss, loans and receivables or held-to-maturity investments.

Available-for-sale financial assets are measured at fair value in the balance sheet. Changes in fair value are recognized in revaluation reserve until the financial asset is derecognized; then accumulated gains/losses included in equity are recognized in the profit and loss account. In the case of debt securities, interest income and discount or premium is settled over time in net interest income based on the effective interest rate method.

If fair value cannot be determined, assets are recognized at cost less impairment charge. Impairment charge is recognized in the profit and loss account.

Dividends from available-for-sale equity instruments are recognized in the profit and loss at the time when the right to obtain them arises.

Gains/losses from assets disposal are calculated with the FIFO method.

### 6.6.3. Equity investments

Investment in subsidiaries that are not fully consolidated in the consolidated financial statement because of the immateriality of their financial statements for the Group and minority interests are classified as available-for-sale portfolio and are recognized at cost less any impairment allowance (if there is evidence of impairment) due to the fact that their fair value cannot be determined reliably. If the impairment charge is higher than the purchase price, the difference is recognized against other than capital exposure, e.g. credit exposure. If there is no such exposures provision for impairment is recognized as a liability.

### 6.6.4. Financial liabilities not held for trading

This category includes amounts due to banks and customers, loans borrowed by the Group, debt securities issued and subordinated liabilities, following the deduction of transaction expenses.

Financial liabilities not held for trading are recognized in the balance sheet in amounts to be paid valued at amortized cost with the application of the effective interest rate method.

### 6.6.5. Hedge accounting

Hedge accounting recognises the effects of compensating for changes in fair value of the hedging instrument and the hedged items, which exert impact on the income statement. According to adopted hedge accounting principles, the Group designates certain derivatives to hedge fair value of specific assets on condition that the criteria provided for in IAS 39 are met. Hedge accounting is applied in the Bank to hedge certain items when all following criteria are met:

- upon the inception of hedge, the Group officially determines and documents hedging relations as well as the purpose of risk management and the strategy of hedge; the documentation identifies the hedging instrument, the hedged item or transaction, the nature of the hedged risk and the method of the Group's assessment of hedging instrument effectiveness in offsetting the risk of changes in fair value of the hedged item or cash flows related to the hedged risk;
- the hedging is expected to be highly effective in achieving offsetting changes in fair value (or cash flows) attributable to the hedged risk, according to the initially documented risk management strategy related to a specific hedging relationship;
- the hedge effectiveness may be assessed reliably, i.e. fair value or cash flows attributable to the hedged item resulting from the hedged risk and the fair value of the hedging instrument may be measured reliably;
- the hedge is assessed on an ongoing basis and is found highly effective in all reporting periods in which the hedge was established.

Fair value hedge, which meets hedge accounting conditions, is recognized by the Group as follows:

- gains or losses resulting from the revaluation of fair value of a hedging derivative are disclosed in the income statement;
- gains or losses related to the hedged item, resulting from the hedged risk, adjust the carrying amount of the hedged item and are recognized in the income statement. The rule is applicable to the hedged item which otherwise is measured at cost. When the hedged item is an available-for-sale financial asset, gains or losses resulting from the hedged risk are recognized in the income statement.

The Group discontinues the hedge accounting principles application if the hedging instrument expires or is sold, terminated or exercised; the hedge no longer meets the criteria for hedge accounting or the Group revokes the hedging designation

In the case of a hedged instrument, which in other circumstances, would be recognized at amortized cost, the adjustment of the carrying amount resulting from the application of the hedging accounting is amortized to income statement. The amortization starts at the time of ceasing to identify the hedging relation, i.e. from the time of ceasing to adjust the hedged item with changes in fair value resulting from the hedged risk. The adjustment is settled with the effective interest rate method estimated as at the date of starting the amortization.

In the case of a hedged instrument which is an available-for-sale asset measured at fair value, the whole change of fair value from the time of ceasing to identify the hedging relation is recognized in the revaluation reserve according to the generally adopted rule.

#### **6.6.6. Embedded derivatives**

An embedded derivative is a component of a hybrid (combined) instrument that also includes a non-derivative host contract –with the effect that some of the cash flows of the combined instrument vary in a way similar to the stand-alone derivative. An embedded derivative is separated from the host contract and accounted for as a derivative only if:

- the economic characteristics and risks of the embedded derivative are not closely related to the economic characteristic and the risks of the host contract;
- a separate instrument with the same terms as the embedded derivative would meet the definition of a derivative
- the hybrid (combined) instrument is not measured at fair value with changes in fair value recognized in profit or loss (i.e. a derivative that is embedded in a financial asset or financial liability at fair value through profit and loss is not separated).

When an embedded derivative is separated, the host contract is accounted for in accordance with accounting principles appropriate for such contracts

#### **6.7. Impairment of financial assets**

##### **Assets carried at amortized cost**

Loan receivables constitute the most significant part of financial assets; and the most exposed to impairment, recognized in the Group's balance sheet at amortized cost. At each balance sheet date (at least once a quarter) the Group carries out an analysis to determine whether an impairment of the individual assets and/or the impairment of a portfolio of financial assets occurred. A financial asset or a group of financial assets were impaired and impairment losses was incurred when, and only when, there is objective evidence of impairment as a result of one or more events that occurred after the initial recognition of the asset (a 'loss event') and that loss event (or events) has an impact on the estimated future cash flows of the financial asset or group of financial assets that can be reliably estimated. Expected future losses are not recognized in the estimates of the current impairment. The list of objective circumstances indicating impairment has been presented in Note 7.



If the Group identifies circumstances that indicate impairment, then the impairment loss is calculated, and is equal to a difference between the book value of a loan receivable and its economic value measured as the present value of expected future cash flows discounted with the effective interest rate of contacts. IFRS provides for the possibility, as a practical solution, of applying the analysis of the fair value of assets and accepted loan collateral in the analysis of the impairment of assets recognized at amortized cost.

Impairment charge is recognized in the profit and loss account.

Individual impairment is measured for all loan receivables for which certain individual signs indicating impairment were identified.

When no objective evidence occurred which indicate the loan impairment assessed on individual basis, regardless of whether or not it constitutes a significant reporting item, such exposure is included in the portfolio of loans with similar risk features and the portfolio analysis of the impairment is performed. Homogenous loans portfolios are created basing upon the similar characteristics of credit risks that are specific for the defined groups of customers and products. The measurement of the portfolio impairment is performed basing on historical parameters of losses generated by the similar assets portfolios. Historical trends for losses are cleared of one-off events and are updated against a current risk profile of homogenous groups of assets. This way, the credit portfolios' risk is identified, and a defined probability exists that this risk will transform into individual losses. The Bank verifies the methodology on a regular basis.

When the circumstances that indicate impairment cease to exist, the impairment charge is reversed through the profit and loss account.

As the Group applied exemptions indicated in IFRS 1 and did not restate the comparable data as provided in IAS 39, the carrying amount of loan receivables as of 1 January 2004 and 31 December 2004 was disclosed in accordance with the Polish accounting principles in force at the Bank and the Group on these days. The Polish principles required the classification of credit exposures into 5 risk groups (normal, under observation, substandard, doubtful and loss), applying a criterion of timely debt coverage and a criterion of the borrower's economic and financial standing. Specific provisions for the risk connected with credit exposures were established at least in the amounts required for the particular risk groups (from 1.5% to 100% of the base of establishment of the specific provisions). The Group, while estimating the amount of specific provisions for the purpose of the Polish principles, estimated the value of securities in line with the regulations in force as well as the internal principles adopted by the Group.

Pursuant to article 130 of the Act of 29 August 1997 – Banking Law (Journal of Laws of 2002 No. 72 item 665 as amended), the Bank established a provision for general risk in the comparable data as at 1 January and 31 December 2004 amounting to PLN 129,951 thousand and PLN 97,317 thousand respectively. Under § 7 of the Ordinance of the Minister of Finance of 10 December 2003 on the rules of establishing provisions for the risk of banking transactions (Journal of Laws of 19 December 2003), the Bank decreased the required level of specific provisions for the risk related to credit exposures resulting from retail loans and credits with the portion of the provision for general risk. As a result, this portion of the provision for general risk was recognized in this financial statement as a decrease in loan receivables.

The remaining portion of the provision for general risk as at 1 January and 31 December 2004 did not meet the criteria of its recognition as a provision under IAS 37 *Provisions, Contingent Liabilities and Contingent Assets*. In accordance with IAS 30 *Disclosures in the Financial Statements of Banks and Similar Financial Institutions*, the Bank recognized these amounts in retained earnings/loss as at the above dates respectively.

#### **6.7.1. Write offs of receivables to provisions**

The Group writes off loan receivables to impairment charges when such receivables are lost receivables, particularly when:

- the costs of further debt recovery will exceed the expected proceeds from debt recovery;
- the ineffectiveness of the Bank's debt recovery process is confirmed with a respective document issued by a respective enforcement body;
- the debtor's assets that can be subjected to enforcement, and the debtor's whereabouts cannot be established;
- the estate of a deceased debtor does not contain assets that can be subjected to enforcement;
- they are prescribed;
- they are written off due to the sale of claims;
- they are cancelled or written off due to debt restructuring;
- they are cancelled for material reasons, other than listed above.

#### **6.7.2. Available-for-sale financial assets**

If the Group identifies objective evidence of the impairment of an asset classified as available for sale, the cumulative negative measurement of this asset, previously accounted for in the revaluation reserve, is written off and recognized directly in the profit and loss account, despite the fact that this asset is not excluded from the balance sheet.

In the case of an equity instrument classified as available for sale, the impairment loss is not reversed through the profit and loss account up to the amount previously accounted for in equity, and the surplus is recognized in the profit and loss account. In the case of a debt instrument, at the time when the circumstances indicating impairment are no longer identified, the amount of the reversed impairment loss is recognized in the profit and loss account.

## **6.8. Finance lease receivables**

Contracts of lease under which the Group generally transfers all the risks and rewards related to the possessed assets are recognized by the Group as finance lease contracts. Receivables due under finance lease contracts are presented by the Group in the balance sheet in the amount equal to net leasing investment, as loans and advances to customers.

Interest income under finance lease contracts is settled with the effective interest rate method in order to reflect the constant, in a given period, rate of return on net leasing investment.

## **6.9. Offsetting financial instruments**

Financial assets and liabilities are offset and the net amount reported in the balance sheet when the Group has a legally enforceable right to offset the recognized amounts and there is an intention to settle on a net basis, or realize the asset and settle the liability simultaneously.

## **6.10. Sale and repurchase agreements**

Securities sold, under repurchase agreements ('repos') are not excluded from the balance sheet; they are only reclassified to pledged assets (available-for-sale assets), if transferee has the contractual or common right to sell or pledge the collateral. Dues to counterparties are recognized in financial liabilities. Securities purchased under agreements to resell ('reverse repos') are recorded as loans and advances to other banks or customers, depending on their nature. The difference between the sale and repurchase prices is treated as interest and accrued over the life of the agreements using the effective interest method.

## **6.11. Tangible fixed assets**

### **Owned fixed assets**

Property and equipment, complete, prepared for direct use, with a foreseeable useful life of over one year, held by the Group and used by it, are recognized in the balance sheet at cost less depreciation and total impairment charges. Property and equipment with low individual value are fully depreciated in the month of putting them into use.

The Group, according to IFRS 1 on the preparation of the opening balance sheet according to IFRS, applied fair value as the deemed cost of tangible fixed assets.

Property and equipment also include construction in progress and fixed assets put into use under the contracts of operating lease. Property and equipment not used by the Group, but held for sale, are recognized in the balance sheet at the lower of: carrying amount as at the day of classification to this category, and fair value less selling costs.

### 6.11.1. Capital expenditure incurred in further periods

The Group recognizes, in the carrying amount of fixed assets, expenses of the increase in value or of the replacement of parts of fixed assets at the time of their incurrence, when it is probable that future economic benefits associated with the item will flow to the Group and the cost of improvement or replacement may be measured reliably. All other expenses are charged to the profit and loss account during the financial period in which they are incurred.

### 6.11.2. Depreciation

Fixed assets are depreciated with the straight-line method in line with the depreciation schedule. The period of economic useful life is taken into consideration while determining the depreciation period and the annual depreciation rate. Land is not depreciated. Fixed assets that are used together, but which have various useful lives, are depreciated separately.

Estimated periods of expected economic useful life of fixed assets:

- |                          |                       |
|--------------------------|-----------------------|
| • Buildings              | 40 years              |
| • Leasehold improvements | 10 years              |
| • Motor vehicles         | 6 years               |
| • Plant and machinery    | Between 3 and 7 years |
| • Other fixed assets     | 10 years              |

The assets' residual values and useful lives are reviewed on an annual basis. The Group performs annual review of impairment indicators and if the indicators occur the tests for impairment of particular groups of fixed assets is carried to ensure whether the present carrying amount is not higher than the market value or discounted value of future economic benefits.

Depreciation rates resulting from the tax regulations in force are applied for the purpose of tax settlements.

### 6.12. Intangible assets

Intangible assets are assets, which comply with the following criteria:

- they can be separated from a business unit and sold, transferred, licensed or given for gratuitous use to third parties, both individually and jointly with related agreements, assets or liabilities, or
- they arise from contracts or other titles, irrespective of whether they can be transferred or separated from a business unit.

Intangible assets acquired under a separate transaction are recognized in the balance sheet at cost. Intangible assets acquired in transactions of business unit acquisition are recognized in the balance sheet at fair value as at the date of the acquisition.

Following the initial recognition, intangible assets are subject to historical cost.

#### **6.12.1. Computer software**

Acquired computer software licenses are recognized as intangible assets at costs incurred to acquire and bring to use the specific software. The Group writes off activated expenses in the estimated useful life of 5 years.

The Group's costs that are directly associated with the production of identifiable and unique software products controlled by the Group, and that will probably be used and generate economic benefits exceeding costs beyond one year, are recognized as intangible assets. Direct costs of the development of software activated in this way are amortized in the estimated useful life not exceeding 5 years.

The Group's expenditures on maintenance and technical service of computer software are recognized as expense as incurred.

#### **6.12.2. Other intangible assets**

Other intangible assets are recognized by the Group in the balance sheet at cost less accumulated amortization and any impairment charges.

The Group recognizes, in the carrying amount of intangible assets, expenses of the increase in value or replacement of the parts of such assets at the time of their incurrence, when it is probable that greater future economic benefits associated with the item will flow to the Group and the cost of improvement or replacement may be measured reliably. All other expenses are accounted for in the income statement as incurred.

#### **6.12.3. Amortization**

Intangible assets are amortized with the straight-line method according to the amortization schedule. The period of economic useful life, if it can be established, is taken into consideration while determining the amortization period and the annual amortization rate. Estimated useful life of intangible asset is 5 years for computer software licenses and copyrights.

Amortization rates resulting from the tax regulations in force are applied for the purpose of tax settlements.

The Bank does not have any intangible assets with indefinite useful life.

### 6.13. Goodwill

Goodwill represents an excess of the cost of an acquisition over the fair value of the Group's share of identifiable assets, liabilities and contingent liabilities of the acquired subsidiary/associate at the date of acquisition. Goodwill on acquisitions of subsidiaries is included in 'goodwill of subordinated companies'. Goodwill on acquisitions of associates is included in 'investments in associates'. Goodwill is not amortized; only analyzed in terms of the risk of impairment basing on the methodology of the cash-generating unit, i.e. the group of financial assets and liabilities generating inflows of cash.

For the purpose of the presentation in comparable data, as of 1 January 2004, the Group ceased to amortize goodwill. As at this date, goodwill of the companies consolidated by the Bank equals to the net value recognized in the 2003 closing balance. At least once a year, the Group performs a goodwill impairment test for based on the models developed in cooperation with the Bank's major shareholder.

### 6.14. The methods of the measurement of impairment of assets other than financial assets

The carrying amount of particular assets is periodically tested for impairment. If the Group identifies evidence of impairment, further it determines whether the present book value of a given asset is higher than the value that can be obtained from its further use or sale, i.e. the recoverable amount of a given asset is established. If the recoverable amount is lower than the present carrying amount of a given asset, impairment loss is recognized and impairment charge is accounted for in the profit and loss account.

#### 6.14.1. Measurement of recoverable amount

Recoverable amount of an asset is determined as the higher of the following: the price than can be obtained from the sale less costs of sells and value in use of a given asset. Value in use is determined as estimated future cash flows generated by a given asset discounted with the market rate and increased with the margin for the risk specific for a given class of assets.

Cash-generating units (CGU), i.e. groups of financial assets and liabilities directly attributable to goodwill and generating cash inflows independent of other groups, are separated for the purpose of goodwill impairment tests. If negative trends in the generated flows are identified, the impairment of the whole group of assets and liabilities is measured and recognized in attributed goodwill.

As at 1 January 2004, the Group has tested for impairment all major classes of assets including goodwill. The Group analysis of impairment indicators and if required performs tests for impairment of intangible assets and tangible fixed assets. Goodwill is tested for impairment annually regardless of the occurrence of the impairment triggers.

#### **6.14.2. Reversal of impairment loss**

Impairment loss for goodwill is not reversed.

In the case of other assets, impairment loss may be reversed if evidence of impairment ceases to exist or the parameters taken into account in estimates of recoverable amount are changed.

Impairment loss may be reversed only up to the carrying amount of an asset, which, having regard for accumulated depreciation, would have been determined if the impairment loss had not been made.

#### **6.15. Trade and other receivables**

Trade and other receivables are reported in the amount due less impairment charges.

##### **6.15.1. Assets taken over for debts**

Assets taken over for debts are measured at their fair value, including the cost of sale. If fair value of assets taken over is lower than the nominal value of receivables, impairment loss is recognized. If the selling price of the assets is higher than debt, the difference constitutes a liability towards the borrower.

#### **6.16. Deferred tax assets and liabilities**

Deferred tax assets are recognized on all negative temporary differences as well as non-consumed tax assets and unused tax losses carried forward, in the amount in which it is probable that taxable income will be generated which will allow for using the said differences, assets and losses:

- except for situations, when deferred tax assets related to negative temporary differences are created as a result of the initial recognition of an asset or a liability in a transaction which is not a business combination and that at the time of the transaction it affects neither profit before tax nor taxable income nor tax loss; and
- in the case of negative temporary differences related to investments in subsidiaries or associates and interests in joint ventures, a deferred tax asset is recognized in the balance sheet only in such an amount for which it is probable that in the foreseeable future the said temporary differences will be reversed and taxable income is generated which will allow for deducting negative temporary differences.

The carrying amount of a deferred tax asset is verified as of each balance sheet date and is subject to a respective decrease by the amount, which corresponds to the lower degree of the probability of generating taxable income or partial or total realization of a deferred tax asset.

Deferred tax liability is recognized for all positive temporary differences:

- except for situations, when the deferred tax liability is created as a result of the initial recognition of goodwill or initial recognition of an asset or a liability in a transaction which is not a business

combination and that at the time of the transaction it affects neither profit before tax nor taxable income or tax loss;

- in the case of positive temporary differences arising from investments in subsidiaries or associates and interests in joint ventures – except for situations when the dates of reversing temporary differences are controlled by an investor and when it is probable that, in a foreseeable future, the temporary differences will not be reversed.

Deferred tax assets and deferred tax liabilities are determined using tax rates (and laws) that have been enacted or substantially enacted by the balance sheet date and are expected to apply when the related deferred tax asset is realized or the deferred tax liability is settled. Deferred tax liability is not discounted.

Deferred tax related to items recognized directly in shareholders' equity is accounted for in shareholders' equity and not in the income statement.

#### **6.17. Cash and cash equivalents**

For the purpose of the cash flow statement, cash and cash equivalents include short-term balances used to settle short-term liabilities, with less than three months maturity from the date of acquisition, including cash and balances with central bank and other qualifying short-term receivables, including term deposits on the interbank market.

#### **6.18. Provisions**

The Bank recognizes provisions in the balance sheet when:

- a) the Bank has a present legal or constructive obligation as a result of past events;
- b) it is more likely than not that an outflow of resources will be required to settle the obligation;
- c) the amount of the future obligation can be estimated reliably.

The provision is recognized at the amount of the estimated outflow of cash. The amount of the provision is determined as the value of the discounted future cash flow for the period after which the provision will be utilized.

##### **6.18.1. Restructuring provision**

The Group recognizes a restructuring provision in the balance sheet for evidenced costs of restructuring. The provision is made on the basis of a detailed, official and published restructuring plan. The provision does not include future operating expense.



### 6.18.2. Employee benefits

The Group does not offer a specific pension scheme for its employees, thus has no commitments to its employees in this respect. The Group's entities, as employers, fulfilling the obligations indicated in the law, is obliged to withhold and pay social security and health insurance contributions for its employees and contributions to the Labour Fund and the Guaranteed Employee Benefits Fund. These payments are part of short-term employee benefits, including remuneration, bonuses, paid leaves. Short-term benefits are recognized in general expenses under general principles.

The provision for retirement severance pays, which is determined annually by actuarial calculations, is the only component of long-term employee benefits.

### 6.19. Equity

Share capital is recognized at nominal value in the amount compliant with the Bank's Memorandum and Articles of Association and the entry in the Court Register. Other shareholders' equity is recognized in the balance sheet by types as required by law and Memorandums and Articles of Association of the Bank and particular subsidiaries. Shareholders' equity also comprises net profit/loss for the period and retained profit or loss. Particular items of shareholders' equity are presented in notes.

### 6.20. Granted off-balance sheet liabilities

Within its operations, the Group enters into transactions, which, at the time of their conclusion, are not recognized in the balance sheet as assets or liabilities, but result in contingent liabilities. A contingent liability is:

- a possible obligation depending on whether some future event occurs, whose existence will be confirmed only at the time of the occurrence or non-occurrence of one or more uncertain future events not fully controlled by the Group's entities;
- a present obligation resulting from past events, but not recognized in the balance sheet, as it is not probable that the outflow of cash or other assets in order to fulfill the obligation is necessary, or the obligation amount cannot be determined reliably.

Granted credit lines and guarantees are the most significant items of granted off-balance sheet liabilities.

Undrawn credit lines are recognized in off-balance sheet liabilities in the amount resulting from contracts.

Guarantees issued by the Bank on behalf of customers are recognized in off-balance sheet liabilities in the amount resulting from contracts.

Credit risk arising from off-balance sheet liabilities is assessed on the basis of discounted, expected, future cash flows. The provisions for estimated risk are created in 'liabilities' in the Bank's balance sheet.

### 6.21. Company Social Benefit Fund (CSBF)

CSBF is created on the basis of write-downs made by the Bank and the Group's companies and charged to operating expenses as required by the CSBF Act. The objective of the Fund is to finance social benefits for employees. The Fund's liabilities are accumulated write-downs made by the Bank the Group's companies for CSBF less non-returnable expenditure from CSBF. The Group has no social assets; all CSBF liabilities are expressed in cash deposited on a separate banking account.

For the purpose of presentation in this financial statement, the Group offset assets and liabilities of CSBF, as it does not constitute Group's assets

### 6.22. Net interest income

Interest income and expense generated by financial assets and liabilities are recognized in the income statement at amortized cost using the effective interest rate method.

The following financial assets and liabilities are measured by the Group at amortized cost:

- credits and loans granted as well as the other receivables – not held for trading;
- held-to-maturity investments;
- non-derivative financial liabilities not held for trading;
- financial assets for which fair value cannot be determined reliably.

In addition, as indicated in in paragraf *“Financial assets and liabilities at fair value through profit and loss”* in the case of debt securities carried at fair value, the coupon rates and acquired discounts or premiums are amortized with effective interest rate method in the income statement.

The purpose of the measurement at amortized cost with the effective interest rate is to ensure that income and expenses, in particular reporting periods, related to the measured financial assets and liabilities over the entire period when they are held in the portfolio are commensurable, and, at the same time, the achievement of the constant rate of return on the assets portfolio financed with the defined deposits portfolio.

The effective interest rate is the rate that discounts a future, expected flow of cash payments to present net carrying amount during the period until maturity or by the time of the next market evaluation of a particular financial asset and liability, and its determination entails any due or cash payments as well as cash flows paid or received by the Bank under the agreement on a given instrument, excluding future, possible credit losses.

The method of settling coupon rates, commissions/fees and certain external costs connected with the financial instruments (with the effective interest method rate or straight-line method) depends on the nature of a given instrument. In the case of financial instruments with fixed cash flows schedules, the effective interest rate method is applied. In the case of instruments with undefined cash flows schedules, it is impossible to calculate the effective interest rate and commissions/fees are settled on the straight-line basis over time.

However, the method of recognizing particular types of commissions/fees settled over time in the income statement as interest income or fee and commission income, and the need for their settlement over time instead of one-off recognition in the income statement, depends on the economic nature of the commission/fee.

The items included in the commissions/fees settled over time include, e.g. fees for a positive appraisal of a loan application, commissions for granting a credit, commissions for releasing a credit, fees for establishing additional collateral, etc. The collection of the above commissions and fees constitutes an integral part of the return generated by a specific financial instrument. This category also includes fees and costs of changes of contractual terms, what modifies the value of initial effective interest rate. Any significant amendment to the terms of a given financial instrument in economic terms is connected with the expiry of the financial instrument of the previous type and creation of a new instrument with different characteristics.

The fees that are collected in this category include, among others, fees for preparing an annex changing a future cash flows schedule, fees for restructuring loan agreements, fees for postponement of payment dates, etc. The above-mentioned types of fees are deferred and settled over time in the income statement applying the effective interest rate method or on a straight-line basis, depending on the type of a product.

Furthermore, if the conclusion of the defined loan agreements is probable, the fees related to the Bank's commitment to conclude them are deemed as remuneration for a permanent commitment in the acquisition of the financial instrument; they are deferred and recognized as the adjustment of the effective return upon the conclusion of a given agreement (with the method of the effective interest rate or on a straight-line basis, depending on the type of a product).

All fees/commissions and external expenses connected with the extension of consumer loans via Żagiel are amortized with the effective interest rate in the income statement.

In the case of assets for which evidence of impairment was identified, interest income is charged to the income statement on the basis of Net Investment defined as the difference between the gross exposure and impairment charge basing on effective interest rate applied to calculate impairment charge.

### **6.23. Net fee and commission income**

As stated above, the Bank in the net interest income accounts for fees and commissions recognized in the income statement with the effective interest rate method.

Whereas fees and commissions not settled with the effective interest rate, are settled over time with the straight-line method or recognized one-off and reported in 'net fee and commission income'. Such income includes commissions on revolving loans, overdraft facilities, credit cards, off-balance sheet liabilities, and fees for managing current accounts. All fees for the activities in which the Group acts as an agent or provides services related to the distribution of shares of investment funds, transfers, and payments, etc. are recognized once.

**6.24. Net trading income**

Net trading income comprises gains or losses on the disposal or change of the fair value of financial assets and liabilities measured at fair value through profit or loss. This item also includes foreign exchange.

**6.25. Dividend income**

In the case of equity investments recognized in the balance sheet at historical cost, dividend income is accounted for in the income statement at the time when the right to dividend is established. In the case of equity investments recognized in the balance sheet with equity method, dividend income is already included in the measurement with the accrual concept, initially recognized in the measurement with the equity method.

**6.26. Other operating income and expenses**

Other operating income and expenses include items not related directly to the Group's operations. These are in particular income and expenses on sale and liquidation of fixed assets, received and paid indemnities, income and expenses on other services provided or acquired by the Group to a marginal extent.

**6.27. Income tax expense**

Tax charge on profit before tax is composed of the current tax and deferred tax.

Current tax for the period is calculated by the Group on the basis of the accounting profit before tax adjusted with income as stated in books, which, under the tax law in force, is not taxable income, and on the basis of accounting expenses which are not deductible expenses. In addition, profit before tax as stated in books is adjusted with accounting revenue and expenses, which were realized for tax purposes in the period.

Deferred income tax recognized as an element of tax charge on profit before tax is calculated as the net effect of the change in deferred tax assets and liabilities.

**6.28. Held-for-sale fixed assets and discontinued operations**

Prior to the classification as 'held-for-sale', assets (and all assets and liabilities in the held-for-sale group) are revalued according to IFRS 5. Further, fixed assets and held-for-sale assets are measured at the lower of: present carrying amount or fair value less costs to sell.

Discontinued operation is an element of the Group's operations, which constitutes the Group's separate major line of business or its geographical area of operations, or if it is a subsidiary acquired exclusively with a view to resale. The Group recognizes operations as discontinued upon sale or classification as 'held-for-sale'.

## 6.29. Comparable data

Where necessary, comparable data were restated so as to take account for changes in accounting and presentation principles effective on 1 January 2005. The description of adjustments of comparable data has been presented in Note 66.

## 7. Accounting estimates

The preparation of financial statements in conformity with IFRS requires a professional judgment of an entity's Management Board on the adopted accounting principles and accounting estimates applied with respect to balance sheet items and income statement items. Estimates are related to uncertain future events and are made basing on historical data and a number of assumptions based on the facts available at the time, resulting from internal and external conditions. The actual results of future business operations may differ from the present accounting estimates. Therefore, accounting estimates are verified on a regular basis. Changes in estimates are recognized in the financial statement in the period they were made.

The most important accounting estimates prepared for the purpose of this financial statement refer to:

- measurement of financial assets and liabilities at fair value, including derivatives for which no active market exists;
- identification and measurement of impairment charges for financial assets measured at amortized cost and historical cost;
- value of deferred tax assets;
- provisions.

### 7.1. Valuation of financial assets and liabilities at fair value

In the case of financial assets and liabilities recognized in the balance sheet at fair value, for which no active market is identified, they are measured on the basis of generally adopted measurement models based on variables that can be observed in the market environment. Certain variables, e.g. future interest rates, volatility parameters, correlations, must be assessed professionally. The models and variables are verified on a regular basis. The change in adopted models or variables in these models might affect accounting estimates related to measurement.

### 7.2. Impairment of financial assets valued at amortized cost and historical cost

Loan receivables constitute the most significant class of financial assets recognized in the Group's balance sheet at amortized cost or historical cost.

Under IAS 39, all receivables are subject to impairment assessment, not only receivables with higher credit risk.

The methodology of assessment evidence of loan impairment has been established in cooperation with the Bank's Major Shareholder on the basis of the Group's experience acquired in the banking sector, analyzing historical data over a long time and taking into account the current specific character of the local market and the nature of the financial assets portfolios managed by the Group.

#### **7.2.1. Evidence of impairment**

The analysis of the evidence indicating the risk of impairment is performed for individual loans as well as portfolios (groups) of loans.

The catalogue of objective evidence takes into account quantitative and qualitative data in static and dynamic terms, in relation to both the servicing of credit exposure by the borrower as well as his financial and economic situation, the management and control processes, market and macro-economic environment, what is reflected in the possibility of generating financial resources necessary to cover the indebtedness.

The evidence items listed are graded in terms of their significance; impairment may be evidenced by one circumstance or a combination of circumstances.

In the case of receivables portfolios, the indicators concerning all homogenous assets that may be identified, assessed and quantified in relation to the entire portfolios, but not the individual receivables, constitute the evidence of impairment.

#### **7.2.2. Measurement of individual impairment**

Individual impairment is measured for all loan receivables in the case of which certain individual evidence of impairment was identified with regard to all evidence of impairment for a given exposure and a given borrower, including mainly the credit risk and the risk of a borrower's insolvency, the probability of recovering amounts due, the transferability of assets being material collateral and the period of recovering amounts due and the collection of collateral.

The process of estimating future, expected cash flows are carried out in an especially dedicated IT tool.

An estimation of a possibility of recovering the collateral is prepared in the case of those receivables for which the debt recovery value of collateral is the only expected future cash flow. The Bank bases the estimation on statistical data collected and updated on a regular basis, related to the historical effectiveness of debt recovery as well as present market value of particular type of collateral, adjusted with the costs of the recovery.

The quality of the measurement of individual impairment of loan receivables is verified during a multi-stage independent process.

### 7.2.3. Measurement of portfolio impairment

In the event where no objective evidence of loan impairment assessed on individual basis occurred, regardless of whether or not it constitutes a significant reporting item, such exposure is included in the credit portfolio of similar nature and the portfolio analysis of the impairment is conducted.

Homogenous loans portfolios are created basing upon similar characteristics of credit risks that are specific for the defined groups of customers and products.

The portfolio impairment is measured basing on historical parameters of losses generated by similar assets portfolios. Historical trends for losses are cleared of one-off events and are updated against a current risk profile of homogenous groups of assets. Thus, the continuous risk of portfolios is identified, and a defined probability exists that this risk will transform into individual losses.

The process of estimating portfolio provision is performed on a quarterly basis and is directly monitored by the Bank's Credit Committee and the Bank's Management Board. The following phenomena, apart from calibrated historical trends, have material impact on the level of the portfolio provision:

- fluctuations in the receivables portfolio, for which individual impairment is not identified;
- the Group's operating effectiveness in credit risk management processes, particularly taking into account the restructuring and debt collecting activities;
- Poland's macroeconomic situation and its direct impact on the material ratios applied in the banking sector;
- the Group's credit policy for selected sectors of economy as well as receivables portfolios compared with the models adopted by other banks.

As the Group took advantage of exemptions indicated in IFRS 1 and did not restate the comparable data as provided in IAS 39, a carrying amount of loan receivables as of 1 January 2004 and 31 December 2004 was disclosed in accordance with the Polish accounting principles effective in the Bank and in the Group on these days. The Polish principles required the classification of credit exposures into 5 risk groups (normal, under observation, substandard, doubtful and loss), applying a criterion of timely debt coverage and a criterion of the borrower's economic and financial standing. Specific provisions for the risk connected with credit exposures have been established at least in the amounts required for the particular risk groups (from 1.5% to 100% of the base of establishment of the specific provisions). The Group, while estimating the amount of specific provisions for the purpose of the Polish principles, estimated the value of collateral as required by the regulations in force as well as the internal principles adopted by the Group.

### 7.3. The value of deferred tax assets

As presented in the Group's consolidated financial statement as of 31 December 2004, the accounting principle related to the measurement of deferred tax assets applied in 2003 and 2004 provided that, at the Bank, bearing in mind balance sheet and tax losses in 2002 and 2003 and the uncertainty of the

settlement of the excess of deferred tax asset over deferred tax liability, deferred tax assets were recognized only up to the amount of deferred tax liability.

The positive trend in the operating income generated by the Bank is a proof of increasing probability of settling tax losses accumulated in previous years. The Bank, as of 30 June 2005, bearing in mind the Bank's improving financial result, decided to recognize an excess of deferred tax asset over deferred tax liability in the amount that is probable to be generated in the future. The accounting policy adopted by the Bank stipulates in this respect that at the end of each of the quarters, the Bank assesses the probability of realizing net deferred tax asset and recognizes the amount in the amount of the probable future realization amount on that account. The probability of realizing the net deferred tax asset is determined on the basis of financial plans and tax forecasts prepared by the Bank's Management Board, updated at the end of each quarter.

## 8. Segment reporting

The Group applies a basic division into business segments subject to the reporting requirement. The Group's operations are not diversified in geographical terms. Operations are focused on the Polish market; the main customer base is composed of Polish natural and legal persons and foreign customers operating on the Polish market.

The Group is organized into four basic sector segments: corporate, retail, treasury and investment.

Corporate Segment entails transactions with large companies (with annual income exceeding PLN 6 million) as well as state budgetary units at the central and local levels. Beside the traditional deposit, credit and settlement services, other specific services are offered. They are tailored to customers' individual needs, e.g. organizing syndicates supporting investment projects, financing real estate transactions, financing foreign trade and bulk payments. The Bank's offer in this segment is expanded by the products of Kredyt Lease, which offers a complete range of services for companies in respect of leasing of fixed assets and real estates, and also of real estate trade.

Retail Segment incorporates products targeted at individual customers as well as Small and Medium-size Enterprises (SME), which annual income does not exceed PLN 6 million. The products on offer comprise a wide range of deposit and loan products, insurance products (banc assurance and assure banking) offered in co-operation with WARTA S.A. as well as clearing services. This offer is addressed to customers through traditional channels of distribution via the Bank's nationwide network of branches as well as KB24, an Internet network. The results of this segment also comprise the result of Żagiel S.A. specializing in the sale of installment loans as well as in intermediation in the distribution of selected services offered by the Bank and WARTA. Furthermore, the Bank's offer for this segment includes products offered by KBC TFI sale of shares in investment funds.

Treasury Segment comprises the result of the transactions performed by the Bank on its own account as an active participant of the money market (Treasury and NBP bills), bonds market (Treasury and commercial bonds), currency market and interbank market. The result of the segment also includes net income on derivative instruments transactions: forward, FX swap, IRS, CIRS, FRA, interest rate and currency options.



Investment Segment incorporates the Group's equity investments in shares of companies whose core business is focused on generating added value for the Group by specializing in non-banking areas of operation, and also on investments in the shares of companies with an expected high long-term rate of return. In addition, the segment focuses on custodian services.

The segment's income and expenses had been determined before inter-segmental exclusions were made. The selling prices exercised among segments are calculated on the basis of the transfer prices methodology. Income and expenses that may not be rationally allocated to any of the segments are disclosed in 'unallocated costs' and 'unallocated income' items. The Bank's expenses are not allocated internally to individual segments. For the purpose of this financial statement, the expenses were allocated using the allocation keys, such as the structure of employment, usable area or the extent of segment's activities as measured with the value of assets and liabilities.

Net profit (loss) of segments presented in the segment note for 2004 included in the Bank's financial statement as at 31 December 2004 differ from the results included in this financial statement due to new rules of calculating inter-company receivables and liabilities between segments as well as a process of profound restructuring, which helped implement considerable changes in the organization structure of segments. In addition, since the beginning of 2005, the Bank has expanded the system of the valuation of internal funds transfers by including the measurement of specific provisions. It means that in 2005, the costs of financing loans and credit activities are calculated on the basis of net value, while in the previous year, they were calculated on the basis of gross value.

As at 31.12.2005 the Bank has not maintained the previous segmentation scheme and data gathering system has been changed what resulted in difficulties for comparable data for year 2004. As a result of the above segment reporting note for a year 2005 is not comparable with the note for the year 2004.

**Consolidated income statement for the period 01.01.2005–31.12.2005**

	Corpora Segme	Retail Segment	Treasury Segment	Investment Segment	Other	Exclusion	Total
1. Segment income (external)	583 782	907 689	492 761	84 358	91 064	-205 905	<b>1 953 749</b>
2. Segment income (internal)	194 090	497 409	531 186	0	14	-1 222 699	<b>0</b>
<b>3. Total segment income</b>	<b>777 872</b>	<b>1 405 098</b>	<b>1 023 947</b>	<b>84 358</b>	<b>91 078</b>	<b>-1 428 604</b>	<b>1 953 749</b>
4. Segment expense (external)	-175 549	-444 695	-287 462	-64 987	-56 687	205 905	<b>-823 475</b>
4a. Allocated costs	-141 563	-599 165	-31 714	-22 174	-6 370	0	<b>-800 986</b>
5. Segment expenses (internal)	-293 440	-228 312	-691 512	-9 435	0	1 222 699	<b>0</b>
<b>6. Total segment expenses</b>	<b>-610 552</b>	<b>-1 272 172</b>	<b>-1 010 688</b>	<b>-96 596</b>	<b>-63 057</b>	<b>1 428 604</b>	<b>-1 624 461</b>
<b>7. Segment result</b>	<b>167 320</b>	<b>132 926</b>	<b>13 259</b>	<b>-12 238</b>	<b>28 021</b>	<b>0</b>	<b>329 288</b>
<b>8. Net impairment charges for financial assets, other assets and provisions</b>	<b>73 999</b>	<b>-56 426</b>	<b>0</b>	<b>-2 486</b>	<b>-24 254</b>	<b>0</b>	<b>-9 167</b>
<b>9. Share in the net profit of subordinated companies measured by the equity method</b>	<b>0</b>	<b>0</b>	<b>0</b>	<b>1 247</b>	<b>0</b>	<b>0</b>	<b>1 247</b>
<b>10. Segment result</b>	<b>241 319</b>	<b>76 500</b>	<b>13 259</b>	<b>-13 477</b>	<b>3 767</b>	<b>0</b>	<b>321 368</b>
11. Profit on discontinued operations							<b>974</b>
12. Income tax							<b>93 536</b>
<b>13. Net profit/(loss)</b>	<b>241 319</b>	<b>76 500</b>	<b>13 259</b>	<b>-13 477</b>	<b>3 767</b>	<b>0</b>	<b>415 878</b>

**Consolidated balance sheet as at 31.12.2005**

	Corporate Segment	Retail Segment	Treasury Segment	Investment Segment	Other	Exclusion and consolidation adjustments	Total
1. Segment assets	5 305 601	4 960 354	10 226 697	607 743	0	-610 526	20 489 869
2. Segment investments in subordinated companies measured with equity method	0	0	0	8 929	0	0	8 929
3. Other assets (unallocated)	0	0	0	0	0	0	342 546
<b>4. Total assets</b>	<b>5 305 601</b>	<b>4 960 354</b>	<b>10 226 697</b>	<b>616 672</b>	<b>0</b>	<b>-610 526</b>	<b>20 841 344</b>
5. Segment liabilities	4 312 381	10 514 937	4 251 054	150 191	0	-610 526	18 618 037
6. Equity	0	0	0	1 681 595	0	0	1 681 595
7. Unallocated liabilities	0	0	0	0	0	0	541 712
<b>8. Total liabilities and equity</b>	<b>4 312 381</b>	<b>10 514 937</b>	<b>4 251 054</b>	<b>1 831 786</b>	<b>0</b>	<b>-610 526</b>	<b>20 841 344</b>
Equity investments (costs of assets acquisition)	965	7 079	0	35	69 763		77 842
Depreciation	24 406	90 721	8 214	11 144	998		135 483

**Consolidated income statement for the period 01.01.2004–31.12.2004**

	Corpora Segme	Retail Segment	Treasury Segment	Investment Segment	Other	Exclusions	Total
1. Segment income (external)	673 871	1 097 381	374 847	305 668	44 242	-360 731	<b>2 135 278</b>
2. Segment income (internal)	187 922	513 644	593 316	0	0	-1 294 882	<b>0</b>
<b>3. Total segment income</b>	<b>861 793</b>	<b>1 611 025</b>	<b>968 163</b>	<b>305 668</b>	<b>44 242</b>	<b>-1 655 613</b>	<b>2 135 278</b>
4. Segment expenses (external)	-246 339	-610 045	-237 088	-177 913	-31 632	360 731	<b>-942 286</b>
4a. Allocated costs	-148 996	-647 668	-32 495	-29 724	-7 040		<b>-865 923</b>
5. Segment expenses (internal)	-330 864	-238 981	-701 566	-21 957	-1 514	1 294 882	<b>0</b>
<b>6. Total segment expenses</b>	<b>-726 199</b>	<b>-1 496 694</b>	<b>-971 149</b>	<b>-229 594</b>	<b>-40 186</b>	<b>1 655 613</b>	<b>-1 808 209</b>
<b>7. Segment result</b>	<b>135 594</b>	<b>114 331</b>	<b>-2 986</b>	<b>76 074</b>	<b>4 056</b>	<b>0</b>	<b>327 069</b>
<b>8. Net impairment charges for financial assets, other assets and provisions</b>	<b>-56 484</b>	<b>-118 867</b>	<b>0</b>	<b>-14 599</b>	<b>41 654</b>	<b>0</b>	<b>-148 296</b>
<b>9. Share in profit of subordinated companies measured with the equity method</b>				<b>1</b>			<b>1</b>
<b>10. Segment result</b>	<b>79 110</b>	<b>-4 536</b>	<b>-2 986</b>	<b>61 476</b>	<b>45 710</b>	<b>0</b>	<b>178 774</b>
11. Income tax expense							<b>-20 032</b>
12. Profit allocated to minority shareholders							<b>-1 902</b>
<b>13. Net profit</b>	<b>79 110</b>	<b>-4 536</b>	<b>-2 986</b>	<b>61 476</b>	<b>45 710</b>	<b>0</b>	<b>156 840</b>

**Balance sheet as at 31.12.2004**

	Corporate Segment	Retail Segment	Treasury Segment	Investment Segment	Other	Exclusio and consolidation adjust + tments	Total
1. Segment assets	6 690 525	5 253 694	8 595 421	2 413 216	0	-2 647 876	20 304 980
2. Segment investments in subordinated companies measured with equity method							0
3. Other assets (unallocated)							641 104
<b>4. Total assets</b>	<b>6 690 525</b>	<b>5 253 694</b>	<b>8 595 421</b>	<b>2 413 216</b>	<b>0</b>	<b>-2 647 876</b>	<b>20 946 084</b>
5. Segment liabilities	3 442 719	10 969 803	5 089 610	2 133 241	0	-2 647 876	18 987 497
6. Equity				1 517 088			1 517 088
7. Unallocated capitals							441 499
<b>8. Total liabilities and equity</b>	<b>3 442 719</b>	<b>10 969 803</b>	<b>5 089 610</b>	<b>3 650 329</b>	<b>0</b>	<b>-2 647 876</b>	<b>20 946 084</b>
Equity investments (costs of assets acquisition)	108	2 003	0	14 899	59 680		76 690
Depreciation	32 737	117 735	5 562	9 373	1 205		166 612

## 9. Interest income

	01.01.2005- 31.12.2005	01.01.2004- 31.12.2004
Amounts due from banks	120 993	150 568
Loans and advances to customers	959 109	861 404
- from financial sector	10 902	12 739
- from non-financial sector	881 808	781 857
- from the budgetary sector	66 399	66 808
Fixed yield securities	327 615	288 053
- held for trading	13 248	18 085
- available for sale	241 634	215 416
- held to maturity	72 733	54 552
Receivables from securities acquired under repurchase agreements	787	2 216
Other	0	732
<b>Total</b>	<b>1 408 504</b>	<b>1 302 973</b>

Interest income in 2005 includes PLN 43,519 thousand of interest calculated under an accrual basis, that the Bank, as at the balance sheet date, did not receive in cash, on receivables with recognized impairment. Interest was calculated with the effective interest rate applied to discounting expected cash flows for the purpose of estimating the impairment of loan receivables. Accrued interest was taken into consideration when estimating impairment charges for loan receivables. In comparable data for 2004, as the Group took advantage of exemptions indicated in IFRS 1 and did not restate the comparable data as provided in IAS 39, interest income on doubtful receivables in the income statement was recognized on the cash basis.

## 10. Interest expense

	01.01.2005- 31.12.2005	01.01.2004- 31.12.2004
Amounts due to banks	84 761	152 204
Amounts due to customers	469 915	440 032
- from financial sector	36 647	14 296
- from non-financial sector	364 888	341 375
- from the budgetary sector	68 380	84 361
Securities sold under repurchase agreements	28 476	10 362
Issued securities, including:	33 530	31 472
- subordinated securities	33 530	31 472
Other subordinated liabilities	23 535	23 934
Other	14 840	11 042
<b>Total</b>	<b>655 057</b>	<b>669 046</b>
<b>Net interest income</b>	<b>753 447</b>	<b>633 927</b>

## 11. Fee and commission income

	01.01.2005- 31.12.2005	01.01.2004- 31.12.2004
Fees and commissions on loans	115 111	274 859
Fees and commissions on deposit-related transactions with customers	123 373	127 947
Fees and commissions due for the servicing of payment cards and ATMs	49 817	46 412
Brokerage commissions	0	3 696
On foreign clearing operations	13 275	13 124
On guarantee commitments	105	4 646
Commission on distribution of investment and insurance services	18 782	6 510
Other fees and commissions	14 118	60 324
<b>Total</b>	<b>334 581</b>	<b>537 518</b>

## 12. Fee and commission expense

	01.01.2005- 31.12.2005	01.01.2004- 31.12.2004
Participation of agents in arrangement fee	164	2 993
Fees and commissions on loans borrowed	2 738	1 772
Fees and commissions due for the servicing of payment cards and ATMs	13 727	7 676
Costs of guarantee commitments	70	5 084
Other fees and commissions	2 992	6 352
<b>Total</b>	<b>19 691</b>	<b>23 877</b>
<b>Net fee and commission income</b>	<b>314 890</b>	<b>513 641</b>

## 13. Dividend income

	01.01.2005- 31.12.2005	01.01.2004- 31.12.2004
Available-for-sale securities	780	817
<b>Total</b>	<b>780</b>	<b>817</b>

## 14. Net trading income

	01.01.2005- 31.12.2005	01.01.2005- 31.12.2004
Net trading income, including:		
- on debt securities	6 852	1 912
- on derivatives	84 632	13 572
- foreign exchange	47 914	113 796
- other	4 414	9 331
<b>Total</b>	<b>143 812</b>	<b>138 611</b>



## 15. Profit/(loss) on investment activity

	01.01.2005 - 31.12.2005	01.01.2004- 31.12.2004
From available-for-sale assets and held-to-maturity assets:		
- from equity instruments	5 632	29 055
- from debt instruments	-9 686	14 462
<b>Total</b>	<b>-4 054</b>	<b>43 517</b>

## 16. Other operating income

	01.01.2005- 31.12.2005	01.01.2004- 31.12.2004
Management of third party assets	0	3 696
Disposal of or liquidation of fixed assets and disposable assets	737	18 506
Recovered bad debts and debt recovery costs	18 774	22 688
Indemnities, penalties and fines received	7 534	1 587
Side income	6 516	5 904
Reversal of impairment charges for amounts due from other debtors	5 154	9 141
Reimbursement of remuneration for distribution of Group's products	18 294	7 322
Reorganization and winding-up of the Bank's business units	0	1 314
Other operating income	9 063	41 684
<b>Total</b>	<b>66 072</b>	<b>111 842</b>

## 17. General and administrative expenses

	01.01.2005- 31.12.2005	01.01.2004- 31.12.2004
<b>Staff costs, including:</b>	<b>410 533</b>	<b>426 892</b>
Salaries and wages	335 962	361 818
Salaries and wages mark-up	56 236	59 793
Employee benefits	11 257	791
Training expenses	7 078	4 490
<b>Operating expense, including:</b>	<b>344 809</b>	<b>461 671</b>
Costs of buildings maintenance and lease	117 405	115 420
Postal and telecommunication expenses	50 546	63 614
IT systems operation costs	25 560	32 709
Public relation and advertising services	30 279	14 795
Costs of machinery repairs and services provided under warranties	12 175	16 068
Property protection costs	17 191	29 096
Costs of balance sheet audit, consulting and advisory	12 291	24 145
Leasing fees	6 191	5 374
Transportation costs	8 935	12 777
Business trips	4 215	4 112
Taxes and fees	12 435	21 357
Costs incurred on account of the Bank Guarantee Fund	3 252	4 457
Other	44 334	117 747
<b>Depreciation, including:</b>	<b>135 483</b>	<b>166 612</b>
Fixed assets	91 371	118 582
Intangible assets	44 112	48 030
<b>Total</b>	<b>890 825</b>	<b>1 055 175</b>

### Operating lease rentals

Leasing contracts under which the lessor retains the whole risk and all rewards arising from the possession of the leased property, are accounted for as an operating lease. Fees under operating lease are recognized as expenses in the income statement on a straight-line basis over the period of leasing.

Contracts of operating lease under which the parent company acts as the lessee are mainly related to the lease of real estate and real estate used by the parent company in the normal course of business. All contracts are executed on market terms, without any exceptional or non-standard terms or conditions.

Under operating leases, the parent company operates two Headquarters buildings, which, towards the end of 2004, were sold to companies, not related to the Bank and are now leased back from them. Sale transactions were executed on market terms; contracts of lease were also executed on market terms. The contracts are executed for 10 years and their terms provide for the possibility of their extension, without the terms set out on the day of their executions. Under the contracts, the parent company has no guaranteed repurchase right to the buildings after the 10-year term of lease.

Gross leasing payments paid by the Group and recognized in particular reporting periods as operating expense were as follows (in gross terms):

<b>31.12.2005</b>	<b>31.12.2004</b>
68 092	60 096

The major portions of fee were the fees for the leasing of real estates.

The total amount of future gross minimum leasing fees that the Group is obliged to pay under irrevocable contracts of leasing, determined as at the balance sheet date, is as follows:

	<b>31.12.2005</b>	<b>31.12.2004</b>
- up to 1 year	74 831	92 149
- from 1 to 5 years	221 840	312 432
- over 5 years	91 829	110 953
<b>Total</b>	<b>388 500</b>	<b>515 534</b>

## 18. Change in impairment charges and provisions

### *Creation of impairment charges and provisions*

	01.01.2005- 31.12.2005	01.01.2004- 31.12.2004
<b>Creation of impairment charges and provisions</b>	<b>701 206</b>	<b>2 013 237</b>
Credits and loans	562 688	1 757 371
Available-for- sale financial assets	1 564	0
Equity investments	0	1 276
Assets to be disposed, property, equipment and intangible assets	24 421	25 197
Other assets	15	0
<b>Total impairment charges</b>	<b>588 688</b>	<b>1 783 844</b>
Provision for restructuring	0	2 000
Provisions for other future liabilities	11 420	3 063
Off-balance sheet liabilities	101 098	224 330
<b>Total provisions</b>	<b>112 518</b>	<b>229 393</b>
<b>Total</b>	<b>701 206</b>	<b>2 013 237</b>

### *Reversal of impairment charges and provisions*

	01.01.2005- 31.12.2005	01.01.2004- 31.12.2004
<b>Reversal of impairment charges and provisions</b>	<b>692 039</b>	<b>1 867 574</b>
Credits and loans	618 413	1 619 267
Available-for- sale financial assets	71	6 081
Equity investments	417	2 062
Assets to be disposed, tangible and intangible assets	5 934	12 631
Other assets	22	0
<b>Total impairment charges</b>	<b>624 857</b>	<b>1 640 041</b>
Provisions for employee benefits	0	563
Provisions for other future liabilities	0	989
Off-balance sheet liabilities	67 182	225 981
<b>Total provisions</b>	<b>67 182</b>	<b>227 533</b>
<b>Total</b>	<b>692 039</b>	<b>1 867 574</b>
<b>Net impairment charges for financial assets, other assets and provisions</b>	<b>-9 167</b>	<b>-145 633</b>

## 19. Other operating expenses

	01.01.2005- 31.12.2005	01.01.2004- 31.12.2004
Management of third party assets	0	3 536
Disposal of or liquidation of fixed assets, intangible assets and disposable assets	3 984	23 317
Written off receivables and debt recovery expenses	23 759	3 544
Indemnities, penalties and fines paid	1 120	603
Banks' incidental expense	216	282
Donations	242	53
Insurance	7 564	7 006
Sponsoring	1 210	1 323
Reorganization and winding-up of the Bank's business units	117	1 177
Other impairment charges	6 474	4 644
Other expenses	10 148	17 259
<b>Total</b>	<b>54 834</b>	<b>62 744</b>

## 20. Income tax expense in the income statement

	01.01.2005- 31.12.2005	01.01.2004- 31.12.2004
Current income tax	-6 394	-22 162
Deferred income tax	99 930	2 130
<b>Income tax on net profit</b>	<b>93 536</b>	<b>-20 032</b>

**Current income tax presented in the income statement**

	01.01.2005- 31.12.2005	01.01.2004- 31.12.2004
<b>Gross financial result</b>	<b>321 368</b>	<b>178 774</b>
Net profit on discontinued operations	974	0
Non-deductible income from associates	-1 247	-1
Consolidation adjustments	902	44 699
<b>Permanent differences</b>	<b>-34 160</b>	<b>-15 297</b>
Impairment charges	-103 364	-111 263
Dividends received	-780	2 471
Depreciation – non tax deductible expenses	2 142	11 124
Penalty interest	1 116	605
Other, including:	<b>66 726</b>	<b>81 766</b>
- income generated abroad	0	-1 512
- donations	206	242
- voluntary membership fees	0	206
- free benefits	1	18
- PFRON	3 784	3 796
- valuation of shares not held for sale	13 281	-27 399
- loss on sale of receivables	43 348	0
- differences arising on IFRS (net profit recalculation)	0	58 647
- other	6 106	47 768
<b>Temporary differences</b>	<b>-103 884</b>	<b>-4 757</b>
Accrued interest to be paid	-46 261	9 287
Bought out purchased interest	21 116	3 235
Valuation of derivatives	-9 123	9 358
Tax goodwill	-40 914	-44 643
Accruals for expenses	11 339	6 624
Finance lease	6 148	10 871
Accrued interest to be received	-44 938	-3 913
Unamortized fixed assets – investment tax relief	919	291
Difference between tax and accounting depreciation rates	22 292	-43 628
Impairment charges – temporary difference	-35 410	0
Commissions and held to maturity securities - EIR	17 600	0
Commissions on accounts	2 218	0
Other temporary differences	-8 870	47 761
<b>Total</b>	<b>183 953</b>	<b>203 419</b>

Prior period tax losses settlements	-149 984	-56 111
Reliefs and donations	-505	-24 423
<b>Tax base for income tax calculation</b>	<b>33 464</b>	<b>122 885</b>
Income tax rate	19%	19%
<b>Income tax</b>	<b>-6 359</b>	<b>-23 348</b>
Current income tax paid abroad not to be deducted in local tax settlement	-35	-1 838
Tax waivers	0	3 024
<b>Current income tax</b>	<b>-6 394</b>	<b>-22 162</b>

#### ***Deferred income tax presented in the income statement***

	<b>01.01.2005- 31.12.2005</b>	<b>01.01.2004- 31.12.2004</b>
Increase due to establishment and reversal of temporary differences	98 285	126 049
Write-off of income tax assets as no possibility to settle in future periods	0	-128 329
Other elements of deferred tax	1 645	4 410
<b>Total deferred tax</b>	<b>99 930</b>	<b>2 130</b>

As mentioned in the Group's consolidated financial statement in note 6 as of 31 December 2004 deferred tax asset was recognized only up to the amount of the deferred tax liability.

The Bank, as of 30 June 2005, bearing in mind the Bank's improving financial performance, decided to recognize an excess of the deferred tax asset over deferred tax liability in the amount that will probably be generated in the future. The accounting policy adopted by the Bank stipulates in this respect that, at the end of each quarter, the Bank assesses the probability of realizing net deferred tax asset and recognizes it in the amount of the probable future realization amount on that account. The probability of realizing net deferred tax asset is determined on the basis of financial plans and tax forecasts prepared by the Bank's Management Board, updated on an ongoing basis as at the end of each quarter.

The Bank's subsidiaries recognize provision for deferred tax for all temporary differences and the probability of realizing deferred tax asset is determined on the basis of financial plans approved by the Management Boards of subsidiaries.

**Reconciliation of effective tax rate**

	31.12.2005	31.12.2004
<b>Gross financial result</b>	321 368	178 774
Net profit on discontinued operations	974	0
Non-deductible income from associates	-1 247	-1
Tax on gross financial result	-61 241	-33 967
<b>Permanent differences</b>	<b>3 467</b>	<b>2 906</b>
Other differences, which become permanent	20 688	0
Recognized deferred tax asset from prior periods	102 215	0
Other	5 269	18 669
Losses from previous periods not recognized in deferred tax asset	28 497	10 558
Donations	89	24
Tax deductions	-5 414	-18 583
Tax waiver	0	3 024
Current income tax paid abroad not to be deducted in local tax settlement	-34	-39
Reversal of deferred tax provision – liquidation of Vilnius branch	0	399
<b>Tax charge</b>	<b>93 536</b>	<b>-20 032</b>

**21. Earnings per Bank's shareholders**

	01.01.2005- 31.12.2005	01.01.2004- 31.12.2004
Net profit (loss) of the parent company for 12 months	410 488	126 528
Net profit (loss) of subsidiaries for 12 months	8 273	77 537
Consolidation adjustments	-2 883	-47 225
<b>Net profit (loss) per Bank's shareholders</b>	<b>415 878</b>	<b>156 840</b>



## 22. Earnings per share (EPS)

	01.01.2005- 31.12.2005	01.01.2004- 31.12.2004
Net profit (loss) for 12 months	415 878	156 840
Weighted average number of ordinary shares	271 658 880	243 783 743
<b>Net profit (loss) per share</b>	<b>1,53</b>	<b>0,64</b>

Earnings per share calculated as the quotient of profit per Bank's shareholders and weighted average number of shares. Kredyt Bank S.A. Capital Group does not calculate diluted earnings per share due to the absence of capital categories causing dilution.

## 23. Cash and balances with Central Bank

### By types

	31.12.2005	31.12.2004
Cash in hand	385 068	487 119
Current account in the central bank	222 022	1 025 472
<b>Total</b>	<b>607 090</b>	<b>1 512 591</b>

### By currencies

	31.12.2005	31.12.2004
- in PLN	551 121	1 441 984
- in foreign currencies (by currency and translated into PLN)	55 969	70 607
- in EURO	29 556	40 170
- in USD	20 334	22 763
- in GBP	4 673	5 481
- in CHF	960	1 567
- other currencies	446	626
<b>Total</b>	<b>607 090</b>	<b>1 512 591</b>

As at 31 December 2005, cash on the Bank's current account in the National Bank of Poland maintained for central bank statutory reserve amounted to PLN 509,457 thousand. As at 31 December 2004, cash amounted to PLN 571,363 thousand.

## 24. Amounts due from banks

### By types

	31.12.2005	31.12.2004
Current accounts	22 598	12 819
Deposits in other banks	2 151 218	2 641 488
Loans and advances to banks	37 121	36 191
Other	6	0
Interest	18 672	9 354
<b>Total</b>	<b>2 229 615</b>	<b>2 699 852</b>

### By currencies

	31.12.2005	31.12.2004
in PLN	676 623	1 013 545
in foreign currencies (by currency and translated into PLN)	1 552 992	1 686 307
- in EURO	536 425	867 361
- in USD	931 001	746 783
- in GBP	32 852	64 410
- in CHF	37 655	368
- other currencies	15 059	7 385
<b>Total</b>	<b>2 229 615</b>	<b>2 699 852</b>

### By maturity dates

	31.12.2005	31.12.2004
- up to 1 month	1 249 077	2 054 733
- 1-3 months	392 722	354 817
- 3-6 months	153 226	32 679
- 6 months to 1 year	375 904	225 909
- 1 - 3 years	0	18 586
- 3 - 5 years	37 120	0
- past due	2 894	3 774
- interest	18 672	9 354
<b>Total</b>	<b>2 229 615</b>	<b>2 699 852</b>

**Gross receivables**

	31.12.2005	31.12.2004
Receivables with no allowance for individual impairment	2 208 049	2 687 304
Receivables with allowances for individual impairment	2 894	3 194
Interest	18 672	9 354
<b>Total</b>	<b>2 229 615</b>	<b>2 699 852</b>

As at 31 December 2005, average effective interest rates of term deposits in other banks were as follows (by main currencies):

- in EUR – 2.38%
- in GBP – 4.65%
- in PLN – 4.45%
- in USD – 4.2%

All deposits were fixed interest rate deposits.

**25. Allowance for impairment losses for receivables due from banks**

	31.12.2005	31.12.2004
Allowances for impairment losses for receivables due from banks at period beginning	3 194	3 194
Adjustments related to first adoption of IFRS	0	0
Allowances for impairment losses for receivables due from banks at period beginning	3 194	3 194
a) increase	0	0
b) decrease	0	0
c) utilization	300	0
Receivables written off in the period as bad debts	300	0
<b>Period end</b>	<b>2 894</b>	<b>3 194</b>

## 26. Financial assets at fair value through profit and loss

	31.12.2005	31.12.2004
<b>Debt securities</b>	<b>487 618</b>	<b>338 292</b>
Treasury securities	202 189	337 634
-bonds	162 130	163 670
-bills	40 059	173 964
Central Bank securities	280 754	0
-bills	280 754	0
Other securities	4 675	658
-bonds	4 675	658
<b>Equity investments</b>	<b>0</b>	<b>19</b>
<b>Derivatives</b>	<b>216 270</b>	<b>219 449</b>
<b>Total</b>	<b>703 888</b>	<b>557 760</b>

	31.12.2005	31.12.2004
<b>Listed</b>		
-shares	0	19
-bonds	166 805	164 328
-bills	320 813	173 964
-derivatives	216 270	219 449
<b>Total</b>	<b>703 888</b>	<b>557 760</b>

### Derivatives (by types)

	31.12.2005		31.12.2004	
	Assets	Liabilities	Assets	Liabilities
<b>Interest rate transactions</b>	<b>161 378</b>	<b>178 384</b>	<b>165 226</b>	<b>149 978</b>
IRS	145 617	160 257	146 791	129 152
FRA	15 761	18 127	18 435	20 826
<b>foreign exchange transactions</b>	<b>54 816</b>	<b>35 510</b>	<b>54 147</b>	<b>76 322</b>
FX swap	20 792	23 612	38 668	66 450
CIRS	17 997	0	0	0
Forward	5 754	5 595	7 779	5 612
Options purchased	10 180	0	7 648	0
Options sold	0	6 233	0	4 186
other	93	70	52	74
<b>embedded instruments</b>	<b>76</b>	<b>6 261</b>	<b>76</b>	<b>7 632</b>
<b>Total</b>	<b>216 270</b>	<b>220 155</b>	<b>219 449</b>	<b>233 932</b>

**Derivatives (by maturity dates)**

	31.12.2005		31.12.2004	
	Assets	Liabilities	Assets	Liabilities
<b>Interest rate transactions (fair value)</b>	161 378	178 384	<b>165 226</b>	<b>149 978</b>
<b>Interest rate transactions (nominal value)</b>	<b>38 991 520</b>	<b>32 705 565</b>	<b>13 950 000</b>	<b>12 746 000</b>
- up to 1 month	475 000	125 000	1 400 000	1 250 000
- 1-3 months	2 725 000	2 375 000	2 625 000	875 000
- 3-6 months	13 115 000	8 370 000	1 925 000	2 200 000
- 6 months to 1 year	19 681 000	19 010 000	4 946 000	5 575 000
- 1 - 3 years	2 364 000	2 332 000	1 718 000	1 527 000
- 3 - 5 years	418 920	346 965	1 111 000	1 094 000
- 5 - 10 years	212 600	146 600	225 000	225 000
<b>foreign exchange transactions (fair value)</b>	<b>54 816</b>	<b>35 510</b>	<b>54 147</b>	<b>76 321</b>
<b>foreign exchange transactions (nominal value)</b>	<b>3 957 279</b>	<b>3 944 799</b>	<b>1 986 909</b>	<b>2 013 441</b>
- up to 1 month	1 759 760	1 754 708	1 177 758	1 188 445
- 1-3 months	849 522	850 060	261 751	251 787
- 3-6 months	583 706	581 157	163 876	176 239
- 6 months to 1 year	377 141	379 520	285 367	296 963
- 1 - 3 years	387 150	379 354	98 157	100 007
<b>Total fair value</b>	<b>216 194</b>	<b>213 894</b>	<b>219 373</b>	<b>226 299</b>
<b>Total nominal value</b>	<b>42 948 799</b>	<b>36 650 364</b>	<b>15 936 909</b>	<b>14 759 441</b>

\* excluding embedded derivatives

**Debt securities**

	31.12.2005	31.12.2004
- up to 1 month	293 218	80
- 1-3 months	55	7 584
- 3-6 months	5 989	58 033
- 6 months to 1 year	51 452	128 954
- 1 - 3 years	63 077	85 288
- 3 - 5 years	13 612	46 840
- 5 - 10 years	55 133	8 400
- 10 - 20 years	5 082	3 113
<b>Total</b>	<b>487 618</b>	<b>338 292</b>

**Financial assets at fair value through profit and loss by currencies**

	31.12.2005	31.12.2004
in PLN	672 083	542 994
in foreign currencies (by currency and translated into PLN)	31 805	14 766
- in EURO	20 604	4 477
- in USD	10 148	9 765
- in GBP	1 046	524
- other currencies	7	0
<b>Total</b>	<b>703 888</b>	<b>557 760</b>

**27. Loans and advances to customers****By types**

	31.12.2005	31.12.2004
Loans and advances	11 596 124	13 338 424
Purchased debt	362 779	460 017
Realized guarantees and sureties	64 618	44 517
Other receivables	202 869	223 514
- including lease receivables	148 128	183 184
Interest	<b>79 896</b>	<b>39 480</b>
<b>Total</b>	<b>12 306 286</b>	<b>14 105 952</b>

**By currencies**

	31.12.2005	31.12.2004
in PLN	9 129 178	10 301 653
in foreign currencies (by currency and translated into PLN)	3 177 108	3 804 299
- in EURO	1 410 783	2 202 244
- in USD	533 283	705 995
- in GBP	0	1 293
- in CHF	1 231 043	893 821
- other currencies	1 999	946
<b>Total</b>	<b>12 306 286</b>	<b>14 105 952</b>

**By maturity dates**

	31.12.2005	31.12.2004
- up to 1 month	241 596	1 314 543
- 1-3 months	645 479	427 357
- 3-6 months	541 630	522 609
- 6 months to 1 year	2 632 167	1 931 232
- 1 - 3 years	1 757 551	1 732 905
- 3 - 5 years	1 111 266	1 199 684
- 5 - 10 years	1 498 527	1 259 624
- 10 - 20 years	964 944	1 262 614
- over 20 years	419 051	347 516
- past due	2 414 179	4 068 388
- interest	79 896	39 480
<b>Total</b>	<b>12 306 286</b>	<b>14 105 952</b>

	31.12.2005	31.12.2004
<b>Natural persons*</b>	<b>5 495 506</b>	<b>5 411 244</b>
- overdraft facilities	514 368	508 949
- purchased debt	307 103	356 344
- term loans	2 636 524	2 973 278
- mortgage loans	2 035 351	1 569 314
- realized guarantees	2 160	2 160
- other receivables	0	1 199
<b>Corporate customers</b>	<b>6 065 342</b>	<b>7 384 165</b>
- overdraft facilities	934 801	920 983
- term loans	4 809 558	6 094 900
- purchased debt	55 656	103 610
- realized guarantees	62 458	42 357
- other receivables	202 869	222 315
<b>Budget</b>	<b>665 542</b>	<b>1 271 063</b>
- overdraft facilities	1 921	12 933
- term loans	663 601	1 258 067
- purchased debt	20	63
<b>Interest</b>	<b>79 896</b>	<b>39 480</b>
<b>Total</b>	<b>12 306 286</b>	<b>14 105 952</b>

\* The item contains: amounts due from private persons, individual entrepreneurs, individual farmers, and noncommercial institutions providing services for households

**By classifications**

	31.12.2005	31.12.2004
Receivables with no allowance for individual impairment	8 739 256	9 819 191
Receivables with allowances for individual impairment	3 487 134	4 247 281
Interest	79 896	39 480
<b>Total</b>	<b>12 306 286</b>	<b>14 105 952</b>

As at 31 December 2005, the unsettled loan commissions amortized with the effective interest rate, which, according to the concept of the measurement of financial assets at amortized cost decreases the value of gross receivables, amounted to PLN 179,282 thousand. This amount has been already recognized in total receivables presented in the note above.

As presented in Note 65, in the comparable data as at 31 December 2004, the Group, taking advantage of exemptions indicated in IFRS 1, decided not to restate the comparable data as provided in IAS 39, that is, among others, related to the measurement of financial assets with the effective interest rate method and the measurement of impairment of loan receivables portfolio. In the comparable data, the carrying amount of assets measured at amortized cost is recognized in line with accounting principles set out in Polish regulations in force as at these dates.

In the case of receivables for which impairment loss was identified, the total value of collateral approved by the Group considered for estimated impairment charges for loans as at 31 December 2005 amounted to PLN 1,111,126 thousand. As at 31 December 2004, this value was equal to PLN 1,499,036 thousand.

As at 31 December 2005, average effective interest rates of loan receivables were as follows (by main currencies):

- in CHF – 4.1%
- in EUR – 4.7%
- in PLN – 9.6%
- in USD – 6.6%



## 28. Allowances for impairment losses for loans and advances to customers

	01.01.2005– 31.12.2005	01.01.2004– 31.12.2004
Allowances for impairment losses for loans and advances to customers at period beginning	2 740 428	2 855 544
Adjustments related to first adoption of IFRS	179 336	42 084
Allowances for impairment losses for loans and advances to customers at period beginning	2 919 764	2 897 628
a) increase	549 587	1 629 475
- impairment charge for loans and advances	547 355	1 629 475
- other changes (inter-account movements)	2 232	0
b) decrease	614 343	1 643 715
- decrease due to company exclusion from consolidation		43 995
- reversal of impairment charges for loans and advances	595 710	1 524 401
- other changes (inter-account movements)	4 192	14 744
- currency translation differences	14 441	60 575
c) utilization	250 802	142 960
- loan receivables written off in the period as bad debts	250 802	142 960
<b>Period end</b>	<b>2 604 206</b>	<b>2 740 428</b>

In addition, as at 31 December 2005, PLN 89,886 thousand of the impairment charge for incurred but not reported (IBNR), credit losses for homogenous receivables portfolios is included in the total impairment charge for loan receivables. In 2005, the charge was reversed for the amount of PLN 45 786 thousand.

## 29. Finance lease receivables and change in charges for leasing receivables

	31.12.2005	31.12.2004
Gross investments in finance lease	168 907	210 872
Unrealized financial income	-20 779	-27 688
Net investments in finance lease	148 128	183 184
Gross investments in finance lease for each period	168 905	210 872
- below 1 year	57 149	79 339
- between 1 and 5 years	105 862	102 637
- over 5 years	5 894	28 896
Net investments in finance lease for each period	148 128	183 184
- below 1 year	49 095	74 436
- between 1 and 5 years	96 536	91 482
- over 5 years	2 497	17 266

**Impairment charges for leasing receivables**

	01.01.2005- 31.12.2005	01.01.2004- 31.12.2004
As at period beginning after the opening balance adjustment - IFRS application	39 403	30 913
a) increase	56 687	16 200
- impairment charges for lease receivables	56 687	16 200
b) reversal	44 885	7 710
- reversal of impairment charges for lease receivables	42 717	7 531
- other changes (inter-account movements)	2 168	179
<b>Closing balance</b>	<b>51 205</b>	<b>39 403</b>

**30. Investment securities**

	31.12.2005	31.12.-004
<b>Available-for-sale securities</b>	<b>4 417 879</b>	<b>2 450 200</b>
Treasury securities	2 037 957	1 795 655
-bonds	2 003 354	1 271 701
-bills	34 603	523 954
Central Bank securities	2 208 510	561 520
-bonds	336 847	335 950
-bills	1 871 663	225 570
Other securities	169 397	13 603
-bonds	159 382	4 624
-shares in investment funds	10 015	8 979
Equity securities	2 015	79 422
<b>Held-to-maturity securities</b>	<b>2 291 832</b>	<b>1 462 671</b>
Treasury securities	2 114 595	1 251 345
-bonds	2 114 595	1 251 345
Other securities	177 237	211 326
-bonds	177 237	211 326
<b>Total</b>	<b>6 709 711</b>	<b>3 912 871</b>

All investment securities classified in the portfolio of available-for-sale financial assets are measured at fair value, except for NBP bonds issued for the purpose of statutory reserve of banks, commercial bonds of the Industry Development Agency and non-listed minority equity investments (equity investments in shares of the Bank's Capital Group are presented in Note 31). NBP bonds and commercial bonds are measured at amortized cost, and equity investments are recognized at cost, as their fair value cannot be determined reliably.

	31.12.2005	31.12.2004
<b>Available-for-sale securities</b>	<b>4 417 879</b>	<b>2 450 200</b>
<b>Listed</b>	<b>4 261 501</b>	<b>2 376 636</b>
-shares	0	5 862
-bonds	2 345 220	1 612 271
-bills	1 906 266	749 524
-shares in investment funds	10 015	8 979
<b>Non-listed</b>	<b>156 378</b>	<b>73 564</b>
-shares	2 015	73 560
-bonds	154 363	4
<b>Held-to-maturity securities</b>	<b>2 291 832</b>	<b>1 462 671</b>
<b>Listed</b>	<b>2 291 832</b>	<b>1 288 490</b>
-bonds	2 291 832	1 288 490
<b>Non-listed</b>	<b>0</b>	<b>174 181</b>
-bonds	0	174 181
<b>Total</b>	<b>6 709 711</b>	<b>3 912 871</b>

**Movement in available-for-sale investment securities**

	01.01.2005- 31.12.2005	01.01.2004- 31.12.2004
<b>Period beginning</b>	<b>2 450 200</b>	<b>2 340 680</b>
Adjustments related to first adoption of IFRS	-669 413	0
<b>Period beginning</b>	<b>1 780 787</b>	<b>2 340 680</b>
Increase	45 818 202	10 060 868
- acquisitions	45 742 805	9 939 141
- other increase	75 397	121 727
Decrease	43 181 110	9 951 348
- sale	43 180 145	9 947 253
- other decrease	965	4 095
<b>Period end</b>	<b>4 417 879</b>	<b>2 450 200</b>

**Financial assets subject to hedge accounting**

Hedged assets – available-for-sale bonds

Bond nominal value	Maturity date	Interest rate	Coupon rate payment	Measurement as at 31.12.2005
25 389	24.10.2013	fix 5%	annually	-374
24 118	24.11.2010	fix 6%	annually	50
14 400	24.03.2010	fix 5,75%	annually	-194
<b>Total</b>				<b>-518</b>

IRS's hedging fair value of bonds

Nominal value	Maturity date	Interest rate		Coupon rate payment		Valuation at 31.12.2005
		coupon received	coupon paid	coupon received	coupon paid	
26 000	03.10.2013	WIBOR 6M	fix 4,595%	every 6 months	annually	593
25 000	16.12.2010	WIBOR 3M	fix 5,11%	every 3 months	annually	-184
15 000	12.04.2010	WIBOR 3M	fix 4,66%	every 3 months	annually	123
<b>Total</b>						<b>532</b>

The rules of recognizing and measuring the effectiveness of the hedges for transactions subject to hedge accounting are described in Notes 6.6.7 and 70 of this financial statement.

### ***Movement in held-to-maturity investment securities***

	01.01.2005- 31.12.2005	01.01.2004- 31.12.2004
<b>Period beginning</b>	<b>1 462 671</b>	<b>1 765 272</b>
Adjustments related to first adoption of IFRS	-193 509	0
<b>Period beginning</b>	<b>1 269 162</b>	<b>1 765 272</b>
Increase	1 251 792	112 554
- acquisitions	1 222 391	88 110
- other increase	29 401	24 444
Decrease	229 122	415 155
- redemption	229 122	415 155
<b>Period end</b>	<b>2 291 832</b>	<b>1 462 671</b>

### ***Available-for-sale investment securities***

	31.12.2005	31.12.2004
- up to 1 month	1 871 663	260 833
- 1-3 months	48 025	207 801
- 3-6 months	149 613	369 605
- 6 months to 1 year	110 033	194 196
- 1 - 3 years	903 021	310 476
- 3 - 5 years	627 526	406 471
- 5 - 10 years	695 968	662 765
- with unspecified maturity dates	12 030	38 053
<b>Total</b>	<b>4 417 879</b>	<b>2 450 200</b>

**Held-to-maturity investment securities**

	31.12.2005	31.12.2004
- 1-3 months	26 960	0
- 3-6 months	168 179	15 555
- 6 months to 1 year	559 018	0
- 1 - 3 years	803 489	841 263
- 3 - 5 years	646 866	163 892
- 5 - 10 years	87 320	441 961
<b>Total</b>	<b>2 291 832</b>	<b>1 462 671</b>

**Available-for-sale investment securities**

	31.12.2005	31.12.2004
	4 202 465	2 450 129
in foreign currencies (by currency and translated into PLN)	215 414	71
- in EURO	143 719	71
- in USD	71 695	0
<b>Total</b>	<b>4 417 879</b>	<b>2 450 200</b>

**Held-to-maturity investment securities**

	31.12.2005	31.12.2004
	2 114 595	1 322 792
in foreign currencies (by currency and translated into PLN)	177 237	139 879
- in EURO	82 050	87 733
- in USD	95 187	52 146
<b>Total</b>	<b>2 291 832</b>	<b>1 462 671</b>

After 1 January 2005, the Group has not reclassified any securities from the portfolio of held-to-maturity securities to other portfolios.

**31. Equity investments in subsidiaries and associates**

Equity investments and shares in subsidiaries classified as available-for-sale.

	31.12.2005	31.12.2004
Other financial institutions	34 266	33 843
Non- financial institutions	1 424	1 424
<b>Total</b>	<b>35 690</b>	<b>35 267</b>

**Equity investments in non-consolidated subsidiaries and associates as at 31.12.2005**

Equity investments in subsidiaries and associates as at 31 December 2005																		
Lp.	a	b																
	company	line of business	carrying amount of shares	total assets	shareholders' equity, including					liabilities including:			receivables			sales	Bank's stake in capital (%)	Bank's share in total number of votes (%)
					share capital	reserve capital	other shareholders' capital including:			short-term liabilities	long-term liabilities		short-term receivables	long-term receivables				
							retained earnings	net profit (loss)										
<b>subsidiaries</b>																		
1.	KB Zarządzanie Aktywami S.A. *	funds' asset management	15 012	16 487	16 478	15 012	246	1 220	380	840	9	9	0	16 487	16 487	0	11 789	100
2.	BFI Serwis Sp. z o.o.*	banking investments	19 254	19 546	19 527	19 250	4 081	-3 805	0	-3 805	19	19	0	17 103	17 103	0	872	100
3.	PTE S.A. ***	open pension fund management	0	0	0	0		0	0	0	0		0	0	0	0	100	100
4.	Net Banking Sp. z o.o. *	internet banking	1 424	1 623	1 609	1 425	0	184	0	45	14	14	0	1 623	1 623	0	69	100
<b>Total</b>			<b>35 690</b>	<b>37 656</b>	<b>37 614</b>	<b>35 687</b>	<b>4 327</b>	<b>-2 401</b>	<b>380</b>	<b>-2 920</b>	<b>42</b>	<b>42</b>	<b>0</b>	<b>35 213</b>	<b>35 213</b>	<b>0</b>	<b>12 730</b>	
<b>associates</b>																		
4.	KBC Towarzystwo Funduszy Inwestycyjnych S.A.	funds' asset management	8 929	54 921	29 765	25 258	451	4 055	0	4 055	24 554	24 554	0	44 112	44 112	0	37 736	30
<b>Total</b>			<b>8 929</b>	<b>54 921</b>	<b>29 765</b>	<b>25 258</b>	<b>451</b>	<b>4 055</b>	<b>0</b>	<b>4 055</b>	<b>24 554</b>	<b>24 554</b>	<b>0</b>	<b>44 112</b>	<b>44 112</b>	<b>0</b>	<b>37 736</b>	

\*unaudited data

\*\* classifies as available for sale

\*\*\* liquidation of PTE has been formally completed on 30.11.2005 and application for deletion from Court Register has been made

On 22 December 2005, the Extraordinary General Meeting of Shareholders of PTE Kredyt Bank S.A. approved the company's winding-up report and on 23 December 2005 the financial statement was submitted, along with the resolution of the Extraordinary General Meeting of Shareholders, to the Registry Court for the capital city of Warsaw, with a request to delete PTE Kredyt Bank S.A. from the National Court Register. As a result of a failure to receive an official decision on the company's deletion from the National Court Register and of the transfer of cash from the investment in this company to the Bank, the carrying amount of the company's shares is recognized as zero.

**Equity investments in non-consolidated subsidiaries and associates as at 31.12.2004**

Equity investments in subsidiaries and associates as at 31 December 2004																			
	a	b	c	d	e						f			g			h	i	j
Lp.	company	line of business	carrying amount of shares	total assets	shareholders' equity, including						liabilities including:			receivables			sales	Bank's stake in capital (%)	Bank's share in total number of votes (%)
					share capital	reserve capital	other shareholders' capital including:		short-term liabilities	long-term liabilities		short-term receivables	long-term receivables						
							retained earnings	net profit (loss)											
1.	KB Zarządzanie * Aktywami S.A.	zarządzanie aktywami klientów na zlecenie, działalność	15 012	15 063	14 978	15 012	183	-217	63	-280	66	66	0	5 684	5 684	0	1 349	100	100
2.	BFI Serwis Sp. z o.o.	* świadczenie usług pośrednictwa i doradztwa	18 831	23 345	23 331	19 250	3 434	647	0	647	14	14	0	16 465	16 465	0	793	100	100
3.	Net Banking Sp. z o.o.	* doradztwo w zakresie sprzętu komputerowego, oprogramowania,	1 424	1 585	1 564	1 425	0	139	0	25	20	20	0	1 584	1 584	0	68	100	100
Total			35 267	39 993	39 873	35 687	3 617	569	63	392	100	100	0	23 733	23 733	0	2 210		

\*unaudited data

\*\* classifies as available for sale

### 32. Investments in associates measured with the equity method

	31.12.2005	31.12.2004
Other financial institutions	8 929	0
<b>Total</b>	<b>8 929</b>	<b>0</b>

#### Equity investments – net value

	31.12.2005			31.12.2004		
	Purchase price	Impairment allowance	Net value	Purchase price	Impairment allowance	Net value
Kredyt Trade Sp. z o.o.	36 697	0	36 697	36 697	0	36 697
BFI Serwis Sp. z o.o.	19 249	0	19 249	19 249	-418	18 831
Victoria Development Sp. z o.o.	18 100	0	18 100	18 100	0	18 100
Żagiel S.A.	141 231	-141 231	0	141 231	-141 231	0
Kredyt Lease S.A.	43 712	-42 886	826	28 712	-28 712	0
Kredyt International Finance B.V.	67	0	67	67	0	67
PTE Kredyt Bank S.A.	0	0	0	159 200	-123 586	35 614
Net Banking Sp. z o.o.	1 424	0	1 424	1 424	0	1 424
KB Zarządzanie Aktywami S.A.	15 012	0	15 012	15 012	0	15 012
Zakłady Przemysłu Jedwabniczego "Dolwis" S.A.	2 914	-2 914	0	2 914	-2 914	0
<b>Total</b>	<b>278 406</b>	<b>-187 031</b>	<b>91 375</b>	<b>422 606</b>	<b>-296 861</b>	<b>125 745</b>

### 33. Tangible fixed assets

	31.12.2005	31.12.2004
<b>Fixed assets, including:</b>	<b>376 305</b>	<b>456 670</b>
- land	18 209	14 363
- buildings and premises	211 578	229 947
- plant and machinery	71 905	131 093
- motor vehicles	8 010	3 237
- other fixed assets	66 603	78 030
Construction in progress	40 095	12 701
<b>Total</b>	<b>416 400</b>	<b>469 371</b>

As at 31 December 2005, the Group identified impairment of a few real estates. The impairment was measured by independent appraisers basing on generally accepted valuation methods based on comparable market transactions and models of discounted cash flows generated for these specific real estates treated as cash generating units under IAS 36.



### 34. Movement of fixed assets

*For the period of 12 months ended 31.12.2005*

	Land (including right to perpetual usufruct of land)	Buildings, premises and civil- and hydro- engineering structures	Plant and machinery	Motor vehicles	Other fixed assets	Construction in progress	Total fixed assets
a) Gross fixed assets as at 01.01.2005	15 371	253 897	501 075	11 595	129 526	18 323	<b>929 787</b>
b) Increase	10 472	66 615	22 889	7 002	2 060	22 430	<b>131 468</b>
- acquisition	1 349	20 525	19 872	4 140	2 060	12 953	<b>60 899</b>
- other increase	9 123	46 090	3 017	2 862	0	9 477	<b>70 569</b>
c) Decrease	1 082	34 876	47 196	4 160	4 065	497	<b>91 876</b>
- sale	773	25 595	35 098	2 956	503	10	<b>64 935</b>
- liquidation	52	984	9 272	243	2 890	0	<b>13 441</b>
- adjustments -change of the consolidation scope	0	0	752	0	24	0	<b>776</b>
- other decreases	257	8 297	2 074	961	648	487	<b>12 724</b>
d) Gross fixed assets as at 31.12.2005	24 761	285 636	476 768	14 437	127 521	40 256	<b>969 379</b>
e) Accumulated depreciation of fixed assets as at 01.01.2005	1 008	22 783	368 390	7 744	50 101	0	<b>450 026</b>
f) Net fixed assets at period beginning – as at 01.01.2005	14 363	229 947	131 093	3 237	78 030	12 701	<b>469 371</b>
g) changes in depreciation	283	37 515	34 225	-1 317	10 105	0	<b>80 811</b>
- amortization	325	7 239	69 028	2 300	12 479	0	<b>91 371</b>
- sale	-25	-1 589	-25 028	-2 809	-422	0	<b>-29 873</b>
- liquidation	0	-564	-8 949	-152	-1 702	0	<b>-11 367</b>
- adjustments -change of the consolidation scope	0	0	-745	0	-14	0	<b>-759</b>
- other changes	-17	32 429	-81	-656	-236	0	<b>31 439</b>

**For the period of 12 months ended 31.12.2005 (cont.)**

	Land (including right to perpetual usufruct of land)	Buildings, premises and civil- and hydro- engineering structures	Plant and machinery	Motor vehicles	Other fixed assets	Construction in progress	Total fixed assets
h) accumulated depreciation as at 31.12.2005	1 291	60 298	402 615	6 427	60 206	0	<b>530 837</b>
i) impairment charges as at 01.01.2005	0	1 167	1 592	614	1 395	5 622	<b>10 390</b>
- increase	5 261	22 726	814	0	0	161	<b>28 962</b>
- decrease	0	10 133	158	614	683	5 622	<b>17 210</b>
j) Impairment charges as at 31.12.2005	5 261	13 760	2 248	0	712	161	<b>22 142</b>
<b>Net fixed assets as at 31.12.2005</b>	<b>18 209</b>	<b>211 578</b>	<b>71 905</b>	<b>8 010</b>	<b>66 603</b>	<b>40 095</b>	<b>416 400</b>

**For the period of 12 months ended 31.12.2004**

	Land (including right to perpetual usufruct of land)	Buildings, premises and civil- and hydro- engineering structures	Plant and machinery	Motor vehicles	Other fixed assets	Construction in progress	Total fixed assets
a) Gross fixed assets as at 01.01.2004	35 196	452 863	527 395	23 871	144 364	27 160	<b>1 210 849</b>
b) increase	371	74 963	24 168	1 050	13 702	479	<b>114 733</b>
- acquisition	49	36 218	12 351	907	13 665	479	<b>63 669</b>
- other increase	322	38 745	11 817	143	37	0	<b>51 064</b>
c) decrease	20 196	273 929	50 488	13 326	28 540	9 316	<b>395 795</b>
- adjustments -change of the consolidation scope	1 928	47 402	6 502	8 781	24 708	844	<b>90 165</b>
- sale	9 213	137 176	29 980	2 753	1 551	116	<b>180 789</b>
- liquidation	0	10	5 197	11	2 010	2	<b>7 230</b>
- other decreases	9 055	89 341	8 809	1 781	271	8 354	<b>117 611</b>
d) gross fixed assets as at 31.12.2004	15 371	253 897	501 075	11 595	129 526	18 323	<b>929 787</b>
e) accumulated depreciation of fixed assets at period beginning as at 01.01.2004	1 788	44 643	301 726	13 871	50 443	0	<b>412 471</b>
f) Net fixed assets as at 01.01.2004	33 408	405 432	225 657	10 000	93 921	22 585	<b>791 003</b>
g) changes in depreciation	-780	-21 860	66 664	-6 127	-342	0	<b>37 555</b>

**For the period of 12 months ended 31.12.2004 (cont.)**

	Land (including right to perpetual usufruct of land)	Buildings, premises and civil- and hydro- engineering structures	Plant and machinery	Motor vehicles	Other fixed assets	Construction in progress	Total fixed assets
- adjustments -change of the consolidation scope	-82	-2 910	-2 667	-5 386	-11 290	0	<b>-22 335</b>
- depreciation	512	12 889	89 488	2 743	12 950	0	<b>118 582</b>
- sale	-1 210	-12 720	-14 144	-1 624	-381	0	<b>-30 079</b>
- liquidation	0	-583	-5 105	-347	-1 399	0	<b>-7 434</b>
- other changes	0	-18 536	-908	-1 513	-222	0	<b>-21 179</b>
h) accumulated depreciation as at 31.12.2004	1 008	22 783	368 390	7 744	50 101	0	<b>450 026</b>
i) impairment charges as at 01.01.2004	0	2 788	12	0	0	4 575	<b>7 375</b>
- increase	0	1 337	1 592	614	1 395	1 047	<b>5 985</b>
- decrease	0	2 958	12	0	0	0	<b>2 970</b>
j) impairment charges as at 31.12.2004	0	1 167	1 592	614	1 395	5 622	<b>10 390</b>
<b>Net fixed assets as at 31 December 2004</b>	<b>14 363</b>	<b>229 947</b>	<b>131 093</b>	<b>3 237</b>	<b>78 030</b>	<b>12 701</b>	<b>469 371</b>

### 35. Intangible assets

	31.12.2005	31.12.2004
Patents, licenses and similar rights, including:	101 101	120 159
- software	101 101	120 159
Other intangible assets	10 374	20 028
<b>Total intangible assets</b>	<b>111 475</b>	<b>140 187</b>

The Group does not have intangible assets with indefinite useful lives.

### 36. Movement of intangible assets

*For the period of 12 months ended 31.12.2005*

	Patents, licenses and similar rights	including: software	Other intangible assets	Total intangible assets
a) gross intangible assets as at 01.01.05	246 610	243 469	60 844	307 454
b) increase	25 362	25 362	6 700	32 062
- acquisition	10 243	10 243	6 700	16 943
- other increase	15 119	15 119	0	15 119
c) decrease	5 781	5 224	16 525	22 306
- sale	2 882	2 882	0	2 882
- adjustments -change of the consolidation scope	898	341	0	898
- other decreases	2 001	2 001	16 525	18 526
d) gross intangible assets as at 31.12.2005	266 191	263 607	51 019	317 210
e) accumulated amortization as at 01.01.2005	126 274	123 133	40 816	167 090
f) Gross intangible assets as at 01.01.2005	120 159	120 159	20 028	140 187
g) amortization for the period	37 463	38 020	-171	37 292
- amortization	42 848	42 848	1 264	44 112
- sale	-2 733	-2 733	0	-2 733
- liquidation	-1 794	-1 794	-1 049	-2 843
- adjustments -change of the consolidation scope	-898	-341	0	-898
- other changes	40	40	-386	-346
h) accumulated amortization as at 31.12.2005	163 737	161 153	40 645	204 382
i) impairment charges as at 01.01.05	177	177	0	177
- increase	1 176	1 176	0	1 176
- decrease	0	0	0	0
j) impairment charges as at 31.12.2005	1 353	1 353	0	1 353
<b>Net intangible assets as at 31.12.2005</b>	<b>101 101</b>	<b>101 101</b>	<b>10 374</b>	<b>111 475</b>

**For the period of 12 months ended 31.12.2004**

	Patents, licenses and similar rights	including: software	Other intangible assets*	Total intangible assets
a) gross intangible assets as at 01.01.04	229 448	222 080	78 895	308 343
b) increase	23 648	25 971	16	23 664
- acquisition	13 005	12 964	16	13 021
- other increase	10 643	13 007	0	10 643
c) decrease	6 486	4 582	18 067	24 553
- adjustments -change of the consolidation scope	3 097	1 201	285	3 382
- sale	938	937	1 949	2 887
- other decreases	2 451	2 444	15 833	18 284
d) gross intangible assets as at 31.12.2004	246 610	243 469	60 844	307 454
e) accumulated amortization as at 01.01.04	88 474	85 233	39 219	127 693
f) gross intangible assets as at 01.01.04	140 974	136 847	39 676	180 650
g) amortization for the period	37 800	37 900	1 597	39 397
- adjustments -change of the consolidation scope	-673	-501	0	-673
- amortization	41 343	41 268	6 687	48 030
- sale	-720	-720	-381	-1 101
- liquidation	-2 015	-2 012	-493	-2 508
- other changes	-135	-135	-4 216	-4 351
h) accumulated amortization as at 31.12.2004	126 274	123 133	40 816	167 090
i) impairment charges as at 01.01.04	0	0	446	446
- increase	177	177	0	177
- decrease	0	0	446	446
j) impairment charges as at 31.12.2004	177	177	0	177
<b>Net intangible assets as at 31.12.2004</b>	<b>120 159</b>	<b>120 159</b>	<b>20 028</b>	<b>140 187</b>

### 37. Goodwill on subordinated companies

	31.12.2005	31.12.2004
Goodwill on subordinated companies	36 052	36 052
<b>Total goodwill on subordinated companies</b>	<b>36 052</b>	<b>36 052</b>

#### *Movement of goodwill on subordinated companies*

	01.01.2005- 31.12.2005	01.01.2004- 31.12.2004
a) gross goodwill at period beginning	66 285	95 717
b) increase	0	100
- acquisition of shares	0	100
c) decrease	0	29 532
- disposal of KBU shares	0	29 532
<b>d) gross goodwill at period end</b>	<b>66 285</b>	<b>66 285</b>
e) write-down of goodwill at period beginning	30 233	48 523
- opening balance adjustment	0	-18 290
<b>f) write-down of goodwill at period end</b>	<b>30 233</b>	<b>30 233</b>
<b>g) net goodwill at period end</b>	<b>36 052</b>	<b>36 052</b>

In comparable data as at 1 January 2004, the Group ceased to amortize goodwill. As at this date, goodwill of the companies consolidated by the Bank is equal to the net values recognized in the 2003 closing balance. Every six months, the Group carries out net goodwill impairment test based on the models developed in cooperation with the Bank's major shareholder. The models are based on generally applied rules of equity investments measurement, i.e. they take into consideration discounted future cash flows.

### 38. Deferred tax assets

Deferred tax asset	31.12.2005	31.12.2004	Change in 2005.
Accrued interest to be paid	48 072	94 317	-46 245
Bought out purchased interest	90 611	69 495	21 116
Valuation of derivatives	53 326	86 204	-32 878
Commissions and held to maturity securities - EIR	131 974	154 116	-22 142
Tax goodwill	56 593	97 507	-40 914
Accruals for expenses	61 480	50 141	11 339
Finance lease	23 685	54 458	-30 773
Impairment charges – temporary difference	454 630	510 340	-55 710
Valuation of trading portfolio	2 520	22 570	-20 050
Tax losses to be settled in future	112 012	0	112 012
Commissions on accounts	18 734	16 516	2 218
Other	174 255	44 796	129 459
<b>Total</b>	<b>1 227 892</b>	<b>1 200 460</b>	<b>27 432</b>
Tax rate	19%	19%	0
<b>Deferred tax assets</b>	<b>233 299</b>	<b>228 087</b>	<b>5 212</b>
Charged to revaluation reserve	479	0	479
Charged to profit and loss account	232 820	228 087	4 733
Unrecognized assets	36 499	142 390	-105 891
Assets recognized in profit and loss account	196 321	85 697	110 624
<b>Total deferred tax asset</b>	<b>196 800</b>	<b>85 697</b>	<b>111 103</b>
<b>Deferred tax liability note 45**</b>	<b>-83 832</b>	<b>-75 262</b>	<b>-8 570</b>
<b>Deferred tax net assets</b>	<b>112 968</b>	<b>10 435</b>	<b>102 533</b>

\* In comparison with the data presented in financial statement as at 30 June 2005 the Bank has changed the amount of the surplus of unrecognized deferred tax asset over deferred tax liability. The change resulted from identification of unrecognized items in the deferred tax calculation. The change has not influenced the level of deferred tax recognized or tax charge for the year 2004 because of significant amount of unrecognized surplus of deferred tax asset over deferred tax liability.

\*\* The difference between amounts presented in this note and amounts presented in note 45 results from the differences in deferred tax presentation by the Group entities (some of them present it on a net basis).



### 39. Other assets

	31.12.2005	31.12.2004
Fixed assets to be disposed	1 619	8 154
Fixed assets to be sold	5 848	0
Inventory	773	683
<b>Other, including:</b>	<b>148 688</b>	<b>195 424</b>
Various debtors	136 729	181 245
Prepaid expenses	10 950	13 498
Other assets	1 009	681
<b>Total</b>	<b>156 928</b>	<b>204 261</b>

The Bank has divided from the fixed assets position assets for sale, which are presented at fair value in other assets. The assets cover real estates, which have not been any longer used by the Bank for its activity.

### 40. Amounts due to banks

#### *Amounts due to banks (by types)*

	31.12.2005	31.12.2004
Current accounts	20 000	24 535
Term deposits	1 587 919	204 094
Loans and advances	949 858	2 767 422
Other amounts due	0	500
Interest	4 390	10 539
<b>Total</b>	<b>2 562 167</b>	<b>3 007 090</b>

#### *Amounts due to banks (by currencies)*

	31.12.2005	31.12.2004
in PLN	944 116	420 378
in foreign currencies (by currency and translated into PLN)	1 618 051	2 586 712
- in EURO	835 429	1 787 106
- in USD	406 690	1 560
- in GBP	2	2
- in CHF	373 628	796 711
- other currencies	2 302	1 333
<b>Total</b>	<b>2 562 167</b>	<b>3 007 090</b>

**Amounts due to banks (by maturity dates)**

	31.12.2005	31.12.2004
- up to 1 month	1 462 522	184 088
- 1-3 months	115 355	233 974
- 3-6 months	15 016	279 227
- 6 months to 1 year	15 000	203 950
- 1 - 3 years	23	1 874 952
- 3 - 5 years	949 695	0
- 5 - 10 years	166	220 360
- interest	4 390	10 539
<b>Total</b>	<b>2 562 167</b>	<b>3 007 090</b>

As at 31 December 2005, average effective interest rates of term deposits accepted from other banks were as follows (by main currencies):

- in EUR – 2.39%
- in USD – 4.35%
- in PLN – 4.34%

All deposits were fixed interest rate deposits.

**41. Amounts due to customers****Amounts due to customers (by types)**

	31.12.2005	31.12.2004
- in current account	6 731 028	5 125 440
- term deposits	7 668 900	8 764 523
- loans and advances	95 448	110 052
- interest	38 248	61 090
<b>Total</b>	<b>14 533 624</b>	<b>14 061 105</b>

**Amounts due to customers (by currencies)**

	31.12.2005	31.12.2004
in PLN	11 818 742	11 765 089
in foreign currencies (by currency and translated into PLN)	2 714 882	2 296 016
- in EURO	1 305 361	975 534
- in USD	1 280 441	1 232 094
- in GBP	105 301	68 528
- in CHF	11 112	14 758
- other currencies	12 667	5 102
<b>Total</b>	<b>14 533 624</b>	<b>14 061 105</b>

**Amounts due to customers (by maturity dates)**

	31.12.2005	31.12.2004
- up to 1 month	10 780 122	9 090 093
- 1-3 months	1 816 801	2 468 467
- 3-6 months	894 819	1 156 233
- 6 months to 1 year	677 193	685 962
- 1 - 3 years	213 739	384 938
- 3 - 5 years	5 049	78 334
- 5 - 10 years	106 054	131 944
- 10 - 20 years	1 599	3 984
- over 20 years	0	60
- interest	38 248	61 090
<b>Total</b>	<b>14 533 624</b>	<b>14 061 105</b>

**Amounts due to customers**

	31.12.2005	31.12.2004
<b>Natural persons*</b>	<b>9 063 921</b>	<b>9 177 815</b>
- in current account	3 841 765	2 530 744
- term deposits	5 222 156	6 647 071
<b>Corporate customers</b>	<b>3 742 862</b>	<b>3 113 027</b>
- in current account	1 593 871	1 240 084
- term deposits	2 053 543	1 762 891
- loans and advances	95 448	110 052
<b>Budget</b>	<b>1 688 593</b>	<b>1 709 173</b>
- in current account	1 295 392	1 354 612
- term deposits	393 201	354 561
<b>Interest</b>	<b>38 248</b>	<b>61 090</b>
<b>Total</b>	<b>14 533 624</b>	<b>14 061 105</b>

\* the item contains: amounts due to private persons, individual entrepreneurs, individual farmers, noncommercial institutions providing services for households

As at 31 December 2005, 92% of customers' deposits were current accounts and other fixed interest rate products, whose maturity dates, as at the balance sheet date, did not exceed 6 months.

As at 31 December 2005, average effective interest rates of customer term deposits were as follows (by main currencies):

- in EUR – 1.4%
- in GBP – 2.3%
- in PLN – 2.8%
- in USD – 1.8%

## 42. Issued debt securities

	31.12.2005	31.12.2004
Bonds	400 000	400 000
Interest	2 435	18 150
<b>Total</b>	<b>402 435</b>	<b>418 150</b>

Issued debt securities are registered perpetual bonds with interest rates based on 6M WIBOR with market margin. The issue has been taken over by the KBC Group Bank's strategic investor entities. Based on the decision of the Banking Supervisory Committee Bank classifies the issued debt securities as subordinated liabilities.

## 43. Securities sold under repurchase agreements

	31.12.2005	31.12.2004
Amounts due to other entities	367 656	716 665
Interest	1 045	2 107
<b>Total</b>	<b>368 701</b>	<b>718 772</b>

## 44. Provisions

	31.12.2005	31.12.2004
- employee benefits provision	911	1 088
- provision for off-balance sheet items	63 039	30 967
- restructuring provision	0	2 000
- provision for litigation	13 897	3 384
<b>Total</b>	<b>77 847</b>	<b>37 439</b>

**Movement in provisions**

	01.01.2005- 31.12.2005	01.01.2004 – 31.12.2004
<b>Period beginning</b>	<b>37 439</b>	<b>289 247</b>
Adjustment related to the adoption of IFRS *	0	-235 278
<b>At period beginning after opening balance adjustment</b>	<b>37 439</b>	<b>53 969</b>
- employee benefits provision	1 088	1 564
- provision for off-balance sheet items	30 967	31 743
- restructuring provision	2 000	10 300
- provision for litigation	3 384	2 616
- other	0	7 746
a) established provisions	112 845	229 774
- employee benefits provision	5	424
- provision for off-balance sheet items	101 098	224 330
- restructuring provision	0	2 000
- provision for litigation	11 742	3 020
b) utilization	-2 911	-10 300
- employee benefits provision	-69	0
- restructuring provision	-2 000	-10 300
- provision for litigation	-842	0
c) reversal	-67 682	-236 318
- employee benefits provision	-113	-338
- provision for off-balance sheet items	-67 182	-225 982
- provision for litigation	-387	-2 252
- other	0	-7 746
d) other changes	-1 844	314
- employee benefits provision	0	-562
- provision for off-balance sheet items	-1 844	876
<b>Provisions at period end</b>	<b>77 847</b>	<b>37 439</b>
- employee benefits provision	911	1 088
- provision for off-balance sheet items	63 039	30 967
- restructuring provision	0	2 000
- provision for litigation	13 897	3 384
<b>Period end</b>	<b>77 847</b>	<b>37 439</b>

\* The total of the reversal of the provisions for general risk and reversal of provision for negative assets of subsidiaries. Change of valuation method now at cost less impairment loss. Impairment loss has been recognized.

‘Provisions for employee benefits’ are composed of provisions for severance pays and provisions for retirement benefits.

## 45. Deferred tax liability

### Deferred tax expense

	31.12.2005	31.12.2004	Change in 2005
Accrued interest to be received	213 040	168 025	45 015
Unamortised fixed assets - investment tax relief	50 652	6 276	44 376
Financial instruments transactions	5 357	73 692	-68 335
Difference between accounting and tax depreciation rates	78 662	100 954	-22 292
Valuation of available for sale portfolio	20 765	4 351	16 414
Other	77 293	53 659	23 634
<b>Total</b>	<b>445 769</b>	<b>406 957</b>	<b>38 812</b>
Tax rate	19%	19%	0
<b>Deferred tax liability</b>	<b>84 696</b>	<b>77 322</b>	<b>7 374</b>
Charged to revaluation reserve	-3 946	0	-3 946
Charged to profit and loss account	80 750	77 322	3 428

## 46. Other liabilities

	31.12.2005	31.12.2004
Employee benefits	47	446
Amounts due to the State Treasury*	20 506	44 760
Various creditors	167 154	82 034
Expenses payable	51 974	48 466
Other (e.g. inter-bank clearings)	164 690	169 678
<b>Total</b>	<b>404 371</b>	<b>345 384</b>

\*This item includes receivables from sale of financial and fixed assets, deposits paid for real estates used by the Bank in the form of finance and operating lease and payment cards settlements.

## 47. Subordinated liabilities

### Movement in subordinated liabilities

	01.01.2005- 31.12.2005	01.01.2004- 31.12.2004
<b>Period beginning</b>	<b>599 286</b>	<b>766 913</b>
a) increase	23 535	23 934
- accrued interest	23 535	23 934
b) decrease	33 240	191 561
- paid interest	22 673	22 858
- currency translation differences from translation of subordinated loan in foreign currency	10 567	168 703
<b>Subordinated liabilities at period end</b>	<b>589 581</b>	<b>599 286</b>

Subordinated liabilities are recognized in the balance sheet in the amount to be paid carried at amortized cost with the effective interest rate method.

### As at 31.12.2005

Entity	Loan value by currency	in PLN '000'	Interest rate terms	Maturity date	Subordinated liabilities	Interest
KBC Bank N.V. Dublin Branch \ Banco Espirito Santo S.A. Madrid	USD	50 000	3M LIBOR +1.25%	17.01.2006	163 065	1 859
KBC Bank N.V. Dublin Branch	EUR	110 000	3M EURIBOR +1.20%	25.05.2008	424 578	79
<b>TOTAL</b>					<b>587 643</b>	<b>1 938</b>

### As at 31.12.2004

Entity	Loan value by currency	in PLN '000'	Interest rate terms	Maturity date	Subordinated liabilities	Interest
KBC Bank N.V. Dublin Branch \ Banco Espirito Santo S.A. Madrid	USD	50 000	3M LIBOR +1.25%	17.01.2006	149 520	1 034
KBC Bank N.V. Dublin Branch	EUR	110 000	3M EURIBOR +1.20%	25.05.2008	448 690	42
<b>TOTAL</b>					<b>598 210</b>	<b>1 076</b>

## 48. Equity

### **Share capital**

As at 31 December 2005, the parent company's share capital totals PLN 1,358,294 thousand and is divided into 271,658,880 shares of nominal value PLN 5.00 each. The parent company's shares are registered shares and bearer shares, but not preference shares. Each share entitles its holder to one vote at the General Meeting of Shareholders. The parent company's shares are admitted to public trading.

The analysis of registered shares and bearer shares presented below was prepared as at 31 December 2005, including the conversion of registered shares of the parent company into bearer shares made by 31 December 2005 by the National Depository for Securities.

In the period, the share capital did not change.

### **Registered shares**

Shareholders of the parent company hold 75,008 registered shares, which accounts for 0.03% of the share capital. Registered shares are shares of the following series:

- » A (2,942 shares),
- » C (1,425 shares),
- » F (8,578 shares),
- » P (35,400 shares),
- » S1 (26,663 shares)

Series A, C and F shares were admitted to stock exchange trading on condition that they are swapped for bearer shares, and series P and S1 shares may be admitted to stock exchange trading when respective authorizations are obtained.

### **Bearer shares**

The Bank's Shareholders hold 271,583,872 bearer shares, which accounts for 99.97% of the share capital. Originally, bearer shares were shares of the following series:

- » B (2,500,000 shares),
- » D (100,000 shares),
- » E (1,580,425 shares),
- » G (480,000 shares),
- » H (3,777,350 shares),
- » I (5,600,000 shares),
- » J (4,400,000 shares),
- » K (2,278,814 shares),
- » L (2,000,000 shares),
- » M (10,000,000 shares),



- » N (847,000 shares),
- » O (25,000,000 shares),
- » R (32,583,993 shares),
- » T (49,301,056 shares),
- » U (63,387,072 shares),
- » W (60,368,640 shares),

In addition, as a result of the swap of registered shares, bearer shares are the shares of the following series:

- » P (2,497,058 shares),
- » C (98,575 shares),
- » F (306,137 shares),
- » P (3,654,282 shares),
- » S1 (823,470 shares).

As at 31 December 2005, as many as 271,583,872 bearer shares have been traded on the main market of the Warsaw Stock Exchange. Whereas, as at 31 December 2004, the number of shares traded on the stock exchange amounted to 271,579,179.

The table below presents Shareholders holding over 5% of total votes at the General Meeting of Shareholders as at 31 December 2005:

Shareholder	Line of business	Number of shares and votes at the GMS	Share in votes and share capital (%)
KBC Bank N.V.*	Banking	232 341 875	85.53

*\*/ By the Resolution of the Commission for Banking Supervision No. 81/KNB/81 of 17 September 2001, KBC Bank N.V. is entitled to exercise no more than 75% of votes at the General Meeting of Shareholders of Kredyt Bank S.A.*

### **Reserve capital**

	31.12.2005	31.12.2004
Share premium	0	298 159
Statutory	0	50 000
Other (by types)	0	2 751
- other	0	2 751
<b>Total supplementary capital</b>	<b>0</b>	<b>350 910</b>

**Revaluation reserve**

	31.12.2005	31.12.2004
Deferred income tax	-3 467	0
<b>Other (by types)</b>	<b>19 395</b>	<b>-20 247</b>
- valuation of financial fixed assets	19 395	-20 247
<b>Total revaluation reserve</b>	<b>15 928</b>	<b>-20 247</b>

**Other reserve capitals (by appropriation), including:**

	31.12.2005	31.12.2004
General banking risk fund created from profit	120 942	173 779
<b>Total other reserve capitals</b>	<b>120 942</b>	<b>173 779</b>

**Capital from translation of subordinated companies and foreign branches**

	31.12.2005	31.12.2004
Capitals from translation of subordinated companies	-637	-285
<b>Total other capitals from translation of subordinated companies</b>	<b>-637</b>	<b>-285</b>

**49. Contingent liabilities granted****Guarantees**

	31.12.2005	31.12.2004
- up to 1 month	71 767	93 503
- 1-3 months	58 410	55 339
- 3-6 months	168 949	73 940
- 6 months to 1 year	169 826	1 593 532
- 1 - 3 years	211 912	308 549
- 3 - 5 years	208 631	146 875
- over 5 years	236 662	899 038
<b>Total</b>	<b>1 126 157</b>	<b>3 170 776</b>

**For financing**

	31.12.2005	31.12.2004
- up to 1 month	170 597	550 480
- 1-3 months	181 354	172 408
- 3-6 months	230 737	121 613
- 6 months to 1 year	1 068 824	616 094
- 1 - 3 years	250 106	186 071
- 3 - 5 years	74 027	43 104
- over 5 years	476 183	396 109
<b>Total</b>	<b>2 451 828</b>	<b>2 085 879</b>

Major items in the contingent liabilities granted are guarantees of good contracts performance and loan repayment guarantees.

The Bank offers its customers guarantees as a standard product offer for corporate customers. Commissions received from guarantees granted are accounted into commission income on straight-line basis over the lifetime of the guarantee.

The Bank treats guarantees granted as an exposure with credit risk for the purpose of credit risk management. All exposures granted to customer including guarantees granted are analyzed by the credit risk department for the occurrence of the impairment indicators and required level of allowance for impairment.

As at 31.12.2005 allowance for impairment losses of the guarantees granted amounted PLN 52 915 thousand, when as at 31.12.2004 PLN 24 740 thousand. These amounts are presented in note 40 as an element of allowance for impairment losses for off-balance sheet exposures

## 50. Capital adequacy ratio

	31.12.2005	31.12.2004
<b>Capital requirement, including:</b>	<b>965 307</b>	<b>1 072 391</b>
- credit risk	949 832	1 059 285
- other risk	5 561	4 491
- market risk	9 914	8 615
<b>Shareholders' equity and short-term capital</b>	<b>1 980 801</b>	<b>1 973 183</b>
- share capital	1 358 294	1 358 294
- reserve capital	0	350 910
- revaluation reserve included in shareholders' funds	15 928	964
- other reserve capitals	120 942	173 779
- currency translation differences from the translation of subordinated companies	-637	-285
- subordinated liabilities	254 747	447 420
- shares in financial entities	-43 198	-45 142
- goodwill	-36 052	0
- intangible assets	-109 049	-136 939
- retained profit / loss	-228 810	-588 923
- issue of own securities	400 000	400 000
- short-term capital	15 475	13 105
- current net profit	233 161	0
<b>Capital adequacy ratio</b>	<b>16,42</b>	<b>14,72</b>

Capital adequacy ratio was calculated as required by the regulations of the National Bank of Poland in force as at 31.12.2005 and 31.12.2004.

## 51. Discontinued operations

On 31 March 2005, the conditional contract on the sale of an organized portion of the enterprise in the form of Inwestycyjny Dom Maklerski S.A. between Kredyt Bank S.A. and KBC Securities N.V. was performed.

Below, we present financial figures for IDM Kredyt Bank S.A. as at 31.03.2005.

### Income statement

	01.01.2005 - 31.12.2005
<b>Income:</b>	
- interest	963
- fees and commissions	2 612
- financial income	12
- other operating income	423
- reversal of impairment charges	38
<b>Total income</b>	<b>4 048</b>
	01.01.2005 - 31.12.2005
<b>Expenses:</b>	
- fees and commissions	-2
- costs of financial activities	-8
- functioning costs, including:	-1 945
<i>staff costs</i>	-1 169
<i>material costs</i>	-725
<i>taxes and fees</i>	-4
<i>depreciation and amortization</i>	-47
- creation of impairment charges	-61
- other operating expenses	-1 058
<b>Total expenses</b>	<b>-3 074</b>
<b>Profit before tax</b>	<b>974</b>
Income tax expense	0
<b>Net profit on discontinued operations</b>	<b>974</b>
<b>Earnings per share</b>	<b>0.0036</b>

**Balance sheet**

	<b>31.03.2005</b>
Intangible assets	264
Property, plant and equipment	128
Cash	33 343
Office cash in the Guarantee Fund of the Warsaw Stock Exchange	14 581
Receivables	50 681
Securities	128
<b>Held-for-sale assets</b>	<b>99 125</b>
Liabilities	-69 403
Securities accounts	-28 748
<b>Liabilities directly associated with held-for-sale assets</b>	<b>-98 151</b>
Net liabilities related to discontinued operations	974

**52. Related party transactions**

Related parties with which the Group concludes transactions, are the Group's subsidiaries, the companies of KBC Group, persons managing the Group and the Group's employees.

Related party transactions are standard banking operations, concluded on market terms: extending loans, issuing bank guarantees, issuing own securities, accepting deposits, borrowing loans, foreign currency transactions, transactions in derivatives. The volumes of transactions and related income and expense have been presented below:

In 2005 there were no material transactions between the Group's companies not consolidated with the full consolidation method, and other companies, including the parent company.

<b>Assets</b>	<b>Associates</b>	<b>Parent company (KBC Group)*</b>	<b>Total as at 31.12.2005</b>
Amounts due from banks	0	598 449	<b>598 449</b>
Loans and advances to customers	0	20 843	<b>20 843</b>
Other assets	0	70 285	<b>70 285</b>
<b>Total assets</b>	<b>0</b>	<b>689 577</b>	<b>689 577</b>

<b>Liabilities</b>	<b>Associates</b>	<b>Parent company (KBC Group)</b>	<b>Total as at 31.12.2005</b>
Amounts due to banks	0	959 297	<b>959 297</b>
Amounts due to customers	38 584	132 258	<b>170 842</b>
Investment securities	0	400 000	<b>400 000</b>
Subordinated liabilities	0	589 581	<b>589 581</b>
Other liabilities	0	58 775	<b>58 775</b>
<b>Total liabilities</b>	<b>38 584</b>	<b>2 139 911</b>	<b>2 178 495</b>

<b>Off-balance sheet items</b>	<b>Associates</b>	<b>Parent company (KBC Group)</b>	<b>Total as at 31.12.2005</b>
Guarantees granted	0	149 377	<b>149 377</b>
Guarantees received	0	90 039	<b>90 039</b>
Derivatives	0	5 609 564	<b>5 609 564</b>
<b>Total off-balance sheet items</b>	<b>0</b>	<b>5 848 980</b>	<b>5 848 980</b>

<b>Income</b>	<b>Associates</b>	<b>Parent company (KBC Group)</b>	<b>Total in 2005</b>
Interest income	0	19 781	<b>19 781</b>
Fee and commission income	0	3 800	<b>3 800</b>
Other operating income	4 050	5 079	<b>9 129</b>
<b>Total income</b>	<b>4 050</b>	<b>28 660</b>	<b>32 710</b>

<b>Expenses</b>	<b>Associates</b>	<b>Parent company (KBC Group)</b>	<b>Total in 2005</b>
Interest expense	0	69 227	<b>69 227</b>
The costs of the Bank's operating and administrative expenses	0	13 267	<b>13 267</b>
<b>Total expenses</b>	<b>0</b>	<b>82 494</b>	<b>82 494</b>

\* Including WARTA S.A.

Below, we present data on transactions with the parent company (KBC Group) as at 31 December 2004. As at 31 December 2004, the Group did not have any associate entities.

<b>Assets</b>	<b>Total as at 31.12.2004</b>
Amounts due from banks	<b>218 415</b>
Loans and advances to customers	<b>69</b>
Other assets	<b>46 663</b>
<b>Total assets</b>	<b>265 147</b>

<b>Liabilities</b>	<b>Total as at 31.12.2004</b>
Amounts due to banks	2 165 551
Amounts due to customers	6 511
Investment securities	400 000
Subordinated liabilities	598 210
Other liabilities	38 765
<b>Total liabilities</b>	<b>3 209 037</b>

<b>Off-balance sheet items</b>	<b>Total as at 31.12.2004</b>
Guarantees granted	1 877 014
Derivatives	5 621 384
Amounts due under sale/purchase transactions	77 909
<b>Total off-balance sheet items</b>	<b>7 576 307</b>

<b>Income</b>	<b>Total as at 31.12.2004</b>
Interest income	19 372
Fee and commission income	8
Other operating income	22
<b>Total income</b>	<b>19 402</b>

<b>Expenses</b>	<b>Total as at 31.12.2004</b>
Interest expense	59 444
Fee and commission expense	5 081
The costs of the Bank's operating and administrative expenses	2 495
<b>Total expenses</b>	<b>67 020</b>

### 53. Remuneration of the Members of the Supervisory Board and the Management Board of Kredyt Bank S.A.

Below are presented salaries, bonuses and other benefits of the Supervisory Board and the Management Board.

Supervisory Board of the Bank	01.01.2005- 31.12.2005	01.01.2004- 31.12.2004
	Salary	
Witkowski Andrzej	263	255
Bergen André	198	207
Florquin Francoise	198	191
Kulikowski Feliks	198	191
Michałowski Marek	198	191
Noga Adam	198	191
Toczek Józef	198	207
Voljc Marko	198	207
Docx Rita	176	0
Mampaey Dirk	22	191
Krawczyk Grzegorz	0	208
Guiral Philippe	0	178
<b>Total</b>	<b>1 847</b>	<b>2 217</b>

Management Board of the Bank	01.01.2005 – 31.12.2005			
	Salary	Bonus	Other benefits	Total
Richardson Ronald	532	297	165	994
Kroker-Jachiewicz Małgorzata	912	1 301	252	2 465
Libot Guy	912	591	181	1 684
Mierzwiński Bohdan	660	556	210	1 426
Kokot Krzysztof	760	400	179	1 339
Di Maggio Fedele	162	254	152	568
<b>Total</b>	<b>3 938</b>	<b>3 399</b>	<b>1 139</b>	<b>8 476</b>



Management Board of the Bank	01.01.2004 – 31.12.2004				
	Salary	Bonus	Other benefits	Termination benefits	Total
Kroker-Jachiewicz Małgorzata	831	463	146	0	1 440
Libot Guy	691	232	91	0	1 014
Mierzwiński Bohdan	656	232	121	0	1 009
Di Maggio Fedele	632	221	90	0	943
Sewerynik Izabela	586	232	140	2 191	3 149
<b>Total</b>	<b>3 396</b>	<b>1 380</b>	<b>588</b>	<b>2 191</b>	<b>7 555</b>

Below, we present information on remuneration for each category of benefits paid to the Management Board and to the Supervisory Board.

Benefit	01.01.2005- 31.12.2005	01.01.2004- 31.12.2004
Short-term employee benefits	10 276	7 556
Benefits paid after employment termination	47	55
Severance pays	0	2 161
<b>Total</b>	<b>10 323</b>	<b>9 772</b>

In 2005, the Members of the Management Board and the Members of the Supervisory Board did not received remuneration in subsidiaries.

In 2004, the Members of the Management and Supervisory Boards received remuneration for their functions in the authorities of subsidiaries in the total amount of PLN 44 thousand.

#### **54. Value of loans and advances granted to employees, members of the Management Board and Supervisory Board of the Bank and in its subsidiaries and associates**

Transactions concluded with the Bank's Management Staff and employees are executed within the standard product offer.

As at 31 December 2005, total indebtedness related to loans and advances, and cash loan granted by the Bank amounted to:

- for Members of the Management Board – PLN 3 thousand;
- for Members of the Supervisory Board – PLN 894 thousand;
- for the Bank's employees – PLN 81,569 thousand.

As at 31 December 2004, total indebtedness related to loans and advances, and cash loan granted by the Bank amounted to:

- for Members of the Bank's Management Board - PLN 61 thousand;
- for Members of the Supervisory Board - PLN 1,096 thousand;
- for the Bank's employees – PLN 69,508 thousand.

As at 31 December 2005, the total indebtedness of Members of the Management Board and Supervisory Board of the Bank is normal, due indebtedness is not present. PLN 800 thousand of the employees' indebtedness remains doubtful.

As at 31 December 2005, the indebtedness of the members of the Management Board and Supervisory Board of the Bank in its subsidiaries was not present.

## 55. Consolidated cash flow statement – additional information

### *Cash and cash equivalents*

	31.12.2005	31.12.2004
Cash and balances with central bank	607 090	1 512 591
Due from other banks	1 641 799	2 409 550
<b>Cash and cash equivalents</b>	<b>2 248 889</b>	<b>3 922 141</b>

With respect to the presentation of cash for cash flow statement, a change in comparable data has been made in relation to the data originating from the approved financial statement for the period ended 31 December 2004. Cash as at 1 December 2004 was adjusted with the amount of 3-month term deposits.

In the position cash and cash equivalents the Bank presents obligatory reserve held in line with the adequate regulation on the Central Bank account and marked as restricted cash.

### *Amounts due from banks*

	31.12.2005	31.12.2004
Change	469 937	-1 346 703
Nostro accounts - cash at period end	9 779	-16 671
Term deposits up to 3 months - cash at period end	-777 530	1 204 436
<b>Total</b>	<b>-297 814</b>	<b>-158 938</b>

**Loans and advances to customers**

	31.12.2005	31.12.2004
Change	1 663 444	2 580 879
Adjustments related to adoption of IFRS	-178 679	1 377
Adjustments related to adoption of IFRS – loans impairment	-147 995	-5 399
Consolidation adjustments	79 062	0
<b>Total</b>	<b>1 415 832</b>	<b>2 576 857</b>

**Amounts due to banks**

	31.12.2005	31.12.2004
Change	-444 923	-1 277 007
Adjustments related to adoption of IFRS	-1 041	0
Proceeds from a borrowed working capital loan – presentation in financial activities	-996 140	0
Repayment of a working capital loan - presentation in financial activities	469 609	308 984
Repayment of an investment credit - presentation in financial activities	432 013	0
Other change in a working capital loan and an investment credit	36 248	96 443
Consolidation adjustments	0	0
<b>Total</b>	<b>-504 234</b>	<b>-871 580</b>

**Amounts due to customers**

<b>Amounts due to customers</b>	<b>01.01.2005- 31.12.2005</b>	<b>01.01.2004- 31.12.2004</b>
Change	472 519	-608 105
Adjustments related to IFRS adoption	2 152	0
Consolidation adjustments	12 881	0
<b>Total</b>	<b>487 552</b>	<b>-608 105</b>

**Held-to-maturity assets**

	01.01.2005- 31.12.2005	01.01.2004- 31.12.2004
Adjustments related to first adoption of IFRS	190 110	0
Adjustments related to adoption of IFRS	-4 223	0
- acquisition in investment activities	-1 222 392	-108 256
- sale in investment activities	333 089	399 629
- changes in interest receivables in operating activities	-131 730	-24 239
- change in held-to-maturity financial assets in operating activities	5 994	-24 081
- currency translation differences in operating activities	-9	26 010
<b>Total</b>	<b>-829 161</b>	<b>269 063</b>

**Available-for-sale financial assets**

	01.01.2005- 31.12.2005	01.01.2004- 31.12.2004
Adjustments related to first adoption of IFRS - in operating activities	669 413	0
Acquisition in investment activities	-45 742 823	-9 953 932
Sale in investment activities	43 267 580	9 971 635
Changes in interest receivables in operating activities	-101 905	-56 651
Change in available-for-sale financial assets in operating activities	-68 437	-42 964
Currency translation differences in operating activities	8 488	0
Consolidation adjustments	5	21
<b>Total</b>	<b>-1 967 679</b>	<b>-81 891</b>

With regard to held-to-maturity assets and available-for-sale assets, the above tables reconcile cash flows presented in various parts of the cash flow statement with the balance sheet change.

**Operating activity – other adjustments**

	01.01.2005- 31.12.2005	01.01.2004- 31.12.2004
Change in tangible and intangible assets	-18 103	43 407
Change in other assets	-46 404	21 071
Change in equity	17 562	13 160
Other items	0	-92 075
Consolidation adjustments	-87 621	70 326
<b>Total</b>	<b>-134 566</b>	<b>55 889</b>

**Investment activity – other investment flows**

	01.01.2005- 31.12.2005	01.01.2004- 31.12.2004
Change of shares into cash (equity pay out for PTE)	36 840	0
<b>Total</b>	<b>36 840</b>	<b>0</b>

**Financing activity – other financing expenses**

	01.01.2005- 31.12.2005	01.01.2004- 31.12.2004
Interest repayment on loans received	15 336	27 594
Interest repayment on subordinated liabilities	22 673	23 876
Interest repayment on issued debt securities	49 244	14 007
<b>Total</b>	<b>87 253</b>	<b>65 477</b>

**Change in the sold securities under repurchase agreements**

	01.01.2005- 31.12.2005	01.01.2004- 31.12.2004
Change in the balances	-350 071	718 772
Change in the accrued interest balances – presented as interest in operating activity	1 063	-2 108
<b>Total</b>	<b>-349 008</b>	<b>716 664</b>

**Change in the balance of shares in subsidiaries, other securities and other financial assets**

	01.01.2005- 31.12.2005	01.01.2004- 31.12.2004
Change in shares in subsidiaries	12 530	-47 831
Change in shares in associates	0	-137
Change in shares in assets for sale	-4 368	-11 208
Change in financial assets	3 179	190 649
<b>Total</b>	<b>11 341</b>	<b>131 473</b>

**Change in debt securities**

	01.01.2005- 31.12.2005	01.01.2004- 31.12.2004
Change in trading portfolio	682 617	213 915
Change in available for sale portfolio	-52 307	-27 753
Change in held to maturity portfolio	-1 628	0
<b>Total</b>	<b>628 682</b>	<b>186 162</b>

## 56. Disposal of subordinated companies and equity investments

On 26 August 2004, the parent company executed the final contract of sale of the whole stake in Kredyt Bank Ukraina S.A., i.e. 65% of shares and votes at the company's General Meeting of Shareholders, to PKO Bank Polski S.A. Below, we present the essential information on the disposed company as at 31 July 2004:

Cash and cash equivalents*	38 216
Balance sheet total*	901 629
<i>*figures as at 31.12.2004</i>	
Income	88 308
Expenses	80 062
Profit/loss on business activities	8 246
Income tax expense	2 542
Net profit/loss	5 704
in PLN million	
Share price	108,8
Shares book value including currency translation differences	72,2
<b>Net profit/loss on shares disposal of Kredyt Bank S.A.</b>	<b>36,6</b>

In 2005, the Bank disposed of its whole stake in Wolny Obszar Gospodarczy S.A. and in Solaris Bus and Coach Sp. z o.o. (information on these disposals was included in the Management Board's report on the operations of Kredyt Bank S.A. Capital Group in 2005, point 2.4).

## 57. Asset pledged as collateral

As at 31 December 2005, the following assets in a form of Treasury bonds were collateral for the parent company's own liabilities:

- Treasury bonds of the nominal value of PLN 100,500 thousand and of the carrying amount of PLN 110,981 thousand were collateral for a loan borrowed by the Bank of PLN 95,454 thousand and the security for interest payments on the loan. The loan was drawn by parent company from the Banking Guarantee Fund for the restructuring of assets and liabilities acquired from Polski Kredyt Bank S.A. pursuant to the recovery plan.
- Treasury bonds of the nominal value of PLN 27,640 thousand and of the carrying amount of PLN 30,523 thousand were collateral for the protection fund for guaranteed cash in the Banking Guarantee Fund and were deposited in the National Depository for Securities.

- Treasury bonds of the nominal value of PLN 550,000 thousand and of the carrying amount of PLN 512,175 thousand as collateral for possible borrowing of a lombard loan in the National Bank of Poland (NBP).
- Treasury bonds of the nominal value of PLN 353,268 thousand and of the carrying amount of PLN 367,747 thousand pledged in relation to REPO transactions with customers.

As at 31 December 2004, the following assets in a form of Treasury bills and bonds were collateral for the parent company's own liabilities:

- Treasury bills of the nominal value of PLN 110,000 thousand were collateral for loans drawn by the parent company of PLN 105,000 thousand and secured the payment of interest on these loans. The parent company drawn the loans from the Banking Guarantee Fund for the restructuring of assets and liabilities acquired from Polski Kredyt Bank S.A. pursuant to the recovery plan and with the rehabilitation of Wschodni Bank Cukrownictwa.
- Treasury bills of the nominal value of PLN 46,000 thousand were collateral for the protection fund for guaranteed cash in the Banking Guarantee Fund and were deposited in the National Depository for Securities.
- Treasury bills of the nominal value of PLN 261,150 thousand were pledged in relation to REPO transactions with customers.
- Treasury bonds of the nominal value of PLN 455,054 thousand were pledged in relation to REPO transactions with customers.

## **58. Changes in the Management and Supervisory Boards of Kredyt Bank S.A in 2005**

On 9 February 2005, the Supervisory Board of Kredyt Bank S.A. appointed, as of 1 March 2005, Mr. Ronald Richardson for the position of the Vice President of the Bank's Management Board. On 8 June 2005, the Commission for Banking Supervision expressed its consent to the appointment of Mr. Ronald Richardson for the position of the President of the Management Board of Kredyt Bank S.A. Under the resolution of the Supervisory Board of 31 March 2005, since the date of the approval, Mr. Ronald Richardson has been performing the function of the President of the Bank's Management Board.

Ms. Małgorzata Kroker-Jachiewicz, the previous President of the Bank's Management Board, remained in the Board as its Vice President.

In addition, on 9 February 2005, the Supervisory Board of Kredyt Bank S.A. appointed, as of 1 March 2005, Mr. Krzysztof Kokot for the position of the Vice President of the Bank's Management Board.

The Supervisory Board also accepted the resignation of Mr. Fedele Di Maggio from the position of the Vice President of the Bank's Management Board. Mr. Fedele Di Maggio was entrusted with other responsibilities in KBC Group.

As at 31 December 2005, the 5-member Management Board of Kredyt Bank S.A. was composed of:

Mr. Ronald Richardson	– President of the Management Board, CEO of the Bank,
Mr. Krzysztof Kokot	– Vice President of the Management Board, Vice CEO of the Bank,
Ms. Małgorzata Kroker-Jachiewicz	– Vice President of the Management Board, Vice CEO of the Bank,
Mr. Guy Libot	– Vice President of the Management Board, Vice CEO of the Bank,
Mr. Bohdan Mierzwiński	– Vice President of the Management Board, Vice CEO of the Bank.

On 9 February 2005, Ms. Rita Docx was appointed a member of the Supervisory Board following the resignation by Mr. Dirk Mampaey from his position in the Supervisory Board of Kredyt Bank S.A.

As at 31 December 2005, the Supervisory Board of Kredyt Bank S.A. was composed of:

Mr. Andrzej Witkowski	– Chairman of the Supervisory Board,
Mr. André Bergen	– Member of the Supervisory Board,
Mr. Marko Voljć	– Member of the Supervisory Board,
Mr. Françoise Florquin	– Member of the Supervisory Board,
Mr. Feliks Kulikowski	– Member of the Supervisory Board,
Ms. Rita Docx	– Member of the Supervisory Board,
Mr. Marek Michałowski	– Member of the Supervisory Board,
Mr. Adam Noga	– Member of the Supervisory Board,
Mr. Józef Toczek	– Member of the Supervisory Board.

## 59. Restructuring program

As a result of the financial loss at the end of 2002, under Article 142 of the Banking Law, the Bank prepared the Recovery Plan for the years 2003-2005 with a view to eliminating a negative impact of the acquisition of Polski Kredyt Bank S.A., a banking enterprise, in the years 2002-2007. This programme was approved by the Commission for Banking Supervision. In December 2003, the plan was updated and communicated to the Commission for Banking Supervision. On 28 June 2004, the Commission for Banking Supervision approved the updated version of the new recovery plan for Kredyt Bank S.A.

The Commission considered the following activities of the parent company: an increase in the Bank's shareholders' equity, covering retained loss, improvement of financial results in 2004 and the restructuring of Kredyt Bank Capital Group. The strategic targets stipulated in the recovery plan provide for the improvement of the Bank's profitability and the maintenance of its strong position as a universal bank, definitely improving its position on the retail banking market while retaining the high level of safety ratios.



The targets assumed in the recovery plan are to be achieved through the utilization and development of existing organization potential based on the identification and neutralization of credit risk, the restructuring of the Capital Group, costs optimization and the development of customer database.

In the event of the improper implementation of the recovery plan, the Bank is subject to sanctions under articles 142-145 of the Banking Law.

The main objectives of the Recovery Plan expressed in the planned net financial result, key performance ratios and capital adequacy were substantially exceeded in the first half of 2005.

In 2004 and 2005, the Bank focused on achieving positive effects related to the restructuring and debt recovery processes, mitigating credit risk and reduction of the functioning costs. Major accomplishments, from the point of view of the income statement, were recorded mainly in the first of the above-mentioned areas.

As the strategic shareholder, KBC Bank fully supports the Bank's actions, issuing deposit guarantees and sureties, which constitute additional collateral for loan receivables.

To date, the Bank focused mainly on credit risk, debt recovery, restructuring and the reduction and control of functioning costs. Related undertakings in these areas resulted in specific and noticeable effects in the income statement. At present, the Bank's and the Group's activities, to a larger extent than ever before, will focus on sale, including the development of the banc assurance area.

## **60. Seasonality or cyclical nature of operations**

Operations of the Group's companies are not of seasonal nature.

## **61. Non-typical factors and events**

Either in 2005 or 2004, no untypical events occurred in the Group's companies that would affect the structure of balance sheet items and the financial result.

## **62. Issue, redemption and repayments of debt or equity instruments**

In 2005, the Group's companies did not issue, redeem or repay any debt securities.

In 2004, the Bank issued 60,368,640 series 'W' ordinary bearer shares with the nominal value of PLN 5.00 each with the subscription rights for existing shareholders. All 60,368,640 shares were subscribed for and such a number was issued to investors. Total cash generated from the issue of series 'W' shares amounts to PLN 603,686 thousand.

Additionally, in 2004 the Bank issued registered securities for the amount of PLN 70 million. The issue was the second tranche under the program of the issue of perpetual banking securities targeted at companies of KBC Bank NV Group. The interest rate of banking securities was WIBOR 6M increased with the market rate. KBC Bank NV Dublin Branch subscribed for the whole issue.

### **63. Dividends paid**

Either in 2005 or 2004, the Group did not have any liabilities related to the distribution of approved dividend.

### **64. Post-balance sheet events**

Subordinated loan agreement of 28 April 2000 concluded with KBC Bank, Dublin Branch and Banco Espirito Santo for USD 50 million was repaid on 17 January 2006 in the amount of USD 50 million.

No other post balance sheet events occurred in the Bank that might have affected figures presented in this financial statement.

### **65. First time adoption of IAS/IFRS**

IFRS 1 - First time adoption of International Financial Reporting Standards, determines the manner of IAS/IFRS application in the financial statements prepared in accordance with IAS/IFRS for the first time.

Preparation of financial statements for the first time in line with IFRS requires a judgment of an entity's Management Board on the adopted accounting principles and estimates applied.

1 January 2004 is the date of adopting IFRS by the Group and by the Bank, i.e. the opening balance prepared according to IFRS.

The accounting principles adopted for financial statements have been applied on a continuous basis in all presented periods, starting from the opening balance (1 January 2004), except for the exemptions from specific IAS/IFRS permitted under IFRS 1.

IFRS 1 determines two categories of exemptions from the principles of preparing the opening balance under IFRS, according to each IAS/IFRS:

- exemption from applying certain aspects of specific IAS/IFRS [IFRS 1 - Section 12a];
- prohibition to retrospectively apply certain aspects of specific IAS/IFRS [IFRS 1 - Section 12b]

The Bank has selected the following options as regards exemptions from the application of certain aspects of specific IAS/IFRS as permitted by IFRS 1 and:

- does not apply retrospectively the stipulations of IFRS 3 Business Combinations in relation to business combinations in the past (before IFRS effective date) [IFRS 1, Section 13a];

- measures, as of the first day of IFRS application, property, plant and equipment as well as intangible assets at fair value and adopts that figure as deemed cost determined on that day [IFRS 1, Section 13b];
- re-determines, as of the day of adopting IFRS, financial assets at fair value, including its changes recognized in the income statement or as available for sale [IFRS 1, Section 13g];
- presents comparable data not compliant with IAS 32 Financial Instruments: Disclosure and Presentation and IAS 39 Financial Instruments: Recognition and Measurement [IFRS 1, Section 36A].

The adoption of the above options is consistent with the accounting policy with respect to the first application of IFRS as adopted by the Bank's Major Shareholder.

## **66. Clarifications related to the adoption of IFRS and the related adjustments in the opening balance**

As the accounting principles applied by the Group for preparation of opening balance in accordance with IFRS, differ from the principles applied on the same date at the time of their historical preparation (pursuant to the Accounting Act), according to IFRS 1, the related adjustments were recognised in the retained earnings.

The Group, acting under IAS 12, has not recognised the effect of deferred tax asset on the adjustments related to the first adoption of IFRS. As mentioned in the Group's consolidated financial statement as of 31 December 2004, the accounting principle applied in 2003 and 2004 provided that, at the Bank, bearing in mind balance sheet and tax losses incurred in 2002 and 2003 and the uncertainty of the settlement of the excess of deferred tax asset over deferred tax liability, deferred tax assets were recognized only up to the amount of the deferred tax liability.

**IAS/IFRS adjustments to the Group's consolidated shareholders' equity and other items of the financial statement in the periods covered by this report**

**Table 1** - Reconciliation of the opening balance of the consolidated shareholders' equity as of 1 January 2004 in accordance with IAS

<b>Consolidated shareholders' equity as at 31.12.2003 according to PAS</b>	<b>644 481</b>
1 Adjustments related to the adoption of IAS disclosed in revaluation reserve:	
a) measurement of fixed assets at fair value	-1 250
b) revaluation of currency translation differences from the translation of subordinated companies and foreign branches	-10 753
2 Adjustments related to the adoption of IAS disclosed in retained earnings (loss):	
a) withdrawal of the measurement of subordinated companies with the equity method	13 857
b) recognition of the impairment of investments in shares of subordinated entities measured with the equity method and under IAS 39 are disclosed at cost less impairment	-16 254
c) measurement of fixed assets at fair value	1 250
d) reversal of the provision for general risk	87 867
3 Currency translation differences from the translation of subordinated companies and foreign branches	10 757
4 Minority interest	29 249
<b>Total IAS adjustments</b>	<b>114 723</b>
<b>Consolidated shareholders' equity as at 01.01.2004 according to IAS</b>	<b>759 204</b>

**Table 2** - Adjustment of the closing balance of consolidated shareholder's equity as of 31 December 2004 in accordance with IAS

<b>Consolidated shareholders' equity as at 31.12.2004 according to PAS</b>		<b>1 459 954</b>	
			<i>Including net profit for the period</i>
			<b>185 176</b>
1	Adjustments related to the adoption of IAS affecting the revaluation reserve:		
a)	measurement of fixed assets at fair value	-1 250	
		-1 250	
2	Adjustments related to the adoption of IAS affecting retained earnings (loss):		
a)	withdrawal of the measurement of non-consolidated subordinated companies with the equity method and the effect of the deconsolidation of immaterial companies recognition of the impairment of investments in the shares of subordinated entities	13 857	
b)	measured with the equity method and which under IAS are disclosed at cost less impairment	-16 254	
c)	measurement of fixed assets at fair value	1 250	
d)	reversal of the provision for general risk	87 867	
		86 720	
3	Adjustments related to the adoption of IAS affecting net profit in the current period:		
a)	withdrawal of the measurement of subordinated companies with the equity method reversal of impairment charge for equity investments in shares of subordinated	-11 012	-11 012
b)	companies measured with the equity method and which under IAS are disclosed at cost less impairment	2 062	2 062
c)	withdrawal of goodwill amortization charged to income statement in 2004 according to PAS	13 247	13 247
d)	reversal of the provision for general risk	-32 633	-32 633
		-28 336	-28 336
<b>Total IAS adjustments</b>		<b>57 134</b>	<b>-28 336</b>
<b>Consolidated shareholders' equity as at 31.12.2004 according to IAS</b>		<b>1 517 088</b>	
			<i>Including net profit for the current period</i>
			<b>156 840</b>

Explanation of the adjustments to consolidated equity as of 31 December 2004

The Bank, as at 1 January 2004 and in accordance with IFRS 1 and IFRS 3, ceased to amortize goodwill. Since this date goodwill impairment test has been carried out every six months.

**Table 3** – Significant reclassifications of consolidated balance sheet items against data published as at 31 December 2004 according to the Polish Accounting Standards

ASSETS		31.12.2004 Polish Accounting Standards	Adjustments	31.12.2004 IFRS
I	Financial assets (*) (**)	A 8 632 398	50 676	8 683 074
II	Loans and advances to customers	B 14 772 682	-666 730	14 105 952
III	Allowance for impairment charges	C -2 698 345	-45 277	-2 743 622
IV	Equity investments	D 74 054	-38 787	35 267
V	Intangible assets and tangible fixed assets	E 611 627	-2 069	609 558
VI	Deferred tax assets	F 18 423	-7 988	10 435
VII	Goodwill	G 29 262	6 790	36 052
VIII	Other assets	B 230 630	-21 262	209 368
<b>TOTAL ASSETS</b>		<b>21 670 731</b>	<b>-724 647</b>	<b>20 946 084</b>

LIABILITIES		31.12.2004 Polish Accounting Standards	Adjustments	31.12.2004 IFRS
I	Financial liabilities (**)	I 19 021 870	16 465	19 038 335
II	Reserve	H 134 756	-97 317	37 439
III	Deferred tax liabilities	J 10 048	-7 988	2 060
IV	Special funds and other liabilities (***)	K 1 044 103	-692 941	351 162
<b>TOTAL LIABILITIES</b>		<b>20 210 777</b>	<b>-781 781</b>	<b>19 428 996</b>
V	Equity	L 1 459 954	57 134	1 517 088
<b>TOTAL LIABILITIES AND EQUITY</b>		<b>21 670 731</b>	<b>-724 647</b>	<b>20 946 084</b>

(\*) – the item contains: cash and balances with central bank, amounts due from other banks, held-for-trading investments, available-for-sale financial assets, held-to-maturity financial assets.

(\*\*) – the item contains: amounts due to banks and customers, liabilities related to securities disposed of under repurchase agreements, debt securities in issue, financial assets liabilities, subordinated liabilities.

(\*\*\*) – in these items the Group has offset assets and liabilities arising on CSBF as it does not constitute Group's assets. Total assets as at 31.12.2004 presented in the financial statement is lower by PLN 2 866 thousand than total assets presented for the first half of the year 2005 at the same date. The difference arose on the offsetting the assets and liabilities on CSFB.

Explanation of reclassification adjustments to comparable data for 12 months of 2004:

Adjustment in assets	Amount in '000' PLN	Item	Adjustment in liabilities	Amount
A	-2 866	Offset of assets and liabilities arising on CSBF	K	-2 866
A	50 348	reclassification of debt securities to available-for-sale assets		
D	-50 348	portfolio		
B	-687 992	offsetting interest accrued on doubtful receivables from financial and non-financial customer with qualified interest	K	-687 992
C	-97 272	reversal of the provision for general risk	H	-97 317
		withdrawal of the measurement of subordinated entities with	L	55 189
D	-11 362	the equity method and re-measurement at cost less impairment loss	L	-11 362
E	-2 069	Offsetting assets and liabilities related to investments in fixed assets	K	-2 069
D	16 465	change of consolidation scope	I	16 465
G	13 248	reversal of goodwill amortization charged to income statement in 2004 according to PAS	L	13 248
F	-7 988	presentation of assets and deferred tax liability (separately at the assets side and liabilities side)	J	-7 988
G	-6 458	reversal of goodwill reclassification for a subsidiary		
D	6 458			
			K	-14
		change of consolidation scope	L	14
<b>Razem</b>	<b>-724 647</b>			<b>-724 647</b>
		<i>including equity adjustment</i>	L	<b>57 134</b>

**Table 4** - Adjustment of the opening balance of consolidated shareholders' equity as of 01.01.2005 in accordance with IAS

<b>Shareholders' equity as at 01.01.2005 according to PAS</b>	<b>1 459 954</b>
1 Adjustments related to the adoption of IAS disclosed in revaluation reserve:	
a) measurement at fair value of debt securities reclassified from held-to-maturity assets to available-for-sale assets	2 726
b) reclassification of the measurement of debt securities at fair value reclassified from available-for-sale assets to assets carried at fair value through profit or loss	25 539
c) measurement of fixed assets at fair value	-1 209
	27 056
2 Adjustments related to the adoption of IAS disclosed in retained earnings/loss:	
a) withdrawal of the measurement of non-consolidated subordinated companies with the equity method and the effect of the deconsolidation of immaterial companies	2 835
b) recognition of the impairment of investments in the shares of subordinated entities measured with the equity method and recognized at cost	-14 191
c) measurement at fair value of the companies: Solaris and Wolny Obszar Gospodarczy reclassified from 'equity investments' to 'available-for-sale assets'	13 281
d) withdrawal of goodwill amortization charged to income statement in 2004 according to PAS	13 247
e) reclassification of the measurement of debt securities at fair value reclassified from available-for-sale assets to assets carried at fair value through profit or loss	-25 539
f) Reversal of the provision for general risk	84 168
g) Reversal of the 1.5% provision for normal consumer loans and under observation loans	20 981
h) impairment of loan receivables - individual exposures	-93 624
i) impairment of loan receivables - portfolios	-135 672
j) measurement of financial assets and liabilities at amortized cost with the use of the effective interest rate	-95 505
k) measurement of fixed assets at fair value	1 209
	-228 810
<b>Total IAS adjustments</b>	<b>-201 754</b>
<b>Shareholders' equity as at 01.01.2005 according to IAS</b>	<b>1 258 200</b>



Explanation of the adjustments to consolidated shareholders' equity as of 1 January 2005

Due to the fact that the Group applied IAS 39 for the first time on 1 January 2005, the related adjustments were included in the opening balance of equity on that day. Below adjustments resulting from IAS 39 application have been described:

1a) adjustment recognized as for 31.12.2004

1b) the Group re-determined, as of the day of adopting IFRS, the financial assets at fair value, including its changes recognized in the income statement; according to the Polish Accounting Standards, these assets were disclosed as available for sale, and their carrying amount as of 1 January 2005 amounted to PLN 862,249 thousand

2a) and 2b) the adjustments were recognized by analogy to the comparable periods in 2004;

2c) as of 1 January 2005, the Group did not exercise actual control and did not exert any significant influence upon the financial activities and operation of Solaris Bus and Coach Sp. z o.o. and Wolny Obszar Gospodarczy S.A., despite the fact that the Group held over 50% of shares in both companies. As of 1 January 2005, investments in shares of these companies were classified as available-for-sale assets and are measured at estimated fair value. In the comparable data presented in this report, shares of these companies were disclosed in 'equity investments' and measured at cost according to IAS 27;

2d) adjustment of goodwill amortization: the Bank, as at 1 January 2004 in accordance with IFRS 1 and IFRS 3, ceased to amortize goodwill. Later on, goodwill impairment test has been carried out every six months;

2e) this adjustment corresponds to adjustment 1 b)

2f) reversal of provision for general risk established at the Bank in accordance with the Polish Banking law;

2g) the reversal of provision at the Bank for the risk connected with consumer credits classified as 'normal' as well as credits classified as 'under observation' in accordance with Polish regulations on establishing provisions for credit risk;

2h) impairment measured for individual credit exposures;

2i) collective impairment measured for portfolios of homogeneous loan receivables;

2j) the measurement of financial assets and liabilities at amortized cost applying the effective interest rate.

With respect to the presentation of cash for the cash flow statement, a change in comparable date was made in relation to the data originating from the approved financial statement for periods ended 31 December 2004. Cash as at 1 January 2004 and 31 December 2004 was adjusted with the amount of 3-month term deposits by PLN 1,315,828 thousand and PLN 2,899,863 thousand respectively, as described in Section 6.17 of the financial statement of the Group.

## 67. Fair value of financial assets and liabilities not recognized at fair value in the balance sheet

Fair value is an amount for which a given asset may be sold or exchanged for another asset, or liability may be paid in a transaction concluded on commercial terms between knowledgeable parties entering freely into the transaction. Fair value is best reflected by the market price, if available. As stated in the section on the accounting principles adopted by the Group, if the market price is unavailable, the measurement is performed on the basis of generally adopted measurement models based on variables that can be observed in the market environment.

It should be noted here that measurement models are sensitive to assumptions made.

The main categories of financial assets and liabilities not measured in the Group's balance sheet at fair value are assets or liabilities measured at amortized cost or historical cost:

- loans and advances granted as well as the other own receivables not held for trading;
- held-to-maturity investments;
- available-for-sale financial assets recognized at cost, including equity investments;
- financial liabilities not held for trading.

The table below shows differences between the carrying amount and estimated fair value of the Group's financial assets and liabilities not recognized in the Group's balance sheet at fair value. As described in Chapter 65 of this financial statement, according to IFRS 1, the Bank took advantage of the exemption from the presentation of comparable data.

31.12.2005	Carrying amount	Fair value
<b>Assets</b>		
Cash and balances with Central Bank	607 090	607 090
Due from banks	2 226 721	2 226 721
Loans and advances to customers	9 702 080	9 885 862
Investment securities	2 671 342	2 756 548

31.12.2005	Carrying amount	Fair value
<b>Liabilities</b>		
Amounts due to banks	2 562 167	2 562 167
Amounts due to customers	14 533 624	14 537 289
Other financial liabilities recognized in the balance sheet at amortized cost*	1 360 717	1 360 717

\* the item contains: debt securities in issue, subordinated liabilities and liabilities from securities disposed under repurchase agreements

**67.1. Amounts due from banks and loans and advances to customers**

As stated in the section on the accounting principles adopted by the Group and the material accounting estimates, granted loans and credits and other own receivables not held for trading are measured at amortized cost with the effective interest rate method, having regard for impairment measured on the basis of future expected cash flows (including those generated upon the sale of loan collateral) discounted with the original effective interest rate.

Poland does not have an active market on which loans and receivables may be traded, therefore, it is not possible to reliably determine the market price of these assets. Estimates performed on the basis of the models of measurement based on discounted expected cash flows of the principal and interest is the best reflection of the fair value. Expected cash flows assume the same credit risk, which is taken into consideration in the case of the measurement at amortized cost. The discount rate is the market rate as at 31 December 2005 plus margin for the risk offered on the market for defined loan facilities and specific customer groups.

As provided for in Note 24, short-term deposits are the major part of term deposits on the inter-bank market. In addition, as presented in Note 27, floating interest rate facilities are the bulk of loans and receivables. Due to these features, fair value of such products when no individual impairment has been identified is similar to their book value.

**67.2. Fixed interest rate loans and advances to customers**

As regards fixed interest rate facilities, the major parts are installment and cash loans granted by the Group and through Żagiel sales network. As at the balance sheet date, average maturity of those loans does not exceed two years. Fair value of those assets have been estimated for homogeneous product portfolios where interest cash flows with the average maturity have been estimated based on weighted average of effective interest rate of contracts active as at 31.12.2005. The discount rate used was a weighted average effective interest rate offered for new clients.

**67.3. Floating interest rate loans and advances to customers**

The Bank has split the loan portfolio for types of products and group of customers for the purpose of the fair value estimation for this group of assets. Expected cash flows have been estimated till the maturity of groups of products based on average credit margins estimated as at 31.12.2005 and expected interest rates for different currencies at balance sheet date. The discount rate used were expected market rates curves adjusted with margins offered for new clients

**67.4. Loans and advances with identified impairment loss**

In the portfolio of loans with identified impairment loss, which are under the restructuring or debt recovery process, there are many cases where the initial effective interest rate is much higher than the current market rates. The estimation of their fair value is particularly sensitive to assumptions made.

As the Group does not grant new facilities to borrowers with similar credit risk profiles the Bank has decided that as the fair value of those receivables can be accepted the net present value of the estimated expected cash flows (from the planned cash and collateral recoveries) determined in the

process of estimation of the loan impairment allowance discounted with the expected market rate curves for particular currencies as at 31.12.2005.

#### **67.5. Held-to-maturity investments and available-for-sale financial assets**

As stated in the section on the accounting principles adopted by the Group, held-to-maturity investments are measured at amortized cost with the effective interest rate methodology. Held-for-sale debt securities not measured at fair value in the balance sheet are also measured in this way. The market prices of securities applied in the measurement of fair value, for both categories of assets, do not take into consideration any potential adjustments resulting from the limited liquidity of the market or transaction costs.

The Group does not have any material commitment in shares of the companies recognized at historical cost; these are shares in subsidiaries and equity investments of minority nature. The subsidiaries operate as a supporting activity for the Bank's activity therefore it is difficult to reliably estimate its fair value. Minority interests are in majority shares taken up for a debt therefore there is no active market for those assets and the fair value estimation may significantly differ from the market offers.

#### **67.6. Other financial assets not recognized in the balance sheet at fair value**

In the case of certain groups of financial assets held at the value of the payment due, it was assumed that fair value was equal to the book value. It is mainly related to cash, current receivables and customer liabilities.

#### **67.7. Financial liabilities not held for trading**

As stated in Note 40 and Note 41, deposits on current accounts and term deposits with balance sheet maturities of less than three months constitute the bulk of deposits. Debt securities issued are based on the floating market rate, which is revaluated every six months. Estimates performed on the basis of the models of measurement based on discounted expected cash flows discounted with the expected interest rate curves as at 31.12.2005 are the best reflection of the fair value.

On the basis of the above-mentioned characteristics of financial liabilities and the assumptions adopted for the measurement models, estimated fair value of financial liabilities not held for trading is not considerably different from their carrying amount as at the date of this financial statement.

### **68. Information on proceedings before courts or public administration authority**

In 2005, the Bank was not a party to any proceedings before court or public administration authority, where the amount(s) claimed would amount to at least 10% of the Bank's shareholders' equity.

Below are presented those proceedings, in which the amounts claimed are the highest

### 68.1. The cases in which the Bank is a plaintiff

With reference to the Bank's failure in the litigation against Inspektorat Towarzystwa Salezjańskiego (Salesian Society Inspectorate) in Wrocław, the guarantor of loans granted by the Bank from February to August 2001 to four entities: St. Jan Bosko's Roman-Catholic Parish, St. Jack's Roman-Catholic Parish and two monastic houses of the Salesian Society in Lublin, the Bank is now pursuing claims by the reason of groundless enrichment against church institutions for the total amount of PLN 14,567,292.83 with possible extension of the suit.

First hearings have already taken place. The defendants replied to lawsuits and applied for the dismissal of all claims.

### 68.2. The cases in which the Bank is a defendant

The highest claim cases are as follows:

- Court proceedings regarding a credit granted to Laboratorium Frakcjonowania Osocza Sp. z o.o. in Mielec. Kredyt Bank S.A. is the leader of the syndicate of five banks, which, under the agreement of 04.03.1997, granted a syndicate loan to Laboratorium Frakcjonowania Osocza Sp. z o.o. in Mielec. The loan was secured by, among others, a registered pledge on the company's fixed assets and the surety of the State Treasury up to 60% of the drawn amount of the loan and accrued interest. As the investment project for which the loan was extended had not been completed and the dates of the payment of commitments had not been met, Kredyt Bank S.A. (Bank), representing the syndicate, terminated the agreement under its terms and conditions and called LFO Sp. z o.o. to pay claims. As at 30 June 2003, the share of Kredyt Bank in the syndicate amounted to PLN 12.4 million. The proceedings related to the Bank's exercise of the collateral under the loan agreement were unsuccessful; as a result, on 28 March 2003, the Bank, on behalf of syndicate members, called the Minister of Finance representing the State Treasury to pay USD 12.7 million, i.e. 60% of the drawn loan amount and USD 1.6 million of interest. By the letter of 1 July 2003, the Minister of Finance informed that LFO Sp. z o.o. sued the Bank for damages for the termination of the loan agreement and refused to exercise the surety by the time of issuing the court's decision on the justness of LFO Sp. z o.o. claims.
  - Claims for damages amounting to PLN 119,477 thousand due to the termination of a loan agreement. The suit was filed on 18 June 2003. The Bank is of the opinion that LFO claims are not based on any actual and legal grounds. On 16 March 2005, the court rejected the suit by LFO. On 4 May 2005, LFO filed a complaint about the decision. On 12 August 2005, the court dismissed LFO complaint against the dismissal of lawsuit. On 21 December 2005, the plaintiff submitted its appeal to the Supreme Court. The Bank filed its reply to the suit and requested for the dismissal of the suit.
  - Laboratorium Frakcjonowania Osocza Sp. z o.o. claims to deprive the executory title of the enforceability clause. The suit was filed on 6 January 2006. The value of the object of the dispute amounts to PLN 102,154 thousand (for all syndicate members, the Bank's portion amounts to PLN 6,787 thousand). The court appointed an expert to resolve on the correctness of amounts included in the bank's executory title issued by the Bank for all syndicate members. The expert confirmed incorrect amount of debt. The Bank files

clarifications and objections to expert's opinion. The court closed the case on 18 January 2006. The judgment was pronounced on 31 January 2006. The banking executory title was partially deprived of enforceability, i.e. in the amount of PLN 252,377.13. At the same time, the court upheld the enforceability of the executory title in the amount of PLN 101,901,864.67

- The banks, members of the syndicate, approached the court in order to concede the enforceability clause to the executory title issued on 1 December 2004 against the State Treasury being the guarantor of the loan granted to LFO. The first instance court, by its ruling of 23 March 2005, dismissed the banks' motion. On 22 April 2005, the banks filed a complaint about the decision. Formal defects were removed from the request on granting enforceability clause. We are waiting for the court decision.
  - The Minister of Finance, on behalf of the State Treasury, requested for determination whether the syndicated loan agreement concluded between Laboratorium Frakcjonowania Osocza Sp. z o.o. in Mielec and a syndicate of five banks expired on 28 February 1998 as a result of the failure to satisfy a contractual condition, i.e. failure to provide certain documents and the resulting expiry of the commitment of the State Treasury as the guarantor of the loan under the guarantor's agreement concluded on 1 July 1997 by Kredyt Bank, acting on behalf of the five banks, and the State Treasury. On 2 January 2006, the Bank filed its reply to the suit and requested for the dismissal of the suit.
- On 5 January 2006, the Bank received a suit filed by the Archdiocese of Gdańsk against bank executory titles issued by the Bank. The plaintiff claims that loan agreements concluded with respect to the business activities of Wydawnictwo Archidiecezji Gdańskiej Stella Maris are invalid, as representatives of the Archdiocese were not duly authorized. The value of the object of the dispute amounts to PLN 14,979 thousand. The Bank prepared its reply to the suit and requested for dismissal of all claims. The Circuit Court in Gdańsk set the date for 17 February 2006 and decided that it was competent only for a part of the subject of dispute and referred the remaining part to the Circuit Court in Bydgoszcz. As a result of an attempt to settle the dispute out of court, both parties requested the court to suspend proceedings.
  - Trustee in bankruptcy of a company operating in the real estate developing sector (the name of the company is subject to confidentiality application) claims for payment of indemnity of PLN 32,256 thousand by the reason of effecting by the Bank of financial orders from the company's account on the basis of bank transfers orders and cheques bearing a forged signature of one of the persons authorized to represent the company in dealings with the Bank. The suit was filed on 6 February 2004. On 13 January 2005, the court suspended the proceedings until penal proceedings are completed.

On 20 September 2005, under the court's decision, the civil proceedings were initiated in connection with the sentence in a criminal case pertaining to the forgery of signatures on cheques. The hearing is scheduled for 17 March 2006.

The Management Board is of the opinion that any risks related to the proceedings before courts or public administration authorities are properly secured by the provisions established.

## 69. Custodian services

An offer of custodian services of Kredyt Bank S.A. entails managing securities accounts for domestic and foreign, both institutional and individual, customers. For the special group of customers, i.e. investment funds, Kredyt Bank S.A. also plays a role of a depository and transfer agent.

Kredyt Bank S.A. holds an authorization of the Polish Securities and Exchange Commission to manage securities accounts; it is also a direct participant of the National Depository for Securities (KDPW) as a Depository and a participant of the Securities Register (RPW) managed by the National Bank of Poland (NBP). On this basis, the Bank manages accounts for securities admitted to public trading, deposited in KDPW or RPW. The Custody Department in the Bank's Head Office is the Bank's business unit providing the said services.

Within its activities, this Department also acts as a depository for investment funds, deposits securities not traded on organized market, registered in securities registers and on sub-fiduciary accounts in domestic and foreign financial institutions.

The Group assists customers in the settlement of sale/purchase transactions related to securities traded on the regulated market (including the stock exchange market) and transactions outside the regulated market (including the inter-bank market).

The Group settles customers' transactions as required by KDPW, NBP and other institutions organizing trade in securities, and acts as an intermediary in the exercise of rights arising from securities, e.g. dividends, pre-emptive rights, interest, redemptions, splits, new issues, general meetings of shareholders.

As a depository for investment funds, the Bank offers the following custodian services:

- 1) keeping the register of a fund's assets;
- 2) ensuring accurate and proper calculation of NAV and NAVPS;
- 3) ensuring the proper settlement of contracts on a fund's assets;
- 4) supervision over fund's investment activities.

## 70. Risk management at Kredyt Bank S.A. Capital Group

The Bank's supervisory bodies, explicitly the Management Board and the Supervisory Board, play the most important role in the risk management process.

The Bank's Supervisory Board, through the Audit Committee, is informed on the most important issues and approves the actions of the Management Board in this respect.

Particular risks are dealt with directly by specialized Committees:

- Financial Markets Committee – supervising market risk in the Bank trading portfolio,
- Assets and Liabilities Management Committee – responsible for the management of market risk in the banking portfolio as well as the management of the Bank's structural liquidity,



- Operating Risk Committee – supervising implementation of the operating risk management process,
- Credit Risk Committee – supervising the credit risk management process.

Members of the Management Board supervise the works of the above committees; there are at least two Board members in each committee.

The Risk Management Department reporting directly to the President of the Bank's Management Board deals with the measurement and monitoring of all types of risks at Kredyt Bank. This is the only unit reporting all issues regarding risk, fully independent of business units.

In the process of the identification, measurement and risk management, the Bank applies techniques relevant to a given type of risk. The most vital ones are described below:

### **70.1. Market risk**

Market risk is defined as a degree of the hazard to the Bank's financial standing resulting from adverse changes in interest rates, exchange rates and prices of shares and their market volatility.

The interest rate and exchange rate risk are the two main risks at the Bank. The Bank does not actively operate on shares market and the majority of investments in stocks are long-term investments or strategic investments in subsidiaries. The Bank does not trade on commodity markets.

In order to improve management quality, since 2002, the activities of the Bank have been divided into two parts: trading book and banking book. Due to different nature of open positions, the risk is monitored in each book separately.

#### **70.1.1. Trading Book**

Trading book is a separated part of the Bank's portfolio, where the Bank intends to generate income resulting from short-term changes of prices, interest rates, exchange rates or other market parameters. The main activity of the trading book is associated with financial instruments in PLN, and, to a lesser extent, in USD and EUR.

##### **70.1.1.1. Interest rate risk**

Interest rate risk reflects the degree of a hazard to Kredyt Bank's financial standing arising from adverse changes in market interest rates.

The Value at Risk (VaR) is the basic metric of risk in trading portfolio; it is calculated in time horizon of 10 days at the 99% confidence level, taking into account market figures for the previous 250 days, what complies with international standards.

VaR limit and utilization as of 31 December 2005 is presented below.



Limit	Utilization as at 31 December 2005
VaR    EUR 2,000 thousand	EUR 257.96 thousand

Additionally, the level of interest rate risk is monitored and limited (by establishment of limits) against BPV (basis point value).

All above-mentioned limits concern the total trading book. The Trading Book Unit in the Treasury Department managing the trading book is divided into two sections (with the primary term of instruments as the basic division criterion). Internal VaR limits and stop-loss (maximum acceptable loss) restrict the activities of particular sections.

#### **70.1.1.2.        Currency risk**

##### **Currency position**

The exchange rate risk is the degree of the risk for the entity's financial standing resulting from adverse changes in exchange rates on the market. This risk covers income on currency exchange operations and measurement of open currency positions resulting from the difference between the value of assets and liabilities in a given currency.

As in the case of interest rate risk, value at risk is the basic measure applied in the monitoring of the currency risk. The parameters applied for calculations are identical as for the interest rate risk. VaR limit and utilization as of 31 December 2005 is presented below.

Limit	Utilization as at 31 December 2005
VaR    EUR 1,000 thousand	EUR 147.31 thousand

The 'value at risk' method is supplemented by stress testing which is the amount of possible loss in extremely adverse (critical), but probable changes in exchange rates.

##### **Foreign exchange options**

The Bank also offers foreign exchange options. The options portfolio is small and comprises mainly the options exercised upon the customer's initiative. The Bank does not maintain options portfolio for its own account, i.e. does not speculate. The options on the inter-banking market are the options hedging the position resulting from transactions with customers. Therefore, the risk in the portfolio of foreign exchange option transactions is immaterial. The scenarios analysis and 'Greek' parameters (open delta, gamma, vega) are the basic measures applied for monitoring this section risk. The scenario analysis method involves the calculation of the most adverse result on open position,

assuming defined changes in exchange rates and volatility. Below, we present the use and limits of the scenario analysis as of 31 December 2005:

Limit	Utilization as at 31 December 2005
Scenario analysis EUR 250 thousand	EUR 3.3 thousand

#### 70.1.1.3. Capital market risk

The Bank does not operate on the stock market within the trading book. As at 31 December 2004, IDM, which now is not included in the Bank's structure, was engaged in only insignificant trading activities related to its role as a market maker.

The capital requirements for the trading book as of 31.12.2005 and 31.12.2004 are as follows:

#### Capital requirements for the trading book

Market risk	30.12.2005	31.12.2004
Including:		
Equity securities price risk	0	3
Specific risk of debt instruments	54	43
General interest rate risk	9 859	8 568
Settlement risk and counterparty risk	5 561	4 491
Other	0	0
<b>Total capital requirement in the trading book</b>	<b>15 474</b>	<b>13 105</b>

#### 70.1.1.4. Financial derivatives transactions in the trading book

In 2005, the Bank entered into the following transactions:

- currency swap;
- interest rate swap;
- cross-currency interest rate swaps (CCIRS);
- forwards,
- forward rate agreements (FRA);
- options.

#### Currency swap

These transactions were made for commercial purposes at normal commercial terms.

As of 31 December 2005, there were 36 active currency swaps whereupon the Bank was obliged to purchase the total of the following amounts: PLN 948,823 thousand; USD 275,239 thousand, EUR 110,984 thousand for total amounts of PLN 933,529 thousand, USD 284,392 thousand, EUR 4,102

thousand and CHF 162,000 thousand. These transactions will be effected from 2 January 2006 to 11 December 2006.

As of 31 December 2005, the balance of currency swaps recognized as 'liabilities from transactions on financial instruments', an off-balance sheet item, amounted to PLN 2,274,837 thousand on forward purchase of currencies by the Bank and PLN 2,278,417 thousand on forward sale of currencies.

### **Interest rate swaps (IRS)**

These transactions were concluded for trading and collateral purposes at market terms. As of 31 December 2005, there were 261 active interest rate swaps with the total nominal value of purchased amounts of PLN 6,675,520 thousand and the total value of sold amounts of PLN 6,330, 565 thousand. These transactions will be effected from 9 January 2006 to 22 June 2015.

In addition, the Bank concluded 3 purchases for securing purposes with the total value of PLN 66, 000 thousand. These transactions will be effected from 12 April 2010 to 3 October 2013.

### **Forward rate agreements (FRA)**

As of balance sheet preparation date, there were 179 active purchase transactions and 154 active transactions on sale of forward rate agreements (FRA). These transactions were concluded for trading purposes at market terms on the interbank market.

As of 31 December 2005, the balance of FRAs recognized as 'liabilities from transactions on financial instruments', an off-balance sheet item, amounted to PLN 32,250,000 thousand on FRA purchase of by the Bank and PLN 26,375,000 thousand on the sale of FRA.

FRA purchase transactions were concluded for the total amount of PLN 32,250,000 thousand, including 132 transactions of the total value of PLN 22,850,000 thousand with domestic banks and 47 transactions for the total amount of PLN 9,400,000 thousand with foreign banks. FRA purchase transactions will be effected from 7 February 2006 to 19 December 2006.

FRA sale transactions were concluded for the total amount of PLN 26,375,000 thousand, including 118 transactions of the total value of PLN 19,450,000 thousand with domestic banks and 36 transactions for the total amount of PLN 6,925,000 thousand with foreign banks, with exercise dates from 8 February 2006 to 15 December 2006.

### **Cross-currency interest rate swaps (CCIRS)**

CCIRS transactions were concluded in order to swap the liquidity from one currency to another at market terms.

As of 31 December 2005, there were 6 active CCIRS whereupon the Bank was obliged to sell the total of EUR 82,082 thousand, USD 65,000 thousand, CHF 50,000 thousand, GBP 10,000 thousand for

total amounts of EUR 32,082 thousand and CHF 229,595 thousand. These transactions will be effected on: 23 May 2006, 1 June 2006, 30 June 2006, 2 January 2007, 1 June 2007.

As of 31 December 2005, the balance of CCIRS recognized as 'liabilities from transactions on financial instruments', an off-balance sheet item, amounted to PLN 692,951 thousand on forward purchase of currencies by the Bank and PLN 708,998 thousand on forward sale of currencies.

All currency swap, IRS, FRA, and CCIRS transactions have been concluded on inter-bank market with financial institutions. The Bank does not require any additional pledge for transactions concluded with those entities concluded within the transaction limits granted.

### **Forwards**

These transactions were concluded for trading purposes on market terms.

As of the balance sheet date, there were 364 forwards concluded with customers, whereupon the Bank was obliged to purchase the total of EUR 40,375 thousand, USD 13,575 thousand, GBP 4,500 thousand, SEK 2,000 thousand and PLN 185,865 thousand. At the same time, the Bank was obliged, as a result of forwards, to sell USD 14,406 thousand, EUR 32,444 thousand, GBP 2,547 thousand, SEK 242 thousand and PLN 225,744 thousand. These transactions will be effected from 2 January 2006 to 4 December 2007.

As of 31 December 2005, the balance of forwards recognized as 'forward exchange transactions', an off-balance sheet item, amounted to PLN 412,111 thousand on forward purchase of currencies by the Bank and PLN 412,382 thousand on forward sale of currencies.

There is a possibility of earlier settlement of transactions under the conditions agreed between the parties. The Bank assumes additional security for forwards. The establishment of the security in the following form is a pre-condition of concluding a forward transaction with a customer:

- frozen term deposit, or
- hold on cash on current account, or
- hold on cash on a separate frozen deposits account, or
- hold on the term deposit made by a customer prior to the forward conclusion date, or
- 'stand-by' loans securing forwards.

### **Options**

Put/call options for currencies are of trading and hedging nature, and are concluded on market terms. As at 31 December 2005, there were 128 active options whereupon the Bank:

- purchased calls for EUR/PLN with the total nominal value of EUR 4,061 thousand;
- purchased calls for EUR/USD with the total nominal value of EUR 16,030 thousand;
- purchased calls for USD/PLN with the total nominal value of USD 2,000 thousand;
- purchased calls for GBP/PLN with the total nominal value of GBP 1,615 thousand;

- purchased puts for EUR/PLN with the total nominal value of EUR 3,988 thousand;
- purchased puts for EUR/USD with the total nominal value of EUR 16,030 thousand;
- purchased puts for GBP/PLN with the total nominal value of EUR 1,615 thousand;
- purchased puts for USD/PLN with the total nominal value of USD 2,000 thousand;
- sold calls for EUR/PLN with the total nominal value of EUR 4,061 thousand;
- sold calls for EUR/USD with the total nominal value of EUR 16,030 thousand;
- sold calls for USD/PLN with the total nominal value of USD 2,000 thousand;
- sold calls for GBP/PLN with the total nominal value of GBP 1,615 thousand;
- sold puts for EUR/PLN with the total nominal value of EUR 3,988 thousand;
- sold puts for EUR/USD with the total nominal value of EUR 16,030 thousand;
- sold puts for GBP/PLN with the total nominal value of GBP 1,615 thousand;
- sold puts for USD/PLN with the total nominal value of USD 2,000 thousand;

There is a possibility of earlier settlement of transactions under the conditions agreed between the parties. As at 31 December 2005, the Bank also recognized in books one call option for indices with the total nominal value of PLN 53,300 thousand and one put option with the total value of PLN 1,400 thousand.

### **Embedded derivatives**

Following the review of assets and liabilities, embedded derivatives, which must be separated and disclosed, were identified in debt instruments issued by a financial entity. As a result, option-type embedded derivatives sold by the Bank were separated, where credit rating and purchased derivatives are the basic instrument. The profit from the measurement of derivatives embedded in debt instruments is recognized in current profit/loss in 'profit/loss on financial operations'. As at 31 December 2005, the measurement of derivatives embedded amounted to PLN 6.2 million.

The embedded derivatives are measured according to the measurement models of these instruments and input data are derived from the market.

#### **70.1.2. Banking book**

The banking book covers operations not covered by trading portfolio, i.e. commercial activities of branches, credit intermediaries and the portfolios of securities hedging the liquidity and constant interest income. The banking book aims at the elimination of the market risk.

##### **70.1.2.1. Interest rate risk**

The Bank actively manages the interest rate risk for 5 main currencies of the balance sheet: PLN, EUR, USD, CHF, GBP.

An interest rate gap prepared separately for each currency is the basic measurement and risk-limiting tool in the banking portfolio. The following risk metrics are calculated on that basis:

- the sensitivity of the measurement of assets and liabilities (BPV);
- duration;
- accumulated gap ratios.

An analysis of the interest rate gap applied in the interest rate risk management of the banking book is based on information on particular items of the balance sheet of the Bank as well as off-balance items sensitive to changes of interest rates. In the case of financial instruments without defined maturity date (according to a stability analysis for each type of product), the Bank implemented the model of periodic deposits rollover. This approach towards products allows for effective management of risk associated with this type of instruments and for the generation of constant income from investments of these assets.

The banking book comprises the following items:

- Hedging - item resulting from the operations of branches (along with hedging transactions).  
We distinguish between:
  - benchmark portfolios of current accounts in PLN, EUR and USD,
  - benchmark portfolio of savings accounts in PLN,
  - branch position, except for the part of stable current accounts and savings accounts.
- Transformation, including:
  - benchmark portfolio of Free Capital,
  - item with credit risk (Credit Book).

### **Interest rate risk analysis**

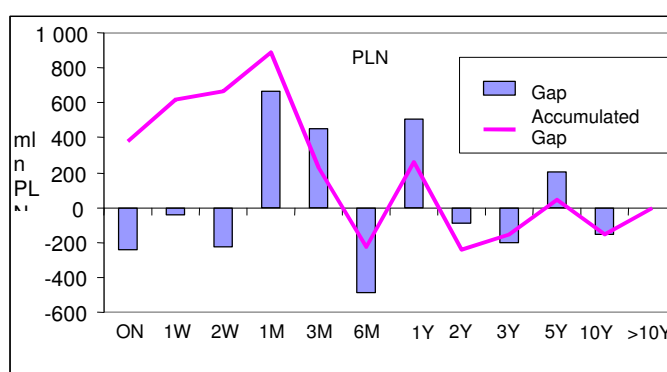
The interest rate risk analysis was conducted upon the following assumptions:

- the stable part of current PLN and foreign currency accounts (in EUR and USD) is invested cyclically for the period of 5 years for PLN (1/60th of the stable part invested monthly), and 2 years for foreign currencies (1/8th of the stable part invested monthly);
- two stable portions are separated from savings accounts; the first portion is invested cyclically for 6 months (1/6th of the stable part invested monthly), and the second part is invested for 3 years (1/36th of the stable part invested monthly);
- unstable parts of current accounts in PLN, EUR and USD, of savings accounts and current accounts in other currencies are classified in the shortest term horizon;
- free capital approved for the whole year is invested cyclically for the period of 10 years (1/120th of the free capital invested monthly), and an excess or shortage compared to actual amount of free capital is classified in the shortest term horizon;
- benchmark is applied to non-working loans (40% - ON, 30% - 1M, 30% - 3M);
- loans are recognized in net terms;
- loans are presented according to repayment schedules;
- except for nominal flows, also known future interest flows are presented in the report;
- each flow is divided proportionally into two parts which are classified in adjoining nodes of the curve;
- cumulative gap is calculated from the longest to the shortest term periods.

The interest rate gaps in particular currencies (in millions) and based on internal system of transfer rates are presented below.

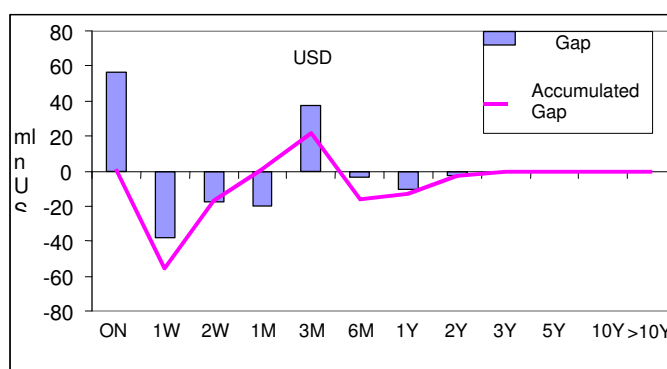
## - PLN

For items in PLN, a negative value of the gap in the term ranges up to 2 weeks result from holding short-term fixed interest rate customer deposits. The positive gap in term ranges from 2 weeks up to 3 months is a result of a mismatch of volumes of floating interest rate loans and deposits. And the gap in the term range from 6 months up to 1 year results from fixed interest rate loans extended by intermediaries. The negative gap in term ranges from 3 months to 6 months is associated with repricing of the first tranche of perpetual bonds based on 6M WIBOR. The gap in various term ranges is a result of the mismatch of the benchmark portfolios structures.



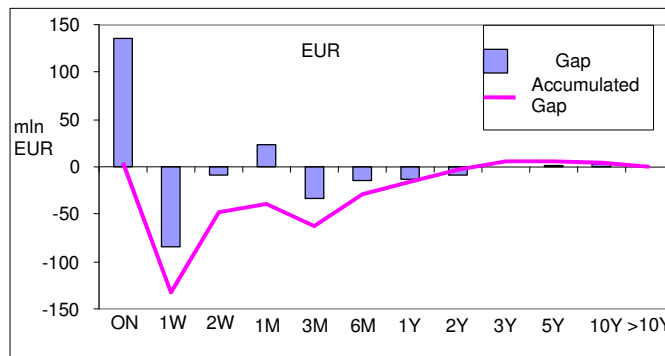
## - USD

The gap for items in USD is positive in ON term range as a result of the classification of non-working loans and mature loans. And, in the term ranges up to 3 months, it is a result of granting FxSwap. A negative gap results from accepted fixed interest rate customer deposits and the cash loan (ranges of 1-2 weeks).



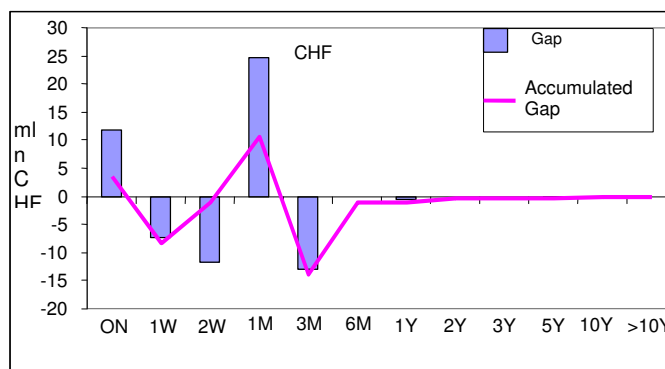
## - EUR

For items in EUR, a positive gap is a result of extending short-term deposit (ON range) and the mismatch of the volumes of floating interest rate loans and deposits and accepted long-term cash loans (the range up to 1 month). A negative gap in short term ranges (up to 1 week, up to 2 weeks) is a result of holding fixed interest rate deposits by the Bank. And, in the term ranges from 1 month up to 3 months, it is a result of accepted long-term cash loans. The gap in term ranges from 3 months to 2 years is a result of the mismatch in the benchmark portfolio between bonds and the stable part of current accounts and fixed interest rate deposits.



## - CHF

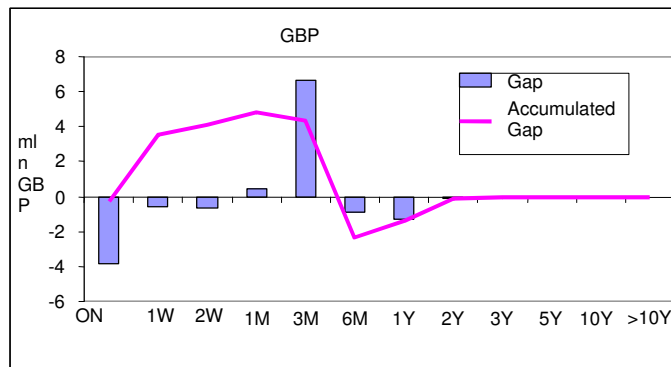
For CHF, a positive gap in ON term range and ranges from 2 weeks to 1 month results from mismatch between floating interest rate loans and deposits and accepted long-term cash loans. A negative gap in term ranges from ON to 2 weeks are associated with the acceptance of FxSwap transaction, and the gap in the range from 1 month to 3 months is a result of accepting CIRS.





## - GBP

The gap for items in GBP in term range from 1 month to 3 months is positive with regard to granted CIRS. A negative gap is a result of accepted fixed interest rate deposits.



The table below illustrates the Bank's basis point value (BPV) accompanied with the Bank's parallel shift in interest rates by 10 p.b. up for particular currencies and portfolios.

		in millions of original currency			
		BPV			
Currency/portfolio		31.12.2005		31.12.2004	
PLN	hedging	0,223	0,188	0,352	0,150
	transformation*		0,035		0,203
PLN	hedging	0,012	0,012	-0,010	0,059
	transformation		0,000		-0,069
PLN	hedging	0,008	0,012	0,051	0,060
	transformation		-0,005		-0,009
CHF		0,004		0,006	
GBP		0,001		0,002	

At the end of 2004, transformation was composed of benchmark portfolios of PLN current accounts, free capital and credit book. In 2005, benchmark portfolios of current accounts are included in hedging.

The use of BPV limit (an aggregate of the absolute values for all currencies, Hedging and Free Capital portfolios) as at 31 December 2005:

Limit in millions EUR	1,000
BPV in millions EUR	0,077

### **Hedge accounting**

In the third quarter of 2005, Kredyt Bank applied hedge accounting (fair value hedge) to asset swaps for the first time. The purpose of hedge accounting is to hedge fixed interest rate bonds - IRS (fix to float). For the purpose of the relationship being described, the bond is recognized as available-for-sale instrument and IRS as held-for-sale instrument. On the date the hedging relationship is established, hedge effectiveness (hedge expected) is preliminarily evaluated with the application of the following method:

$$HE = - \frac{BPV_{BOND}}{BPV_{IRS}}$$

During the hedging relation, a hedge effectiveness ratio is determined with Dollar-Offset method:

$$HER = - \frac{\Delta FV^{BOND}}{\Delta FV^{IRS}} = - \frac{FV_t^{BOND} - FV_0^{BOND}}{FV_t^{IRS} - FV_0^{IRS}}$$

Exceeding the limit of 80%-125% is related only to material changes in fair value. The effectiveness is measured at the end of each month.

#### **70.1.2.2. Currency risk**

As mentioned above, the currency position is managed in the trading book. The positions related to the Bank's customers' transactions arising during the day are transferred, via internal transactions, to the trading book.

It should be noted here that the currency risk at Kredyt Bank is perceived not only as the risk occurring for open currency position, but also as the risk of change in the value of certain products as a result of changes in exchange rates. In particular, this risk occurs in the case of loans extended in foreign currencies. In order to mitigate credit risk, increasing in the case of the growth in the exchange rate of loan currency (this also refers to loans granted in PLN, with its value indexed to the foreign currency exchange rate), the loans agreements for institutional customers contain clauses on the establishment of additional collateral or permit to translate the loan, when the customer does not generate income in the loan currency. Additionally, in order to hedge the exchange rate risk the customer is exposed to, derivatives (forwards, options) are offered to him.

## 70.2 Liquidity risk

The liquidity risk is strictly associated with activities of any bank. It results, among other things, from the mismatch of assets and liabilities in terms of maturity dates what is a natural effect of varied customers' requirements as regards deposits and loans. Maintenance of financial liquidity, understood as the ability to timely meet financial liabilities, is the crucial element of the policy on assets and liabilities management applied by the Bank. The current liquidity is maintained through correcting the surplus or shortage of liquid cash by operations conducted on the interbank money market. The Bank safety calls for the maintenance of liquid reserves as well as term and quality structure of the whole balance sheet. Decisions related to liquidity risk management are made by the Bank's Assets and Liabilities Management Committee. The Risk Management Department measures and monitors strategic (long-term) liquidity. The current and operating tasks are performed by the Treasury Department.

The Bank hedges the liquidity risk by:

- maintenance of appropriate level of cash, taking into account volume of statutory provisions;
- maintenance of liquid securities (government bonds) portfolio, properly hedging the term structure of the Bank's liabilities without specific maturity dates;
- performing transactions on derivatives;
- establishment and monitoring of the observance of corporate prudence standards related to liquidity;
- maintenance of a diversified portfolio of deposits as regards terms and customers;
- monitoring the mismatch of the maturity dates of assets and liabilities, what makes it possible to forecast the demand for liquid assets and avoid excessive concentration of cash disbursements on a close date;
- access to the interbank market and open market transactions;
- access to the lombard loan;

A crucial factor affecting the safety of the Bank operations is the support of KBC Group – the strategic investor.

An analysis of the Bank's liquidity is performed mainly on the basis of the liquidity gap report and the assessment of the deposit base stability.

To monitor the liquidity risk, on the basis of the liquidity gap, the Bank established the following liquidity limits:

- Stock Liquidity Ratio (SLR)
- Coverage Ratio (CR)

### **The stability of the deposit base**

A stable deposit base<sup>1</sup>, not affected by seasonal phenomena, is the basic source of the Bank's financing.

The diversification of the deposit base allows for the bank's independence of any specific market segment, customer group or specific deposit type. As at 31 December 2005, large deposits of over EUR 1 million accounted for 19% of the total deposits value.

The stability of the deposit base is particularly ensured with cash from individual customers. At the end of 2005, the percentage of individual customers' deposits was at the level of 56%. More volatile deposits of the financial sector, business entities and the public sector accounted for 4%, 28% and 12% of the deposits respectively.

Current deposits and negotiable term deposits account for 58% of the base, whereas the remaining 42% comprises term deposits (27%) and savings accounts (15%).

The structure of term deposits (except for interbank term deposits and negotiable term deposits) is extremely advantageous from the point of view of initial maturity date. On 31 December 2005, it was as follows:

▪ Up to 1 week	12.87%
▪ Up to 1 month	6.10%
▪ Up to 3 months	28.60%
▪ Up to 6 months	24.35%
▪ Up to 12 months	16.48%
▪ Up to 24 months	2.41%
▪ Other	9.19%

In terms of a currency type, the structure of the deposit base as at 31 December 2005 was as follows: PLN – 80.9%, USD – 9.0%, EUR – 9.2%, GBP – 0.7%, CHF – 0.1%, other currencies – 0.1%.

### **70.3. Operating risk**

Being aware of dangers resulting from operating risk, the Bank continued preparations for the implementation of the project on measurement and monitoring of this type of risk under so called 'standard method' defined by the Basel Committee. The Operating Risk Committee is responsible for supervision over this process. The business units comprising, among others, employees acting as operating risk coordinators are in charge of the current operating risk management for supporting strategic targets of the Bank.

A separate risk management function, independent from other units generating risk, develops tools for identification and assessment techniques for the operating risk and reports volume of losses.

The actions required by methodologies and rigours enabling the application of the standard method for the establishment of capital requirements were taken. The database including information

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<sup>1</sup> Deposit base figures do not concern interbank deposits.

facilitating the quality assessment of the most frequent events, and statistical material for quantitative measurement of operating risk has been created. At the same time, the Bank conducts piloting operating risk self-assessment processes, recognizes the risks inherent in business processes and processes supporting the business activities which may generate substantial operating risk for the Bank.

#### **70.4. Credit risk**

The Bank's credit risk is defined as the risk of non-payment of amounts due if a borrower, guarantors, reinsurer, contractor or issuer loses its creditworthiness.

Credit risk is managed taking into account the credit risk aspect corresponding to individual transactions and from the portfolio perspective.

The process of risk management for individual transactions entails risk assessment for such a transaction and, depending on its level, application of an appropriate decision-making process.

The portfolio risk management is the responsibility of the Bank's Management Board and the Credit Risk Committee, where the Credit Risk Committee is responsible for the following:

- acceptance and substantial supervision over the methods of credit risk measurement;
- recommending to the Bank's Management Board and the Supervisory Board admissible level of credit risk in the Bank's and subsidiaries' balance sheets;
- expressing opinions on the Bank's credit policy;
- expressing opinions on creation of provisions and collateral;
- expressing opinions on internal credit limits;
- changing risk limits and approval of limit exceeds within the powers of the Bank's Management Board;
- substantial supervision over the program of the Bank's adjustment to the requirements of the New Capital Accord related to credit risk;
- approval of the new products in terms of credit risk.

With reference to the New Capital Accord (Basel II), the Bank is intensively preparing its implementation.

With regard to credit risk, application of an option which involves successive conversion from less advanced approaches offered under the agreement (Standard Method) to more advanced approaches (Internal Ratings Method: Basic and Advanced).

The Programme on Quantitative Assessment of Credit Risk - QCR (Quantitative Credit Risk) Programme - was created for the fulfillment of the tasks in this area, the completion of which will facilitate among others:

- development and implementation of credit risk measurement models;

- development and implementation of databases and tools facilitating the collection of data for the purposes of model development and their testing;
- reorganisation of the credit process taking into account the established level of risk;
- development and implementation of RAROC concept at the Bank,
- development and implementation of databases on credit risk, tools and reporting standards for the purposes of calculating capital adequacy by the standard method and internal ratings.

It is assumed that fulfillment of the above tasks will improve ROE through optimal adjustment in terms of capital requirements, the improvement of efficiency of credit processes at the Bank and enhancement of business management.

#### **70.4.1. Restructuring and debt recovery processes in 2005**

In 2005, the Bank took an extensive action to reduce the portfolio of non-performing receivables.

As a result of the Bank's internal changes in 2004, in 2005 cooperation between the units servicing doubtful portfolio improved and the access to customer data was better, what positively affected the decisions made with regard to restructuring and debt recovery in 2005. Additionally, the adjustment of the problems related to reporting data to decision-making units contributed to the above improvement what made it possible to generate the results described above.

At the beginning of 2005, the Bank managed the portfolio of receivables for which individual evidence of impairment was identified for the total amount of PLN 3,909,885 thousand. At the end of the year, non-performing receivables decreased by PLN 779,681 thousand.

Throughout the whole year, the Bank conducted intensive works aimed at effective debt rescheduling and recovery. As a result, the Bank considerably decreased receivables for which individual evidence of impairment was identified, mainly due to total or partial payments made by debtors, the sale of the Bank's debt, the sale of collateral and restructuring resulting in change in estimates of impairment and decrease in impairment charges.

## 70.4.2. Risk metrics

### Balance sheet instruments

Instrument	Carrying amount	Risk weighted value
Cash	385 048	0
Receivables	12 490 762	9 508 997
Debt securities	6 538 299	0
Other securities, shares	227 573	227 573
Fixed assets	346 913	346 913
Intangible assets	2 426	2 426
Other	298 020	72 602
<b>Total banking portfolio</b>	<b>20 219 041</b>	<b>10 158 511</b>
Trading portfolio	692 854	1 530
<b>Total balance sheet instruments</b>	<b>20 911 895</b>	<b>10 160 041</b>

### Off-balance sheet instruments

Instrument	Nominal value	Balance sheet equivalent	Risk weighted value
Interest rate instruments	137600	2761	552
Foreign exchange instruments	72 002	7 219	1 444
<b>Total derivatives</b>	<b>209 602</b>	<b>9 980</b>	<b>1 996</b>

### Other off-balance sheet – banking portfolio

Instrument	Carrying amount	Credit equivalent	Risk weighted value
Credit lines	2 612 053	1 041 078	1 027 645
Guarantees granted	1 073 738	913 098	883 619
Letters of credit	28 705	28 705	28 705
Other	11 250	11 250	2 250
<b>Total</b>	<b>3 725 746</b>	<b>1 994 131</b>	<b>1 942 219</b>

	Risk weighted value	Capital requirement
<b>Total credit risk exposure (banking portfolio)</b>	<b>12 102 726</b>	<b>968 218</b>

#### 70.4.3. The structure of the exposure concentration for the Group

The Bank's exposure towards corporate customers as at 31.12.2005 and 31.12.2004, by major exposures, is as follows:

Exposure towards 10 major corporate customers of the Group		
Entity	Share (%) in the portfolio as at 31.12.2005	Share (%) in the portfolio as at 31.12.2004
Customer 1	2.7	3.6
Customer 2	2.3	2.0
Customer 3	2.0	1.9
Customer 4	1.9	1.8
Customer 5	1.9	1.6
Customer 6	1.5	1.4
Customer 7	1.4	1.2
Customer 8	1.4	1.2
Customer 9	1.2	1.2
Customer 10	1.2	1.1
<b>Total</b>	<b>17.4</b>	<b>16.9</b>

The Bank's exposure as at 31.12.2005 and 31.12.2004, by industrial segments, was as follows:

Exposure in industrial segments	Exposure (%)	Exposure (%)
Industry	31.12.2005	31.12.2004
Production activities	28.8	27.0
Retail and wholesale; repairs of motor vehicles and articles for personal and home use	22.9	21.5
Real estate administration and lease	14.6	14.3
Public administration and national defense, legally guaranteed social care	8.4	12.7
Financial intermediation	8.1	5.7
Supplies of electricity, gas and water	4.9	5.7
Construction	3.5	3.3
Other services for municipalities, social and individual services	1.4	2.6
Agriculture, hunting and forestry	2.3	1.9
Hotels and restaurants	1.6	1.6
Transport, storing and communication	1.6	1.5
Education	1.2	1.1
Health care and social care	0.5	0.2
Other	0.2	0.9
<b>Total</b>	<b>100</b>	<b>100</b>



The Group's exposure as at 31 December 2005 and 31 December 2004 by geographical segments was as follows:

Geographical exposure		
Province	Gross loans structure (%)	Gross loans structure (%)
	31.12.2005	31.12.2004
Mazowieckie	18.5	23.8
Lubelskie	15.8	13.6
Śląskie	10.9	9.5
Wielkopolskie	9.7	9.2
Dolnośląskie	9.1	9.6
Pomorskie	7.6	8.0
Małopolskie	6.3	5.2
Łódzkie	4.6	4.6
Zachodniopomorskie	3.8	3.4
Podlaskie	3.2	3.1
Kujawsko-pomorskie	2.3	2.2
Warmińsko-mazurskie	2.3	2.3
Podkarpackie	1.7	1.8
Świętokrzyskie	1.5	1.3
Non-resident	1.1	1.1
Lubuskie	0.8	0.8
Opolskie	0.8	0.5
<b>Total</b>	<b>100</b>	<b>100</b>

**Signatures of all Management Board Members**

Date 28.02.2006	Ronald Richardson	President of the Management Board	.....
Date 28.02.2006	Krzysztof Kokot	Vice-President of the Management Board	.....
Date 28.02.2006	Małgorzata Kroker-Jachiewicz	Vice-President of the Management Board	.....
Date 28.02.2006	Guy Libot	Vice-President of the Management Board	.....
Date 28.02.2006	Bohdan Mierzwiński	Vice-President of the Management Board	.....

**Signature of a person responsible for keeping the account books**

Date 28.02.2006	Joanna Gajda	Chief Accountant of the Bank	.....
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The Management Board's report on  
the operations of Kredyt Bank S.A.  
Capital Group  
in the period covered by this financial  
statement prepared as at  
31.12.2005

## TABLE OF CONTENTS

<b>1. Introduction – basic economic and financial values disclosed in the annual financial statement.....</b>	<b>4</b>
<b>2. Events and factors exerting material impact on the operations and the financial result of Kredyt Bank Group in 2005 .....</b>	<b>5</b>
2.1. Macroeconomic situation .....	5
2.1.1. Overall economic situation in Poland .....	5
2.1.2. Monetary policy of the central bank.....	6
2.1.3. Outlook for the Polish economy in 2006.....	8
2.2. Banking sector in 2005.....	9
2.3. Risk management .....	10
2.3.1. Credit risk.....	11
2.3.2. Liquidity risk .....	13
2.3.3. Market risk .....	14
2.3.4. Operating risk .....	15
2.4. Events and contracts material for the Group's operation in 2005.....	15
<b>3. The Group's organization and capital relations .....</b>	<b>18</b>
3.1. The Group's structure and description.....	18
3.2. Investment plans, including capital investments .....	19
3.3. Shareholding structure of the Group's parent company .....	20
3.4. Authorities of the Group's parent company.....	20
3.5. The Bank's and the Group's shares held by members of management and supervisory authorities.....	22
3.6. Remuneration of persons managing and supervising the Group's parent company.....	22
3.7. Related party transactions .....	23
<b>4. The Group's products, services and areas of operation .....</b>	<b>23</b>
4.1. The Bank's products, services and areas of operation.....	23
4.1.1. Retail segment.....	23
4.1.2. Corporate segment .....	28
4.1.3. Money and capital markets.....	29
4.1.4. Custody services .....	29
4.1.5. Cooperation with international financial institutions.....	29
4.1.6. Distribution channels .....	30

4.2.	Operations of the Group companies .....	31
<b>5.</b>	<b>The Group's financial results in 2005 .....</b>	<b>33</b>
5.1.	Income statement structure.....	33
5.2.	Assets structure.....	36
5.3.	Liabilities structure .....	41
5.4.	Off-balance sheet items .....	44
<b>6.</b>	<b>Ratings of the Bank's financial reliability .....</b>	<b>45</b>
<b>7.</b>	<b>Corporate governance .....</b>	<b>46</b>
<b>8.</b>	<b>The Group's outlook and growth drivers .....</b>	<b>47</b>
<b>9.</b>	<b>Statement of the Management Board .....</b>	<b>48</b>
9.1.	True and fair view presented in the financial statements.....	48
9.2.	Appointment of the certified auditor for financial statements .....	49

## **1. Introduction – basic economic and financial values disclosed in the annual financial statement.**

In 2005, the Group generated net profit of PLN 415,878 thousand, i.e. by 165.2% higher than net profit for 2004. ROE increased by 11.5 p.p., to the level of 26.0%, ROA by 1.3 p.p., to the level of 2.0%. In 2005, the Group focused mainly on credit risk, debt recovery and restructuring areas and the reduction and control of functioning costs. Actions taken in these areas resulted in specific effects reflected in changes of basic financial ratios and values.

In 2005, unlike in the previous year, risk costs had marginal impact upon the Group's financial results. Net impairment charges for financial assets, other assets and provisions as at 31.12.2005 amounted to – PLN 9,167 thousand, i.e. were by 93.7% lower as compared to 2004 figures.

As a result of the loan portfolio restructuring, the value of non-performing loans in 2005 dropped by 17.9%, i.e. PLN 760,147 thousand. The quality of the portfolio measured with the share of non-performing receivables in total gross loans and advances to customers improved by nearly 2p.p. to 28.5%, despite the decrease in total gross loans and advances to customers. The coverage of doubtful receivables by impairment charges ratio in 2005 increased by 8.8 p.p. to 72.1%; this ratio was among the highest in the banking industry.

Cost/income ratio (CIR) at the end of 2005 was at the level of 73.0%, what implies an improvement by 3.5 p.p. against last year's figures, achieved despite a slight decrease in net income. Further improvement of this ratio remains one of the Group's most imperative financial goals for the future. Functioning and administrative costs in 2005 amounted to PLN 890,825 thousand and were lower by 15.6% than in the previous year. Savings were made in all basic categories: material costs, depreciation and staff costs.

The positive trends in net operating income generated by the Bank confirm an increasing probability of settling retained tax losses. Therefore, the Bank, as of 31.12.2005, recognized the excess of deferred tax asset over deferred tax liability amounting to PLN 102,2 mln, what had a direct impact upon the Group's net result in 2005.

As a result of the Group's restructuring process, the balance sheet structure has improved. As compared to 31.12.2004, as at 31.12.2005, total customer loans to total customer deposits ratio increased from 100.3% to 84.7%. The share of liquid assets, defined as the aggregate of amounts due from banks, financial assets measured at fair value through profit or loss and investment securities, in total net assets rose from 34.2% to 46.3%. Capital adequacy ratio improved from 14.7% to 16.4%.

All measures taken by the Group which resulted in the improvement of relations and ratios described above aim at further upgrading of operations safety and the establishment of dependable basis for future profits.

## **2. Events and factors exerting material impact on the operations and the financial result of Kredyt Bank Group in 2005**

### **2.1. Macroeconomic situation**

#### **2.1.1. Overall economic situation in Poland**

Following the decline in economic situation in the first quarter of 2005 resulting, to a large extent, from the static base effect, further on during the year a gradual improvement in economic growth rate was observed. In further quarters of 2005, GDP amounted to 2.1%; 2.8% and 3.7% y/y. The growth was a result of the vanishing high base effect and gradual improvement in internal demand levels. However, export remained the main driving force of the Polish economy, despite the appreciation of the Polish zloty in this period. The tendencies observed from the beginning of the year consolidated in the last quarter. It is estimated that, in the last three months of the year, an economic growth rate rose to 4.0% y/y, mainly due to further moderate increase in domestic demand and still positive impact of net exports. And, in the whole year 2005, it should be at the level of ca. 3.2% y/y.

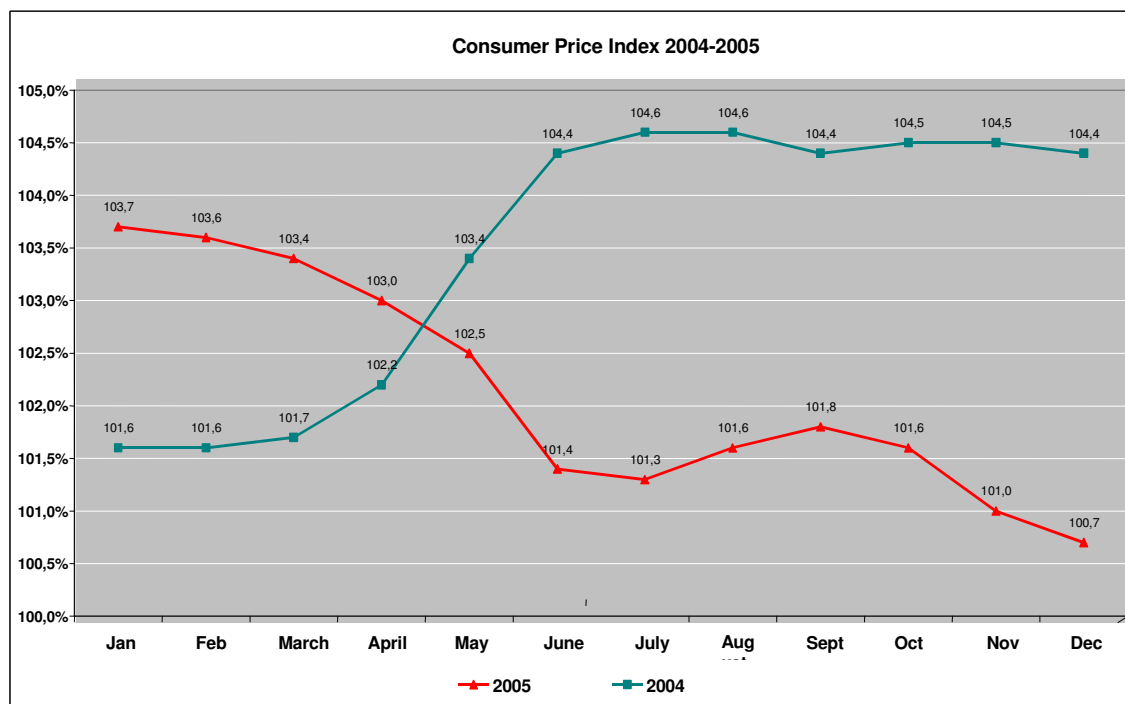
The major factors having a positive impact upon the macroeconomic environment are as follows:

- gradual improvement of domestic demand;
- growth in the building industry;
- gradual improvement of the labour market;
- decrease in investment risk following the accession of Poland to the EU;
- growth in financial profitability of enterprises;
- safe implementation of the State budget (the deficit on the level lower than assumed in the 2005 schedule) and good perspectives for the 2006 budget;
- significant improvement of external balance due to exports increase and influx of EU grants.

Throughout 2005, a significant decline in consumer prices occurred (on a year-to-year basis) being, particularly in the second half of the year, a direct effect of the stabilization of prices on the global fuels market, the appreciation of the Polish zloty and a material decrease in annual dynamics of food prices which resulted, among others factors, from the embargo on the import of Polish foodstuffs to Russia placed in November.

At the end of 2005, inflation (measured with CPI) equaled 0.7%, i.e. it was below the bottom limit established by the Monetary Policy Council for the year 2005 regarding the inflationary target of 2.5%  $\pm$  1p.p. y/y.

The diagram below shows CPI in 2005 against CPI in 2004.



The following factors are listed among the worrying macroeconomic tendencies and negative phenomena:

- relative weakness of factors that may steadily support economic growth, including relatively low level of the absorption of EU grants limiting the scale of observable growth in investments;
- potentially unstable political environment.

The increase in the share of investments in GDP should be perceived as the key issue and the main threat to the re-establishment of the high growth in the medium-term time horizon.

### 2.1.2. Monetary policy of the central bank

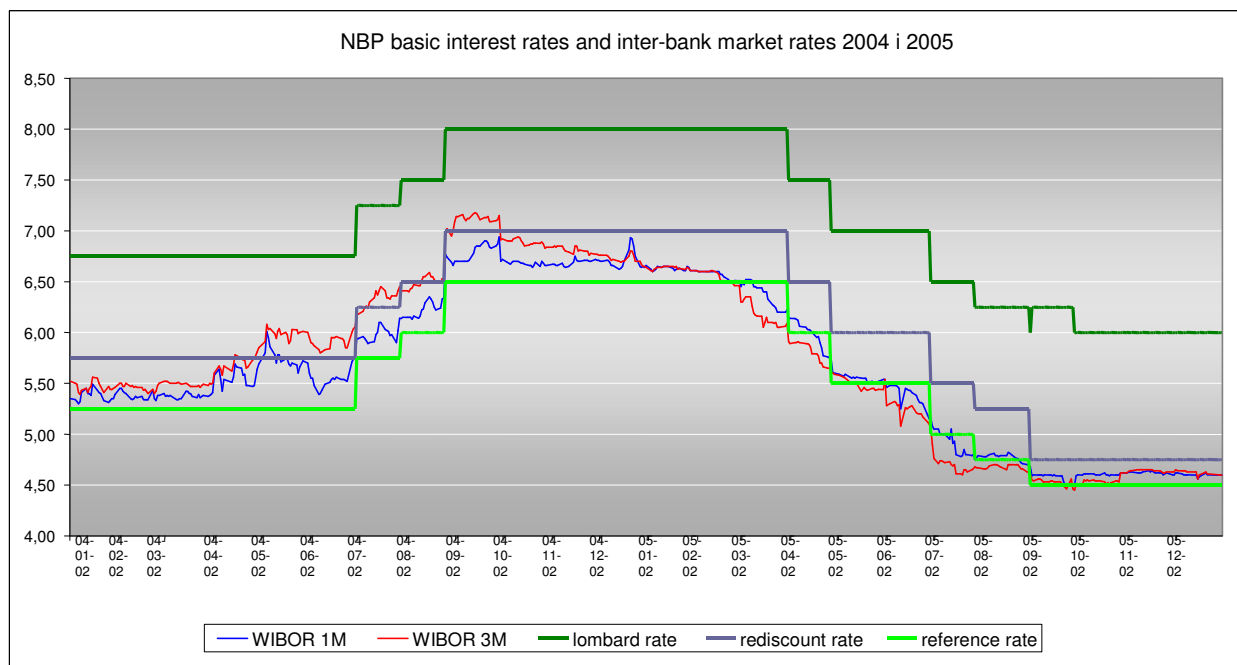
In 2005, the Monetary Policy Council, in response to the decline in CPI and surprisingly low GDP figures in the first quarter of 2005, decreased interest rates repeatedly (by the total of 200p.p.). Nevertheless, towards the end of the second quarter and in the second half of the year, the pace of interest rates decreases was hindered due to the signs of upcoming growth in business activity and the anxiety related to the impact of record-breaking crude oil prices upon the inflation rate. In the first half of 2005, the Monetary Policy Council changed its approach in monetary policy three times: in February – to non-restrictive, in April – to neutral, and again to non-restrictive in June. Since the beginning of 2006, this instrument has no longer been available; instead the Council will publish a detailed report on hazards to inflation.

- At the end of 2005, the basic interest rates of the central bank were as follows:
- reference rate 4.5% p.a.;
- lombard rate 6.0% p.a.;



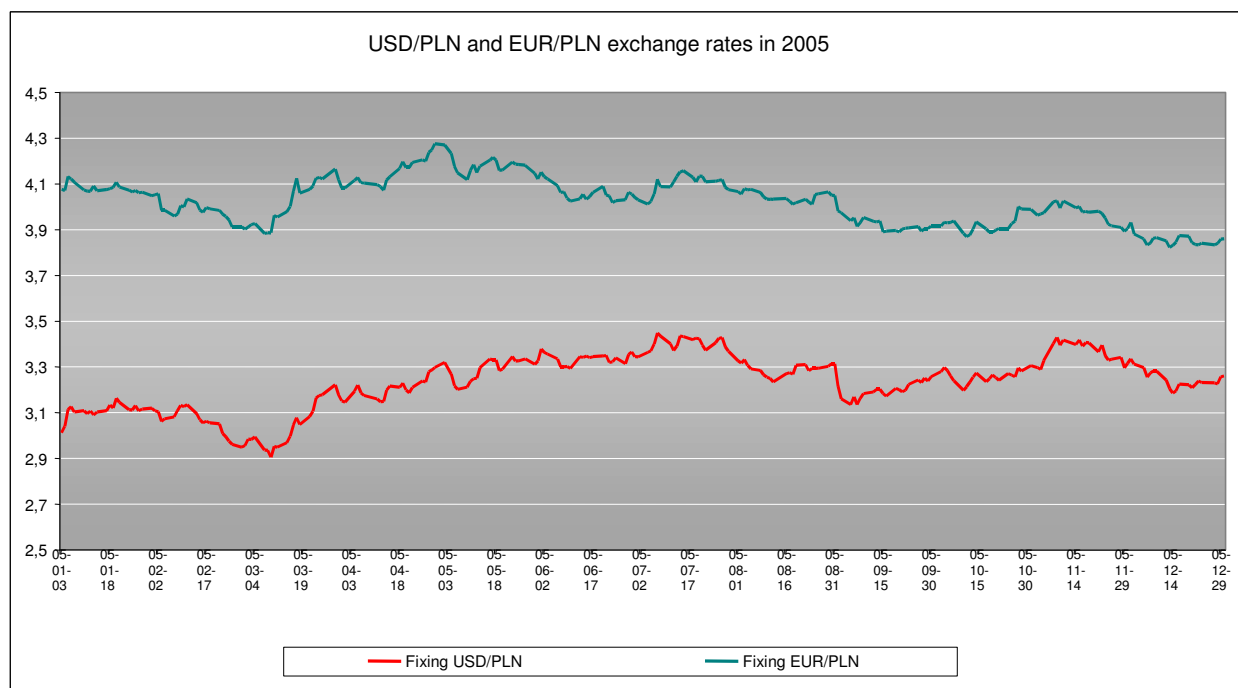
- rediscount rate 4.75% p.a.;
- NBP deposit rate 3.5% p.a.

The diagram below illustrates basic interest rates of the National Bank of Poland against inter-bank market rates in 2004 and 2005.



The fear that too restrictive monetary policy contributed to the slump in economic growth in the first half of 2005 was the main cause of the decrease in NBP interest rates in the first half of 2005. At the same time, the decline in the inflation rate resulting from a base effect and no pressure on an increase in salaries and wages was conducive to deeper cuts.

The Polish zloty, after significant appreciation in the first quarter to its record high, both against Euro and US dollar, slightly lost in value in the second quarter due to a global change in investors' approach to the currencies of emerging economies and an increase in political risk prior to parliamentary elections. The losses were compensated for in further quarters. At the end of December 2005, the exchange rates were as follows: PLN 3.8598 per 1 EUR and PLN 3.2613 per 1 USD. The diagram below illustrates tendencies in USD/PLN and EUR/PLN exchange rates in 2005.



### 2.1.3. Outlook for the Polish economy in 2006

Domestic demand and exports, although to a lesser extent than in previous years, will be the main driving force of economic growth in 2006. The increase in domestic demand will be an effect of a higher level of individual consumption and increase in investing activities in the Polish economy. Gradual enhancement on the labour market and adjustment of pensions planned for 2006 will be the basic causes of the consumption improvement. A more dynamic consumer demand, very high levels of resources of Polish enterprises and the lowest ever interest rates will contribute to the growth in investment demand. Furthermore, simplification of application procedures for EU grants declared by the government which so far have been very effective obstacles in utilizing such grants, will be a crucial factor. Imports will rise along with the growth in domestic demand, what will also contribute to a greater role of net exports in economic growth.

Despite the growth in domestic demand, the inflation rate should still remain under control and in 2006 it should not exceed the NBP inflationary target of 2.5% y/y. The low inflation rate in 2006 will be a result of its extremely low level towards the end of 2005 and wage discipline resulting from a high unemployment rate. The situation on the fuels market and food market will also be crucial in inflation processes. However, it should not result in exceeding the inflation rate of 2.5% y/y. In response to the low inflation rate, the absence of excessive wage pressure and Polish zloty appreciation, the central bank may further reduce the cost of money, i.e. continue reducing interest rates.

In 2006, PLN exchange rate should remain strong due to fundamental factors, such as still low deficit on current accounts and the influx of direct foreign investments fully covering the above deficit. PLN exchange rate will depend, to a large extent, on the political situation and on its stability. The intensification of works on the 2007 budget and local government elections in autumn will become potential periods of increased anxiety on the foreign currency market. Also, excessive appreciation of the Polish zloty may undermine the Polish export and, as a result, the economic growth in Poland.

## 2.2. Banking sector in 2005

The economic recovery, progressing on a quarter-by-quarter basis, has contributed to an increased interest in financial services and to the situation of the banking system, which in 2005, reported a record-breaking increase in net profit<sup>1</sup> and further improvement of assets quality. The main causes of the above financial results were as follows:

- increase in balance and transaction volumes;
- lower balance of write-downs for non-performing receivables;
- control over functioning costs.

The prevailing high profitability of enterprises accompanied with their low investing activity had a material impact on the changes of banks' loans portfolios. Loans to corporate customers increased by only 3% p.a. Slow growth of volumes was compensated for with high growth in loans to households (23% y/y). Particularly fast growth in sales was recorded for loans to finance real estate. Fast growth in mortgage loans (over 40% y/y in nominal terms and ca. 23% net of the impact of changes in PLN exchange rates), and particularly the fact that over 60% of amounts due are expressed in foreign currencies, resulted in objections of the banking supervision authorities which emphasized that the present FX-related preferences of certain banks and their customers complicate an issue of prudent assessment of exchange rate risk the borrowers are exposed to.

As a result of the above-mentioned phenomena characteristic of the credit market, a role of the retail segment has been more and more dominant in the structure of receivables from the non-financial sector. At the same time, this tendency contributes to the improvement of the quality of the whole loan portfolio<sup>2</sup>. The increasing potential of retail banking growth results in its higher and higher importance as a source of banks' income against a role of the corporate segment.

As regards deposits, the banks' situation is a derivative of two factors: a gradually increasing purchasing power of citizens (a result of the decrease in the unemployment rate in the second half of the year and rising wages and salaries) and good financial standing of enterprises accompanied with the absence of growth in investments. As a result, in the first half of the year, the drop in household deposits was halted and, towards the end of December 2005, they grew again (5.4% y/y). On the other hand, business entities were the source of net resources for the banking sector for the second successive year<sup>3</sup>.

Declining deposit spreads and alternative forms of investing savings supported a trend of relocating financial assets of households to increase their liquidity<sup>4</sup> and rate of return. Shares of investment funds were among the most popular groups of products dedicated to households. An annual change of the

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<sup>1</sup> According to preliminary data of General Inspectorate of Banking Supervision (GINB), net profit of the commercial banking sector improved in 2005 to PLN 8.69 bn from PLN 6.82 bn recorded in the previous year.

<sup>2</sup> According to NBP data, non-performing loans ratio (understood as a share of non-performing loans in total gross receivables from domestic sectors) at the end of 2005 amounted to 10.4% against 14% recorded in the previous year.

<sup>3</sup> According to NBP data, annual change in loan receivables amounted to PLN +1.7 bn, and PLN +19.3 bn for deposits.

<sup>4</sup> According to NBP data, over 80% of the growth in deposits volume was financed with current resources.

volumes of investment funds assets (over PLN 23 billion) was twice as high as the growth in household deposits in this period.

Assuming that the Polish economy is growing, the perspectives for the banking sector development are constructive. First and foremost, further growth in the volumes of mortgage loans and consumer (retail) loans is expected what, in turn, should be reflected in the development of distribution network. It seems that neither so called 'anti-usury act' nor contemplated restrictions on extending loans in foreign currencies will arrest the development of both markets.

In terms of liabilities, we expect that the deposit base will still compete with interest-free saving and investment products.

## **2.3. Risk management**

The aim of risk management is to optimize the financial result and, at the same time, to limit and diversify the operating risk. The Bank's supervisory bodies, explicitly the Supervisory Board and Management Board, are crucial in the risk management process. The Bank's Supervisory Board, through the Audit Committee, is notified of the most important decisions and approves the measures taken by the Management Board in this respect.

Particular risks are dealt with directly by specialized Committees:

- Credit Risk Committee – supervises the credit risk management process;
- Assets and Liabilities Management Committee – responsible for the management of market risk in banking portfolio as well as the management of the Bank's structural liquidity;
- Financial Markets Committee – supervises market risk in the Bank's trading portfolio;
- Operating Risk Committee – supervises implementation of the operating risk management process.

Members of the Management Board supervise works of the above committees; there are at least two Board members in each committee. The Risk Management Department, reporting directly to the President of the Bank's Management Board, is involved in the measurement and monitoring of all types of risks in Kredyt Bank. It is the only unit reporting all risk-related issues, fully independent of business units. In the process of risk identification, measurement and management, the Bank applies techniques relevant to a given type of risk.

## **Hedge accounting**

As at 31.12.2005, the Group applied hedge accounting of fair value to hedge specific assets against interest rate risk resulting from the Group's investing activities. Hedge accounting issues have been described in detail in the description of accounting principles applied by the Group and in Notes.

### 2.3.1. Credit risk

#### Credit policy

Kredyt Bank S.A. Capital Group follows a prudent credit risk policy. The basic aim is to establish a safe credit portfolio with a minimum share of doubtful receivables. The primary assumptions of the credit policy are as follows:

- clear-cut division of sale and credit risk management functions;
- risk diversification through a decrease in receivables concentration;
- limited financing of higher-risk business activities;
- monitoring and early identification of hazards;
- centralization of decision-making powers in the credit process and in the process of the management of non-performing loans portfolio.

New guidelines were developed for corporate customers which stipulate:

- general assumptions related to transaction financing;
- preferences regarding concentration of credit exposure in single borrowers and/or borrowers' group, indicating obligatory concentration limits;
- direction of actions related to certain groups of industries and exclusion of financing for enterprises in certain industries;
- preferences and exclusions regarding the extension of working capital loans, investment loans and guarantees;
- general rules concerning the application of financial and non-financial clauses.

#### Credit risk management

The Bank's credit risk is defined as the risk of non-payment of amounts due if a borrower, guarantor, reinsurer, contractor or issuer loses its creditworthiness. Credit risk is managed taking into account the credit risk aspect corresponding to individual transactions and from the portfolio perspective. The process of centralization of the risk assessment and management both at the Bank, in Żagiel and in Kredyt Lease ended in 2005. The Bank developed and implemented rules of identifying evidence of and testing impairment according to IAS 39.

The risk management process for individual transactions entails risk assessment of such a transaction and, depending on its level, the application of appropriate decision-making process.

The portfolio risk management is the responsibility of the Bank's Management Board and the Credit Risk Committee, where the Credit Risk Committee is responsible for the following:

- acceptance and substantial supervision over credit risk measurement methods;
- recommending, to the Bank's Management Board and the Supervisory Board, admissible level of credit risk in the Bank's and subsidiaries' balance sheets;
- expressing its opinion on the credit process organization;

- expressing its opinion on the Bank's credit policy, making impairment charges and the valuation of hedges;
- expressing its opinion on the limits of decision-making powers in the credit process;
- expressing opinions on internal credit limits;
- changing risk limits and approving limit exceeds within the powers of the Bank's Management Board;
- approval of new products in terms of credit risk;
- substantial supervision over the programme of the Bank's adjustment to the requirements of the New Capital Accord on credit risk.

The Bank, in order to satisfy the requirements of the New Capital Accord (Basel II) in the area of credit risk, implemented the Programme on Quantitative Assessment of Credit Risk - QCR (Quantitative Credit Risk) Programme, under which the Bank:

- develops and implements credit risk measurement models;
- develops and implements databases and tools facilitating collection of data for the purposes of models development and testing;
- reorganizes the credit process taking into account the established level of risk;
- develops and implements RAROC concept (the system of calculating effectiveness of cooperation with a customer at various levels).

The Bank created an online central credit database - CMT (Credit Management Tool) - an obligatory credit rating tool. It entails all enterprises keeping accounts under the Accounting Act and includes:

- risk measurement model - PD (Probability of Default),
- data on customers' financial standing and risk assessment sheet;
- electronic monitoring reports containing information on customers' receivables,
- 'Ryzyko Grupy' [Group's Risk] application with information on groups of customers related in organizational and equity terms.

Implementation of the new risk assessment and credit rating tools was accompanied with further improvement of the credit process, which was supported, among others, by:

- changes in decision-making powers;
- detailing, in one manual, the rules of extending loans to entrepreneurs, including, among others, the documentation required from a customer, credit rating rules, division of employees' responsibilities at particular stages of the credit process, what allowed for the elimination of any possible irregularities in the functional division between the areas of credit products sale, credit rating and decision making as well as administration and credit documentation.

In the individual customers group, creditworthiness and risk group are determined in the scoring system. In 2005, the Bank implemented its own risk scoring sheet both for the Bank's customers and the customers of Żagiel S.A. A behavioral base was also created; it includes all individual and

corporate customers who keep simplified accounts. In order to take advantage of the information on customers' behavior, the Bank has also developed a quasi-behavioural scoring model according to which behavioural risk groups will be determined; they are an additional element of the credit rating process.

### **Number and value of executory titles and the value of collateral established on customers' accounts and assets**

In the course of the Bank's restructuring process, debt recovery and restructuring functions were merged to create the non-performing loans division. In 2005, in the course of debt recovery actions aimed at non-paying customers, the Bank issued 22,448 banking executory titles for the total amount of PLN 186.9 million.

In the case of receivables for which impairment was identified, the total value of loan collateral approved by the Bank as at 31.12.2005 amounted to PLN 1,088,670 thousand. As at 31.12.2004, this value was equal to PLN 1,499,036 thousand.

### **2.3.2. Liquidity risk**

Liquidity risk results from the mismatch of assets and liabilities in terms of maturity dates, which is a natural effect of varied customers' requirements as regards deposits and loans. Maintenance of financial liquidity, understood as an ability to meet financial obligations in a timely manner, is the crucial element of the policy on assets and liabilities management applied by the Bank. The current liquidity is maintained by correcting an excess or shortage of liquid resources with operations conducted on the inter-bank money market. The Bank's safety is fully ensured by the maintenance of liquid reserves as well as the proper term and quality structure of the whole balance sheet. Liquidity risk management decisions are taken by the Bank's Assets and Liabilities Management Committee. The Risk Management Department measures and monitors strategic (long-term) liquidity. The current and operating tasks are performed by the Treasury Department.

Kredyt Bank hedges the liquidity risk by:

- maintenance of an appropriate level of cash, taking into account the volume of statutory provisions;
- maintenance of liquid securities (government bonds) portfolio, properly hedging the term structure of the Bank's liabilities without specific maturity dates;
- performing transactions on derivatives;
- establishment and monitoring of the observance of corporate prudence standards related to liquidity (liquidity gap analysis, assessment of the deposit base stability, internal liquidity limits);
- maintenance of a diversified portfolio of deposits as regards terms and customers;
- monitoring the mismatch of the maturity dates of assets and liabilities, what makes it possible to forecast the demand for liquid assets and avoid excessive concentration of cash disbursements on a close date;
- access to the inter-bank market and open market transactions;

- access to the lombard loan.

Support of KBC Group, the strategic investor, in the case of any potential emergency situation is a crucial factor affecting safety of Kredyt Bank's operations.

### **2.3.3. Market risk**

Market risk is defined as a degree of the hazard to the Bank's financial standing resulting from adverse changes in interest rates, exchange rates and prices of shares and their market volatility. It is identified, measured and monitored by the Risk Management Department.

The interest rate and exchange rate risk are the two main risks identified at the Bank. The Bank does not actively operate on the shares market and the majority of investments in stocks are long-term investments or strategic investments in subsidiaries. The Bank does not trade on the commodity markets.

In order to improve management quality, since 2002, activities of the Bank have been divided into two parts: trading book and banking book. Due to different nature of open positions, the risk is monitored in each book separately.

The trading book is a separated part of the Bank's portfolio, where the Bank intends to generate income resulting from short-term changes of prices, interest rates, exchange rates or other market parameters. The banking book covers operations not covered by trading portfolio, i.e. commercial activities of branches, credit intermediaries and portfolios of securities hedging the liquidity and constant interest income. The banking book aims at the elimination of the market risk.

Value at Risk (VaR) is the basic measure in the monitoring of interest rate risk and the currency risk as well as for the determination of limits in the trading portfolio. Additionally, the level of interest rate risk is monitored and limited (by establishment of limits) with the application of BPV (basis point value). The 'value at risk' method is supplemented by stress-testing which is the amount of a possible loss in extremely adverse (critical), but probable changes in exchange rates.

An interest rate gap prepared separately for each currency is the basic measurement and risk-limiting tool in the banking portfolio. The sensitivity of the valuation of assets and liabilities (BPV), duration and accumulated gap ratios are calculated on that basis. The analysis of interest rate gap applied in the interest rate risk management of the banking book is based on information on particular items of the balance sheet of Kredyt Bank S.A. as well as off-balance items sensitive to changes of interest rates. The Bank's exposure to interest rate risk is marginal.

Currency risk covers currency exchange operations and measurement of open currency positions resulting from the difference between the value of assets and liabilities in a given currency. Foreign exchange transactions performed by the Bank are marginal; the majority of them are performed by customers. The Bank does not pursue speculative activity. The options on the inter-bank market are the options hedging the position resulting from transactions with customers. The risk in the portfolio of foreign exchange option transactions is marginal. Currency position is managed in the trading book. The currency risk at Kredyt Bank is perceived not only as the risk occurring for open currency position, but also as the risk of a change in the value of certain products as a result of changes in exchange rates, particularly in the case of loans expressed in foreign currencies. In order to reduce the credit risk in the case of the growing exchange rates, loan agreements for institutional customers contain clauses on establishment of additional collateral or permit to translate the loan, when the customer does not



generate income in the loan currency. In order to hedge a customer's exchange rate risk they are exposed to, they are offered derivatives (forwards, options).

#### **Average interest rates in Kredyt Bank S.A. in 2005**

Floating interest rate facilities as at 31.12.2005 accounted for ca. 80% of receivables. As at 31.12.2005, average effective interest rates of loan receivables were as follows (by main currencies):

in CHF – 4.1%

in EUR – 4.7%

in PLN – 9.6%

in USD – 6.6%

As at 31.12.2005, 92% of customers' deposits were current accounts and other fixed interest rate products, whose maturity dates, as at the balance sheet date, did not exceed 6 months. As at 31.12.2005, average effective interest rates of customer deposits were as follows (by main currencies):

in EUR – 1.4%

in GBP – 2.3%

in PLN – 2.8%

in USD – 1.8%

#### **2.3.4. Operating risk**

In 2005, the Bank continued preparations for the implementation of the project on measurement and monitoring of this type of risk under so called 'standard method' defined by the Basel Committee. The Operating Risk Committee is responsible for supervision over this process. Business units comprising, among others, employees acting as operating risk coordinators are in charge of the current operating risk management in processes supporting completion of the Bank's strategic targets.

An action allowing for the application of a standard method for establishment of capital requirements was taken. A database including information facilitating the quality assessment of the most frequent events and statistical material for quantitative measurement of operating risk has been created. At the same time, the Bank conducts piloting operating risk self-assessment processes, recognizes the risks inherent in business processes and processes supporting the business activities which may generate substantial operating risk for the Bank.

#### **2.4. Events and contracts material for the Group's operation in 2005**

The following events and contracts were material for the Group's operations in 2005:

- On 18.01.2005, KB S.A. disposed of its whole stake in Wolny Obszar Gospodarczy S.A., i.e. 49.95% share in the capital and votes at the General Meeting of Shareholders of the company to Hutchison Ports Poland (a subsidiary of Hutchison Whampoa Limited). The shares were

sold for PLN 11,132 thousand against PLN 10,346 thousand of the book value of shares held by KB S.A.

- A conditional contract of the sale of an organized portion of the enterprise in the form of IDM S.A. to KBC Securities N.V., Brussels was signed on 18.02.2005 and performed on 31.03.2005. The value of the transaction added up to PLN 10,922.3 thousand and was neutral for the Bank's results. Brokerage activities, so far performed by IDM KB S.A., will be continued and developed in the Polish branch of KBC Securities.
- On 07.01.2005, Kredyt International Finance BV, the Netherlands, a wholly-owned subsidiary of Kredyt Bank S.A. repaid 83.3% (EUR 150 million) of the loan granted in October 2002 by KBC Bank NV Dublin Branch, before due date. As a result of the transaction, Kredyt Bank S.A. decreased the amount of the guarantee securing the loan.
- On 13.04.2005, Kredyt Bank S.A. and Clif S.A. settled all disputes between them out of court. The compromise resulted in mutual expiry of claims. The termination of the dispute has had a positive impact on financial results of Kredyt Bank S.A.
- On 20.04.2005, the District Court for the capital city of Warsaw registered a merger of the following companies: Towarzystwo Funduszy Inwestycyjnych Kredyt Bank S.A. (TFI KB), WARTA Asset Management S.A. (WARTA AM), WARTA Towarzystwo Funduszy Inwestycyjnych S.A. (WARTA TFI). As a result, KBC Towarzystwo Funduszy Inwestycyjnych S.A. (KBC TFI) was established. The company's shareholders were: Kredyt Trade Sp. z o.o., a subsidiary of Kredyt Bank S.A., and TUIR 'WARTA' S.A. holding 39.6% and 60.4% of the share in capital and votes respectively. On 25.07.2005, Kredyt Trade Sp. z o.o. sold, to KBC Asset Management N.V., 2,422,605 shares of KBC TFI and, as a result of the transaction, it holds 30.0% share in capital and votes at the General Meeting of Shareholders of the company.
- On 25.04.2005, under the decision of the General Meeting of KB S.A.'s Shareholders, retained loss disclosed in the financial statement for 2004 of PLN 588.9 million was covered from the supplementary capital (PLN 350.9 million), net profit for 2004 (PLN 185.2 million) and from the general risk fund (PLN 52.8 million).
- On 28.04.2005, Kredyt Bank S.A. disposed of 28,545 (82.32%) shares in Solaris Bus and Coach Sp. z o. o., a subsidiary of Kredyt Bank S.A., to Openaco Trading CO, Limited, Nicosia (Cyprus). The total value of sold shares amounted to PLN 54,238.9 thousand. The book value of disposed shares amounted to PLN 51,254.9 thousand.
- On 01.07.2005, the Management Board of KB S.A. informed that KB S.A. had acquired, under a contract, from Centralny Fundusz Inwestycyjny Sp. z o.o., 15,300 shares of Korporacja Budowlana Inwestycje Sp. z o.o. They account for 40.37% of share in the capital and votes of the Company's General Meeting of Shareholders. The total value of acquired shares amounted to PLN 95 thousand.
- On 07.07.2005, KIF BV, the Netherlands, a wholly-owned subsidiary of Kredyt Bank S.A. repaid the remaining portion (EUR 30 million) of the total loan of EUR 180 million granted in October 2002 by KBC Bank NV Dublin Branch, before due date. At the same time, KIF BV repaid the total loan of CHF 200 million granted in October 2002 by KBC Bank NV Dublin

Branch, before due date. As a result of the above transactions, KB S.A. guarantees securing the repaid loans expired. The transaction value was PLN 654,805 thousand.

- On 14.07.2005, Kredyt Bank S.A. concluded with KBC Bank NV Dublin Branch two loan agreements on market terms with a five-year maturity amounting to EUR 150 million and CHF 150 million. Cash obtained under the above loans was used to finance the Bank's current operations. Contract value: PLN 1,022,790 thousand.
- On 18.08.2005, Kredyt Bank S.A. sold to Gdańska Stocznia Remontowa S.A. its all shares in Stocznia Północna S.A. (27.17% share in the capital and votes at the General Meeting of Shareholders). The selling price was: PLN 12,172.9 thousand. This transaction exerted a neutral impact upon the results of Kredyt Bank S.A.
- On 24.10.2005, the District Court for the capital city of Warsaw registered an increase in the share capital of Kredyt Lease S.A. Following the registration, the company's share capital increased to PLN 27,501 thousand. KB S.A. holds 99.98%, and Kredyt Trade Sp. z o. o. (a subsidiary of KB S.A) holds 0.02% share in the capital and votes at the General Meeting of Shareholders.
- On 22.12.2005, a syndicated loan agreement was signed with a company operating in the fuels and chemicals industry. It is composed of two tranches: Tranche A – EUR 250 million (PLN 958,325 thousand) and Tranche B – EUR 750 million (PLN 2,874.9 thousand). The share of KB S.A. in the said Tranches is EUR 22.7 million (PLN 87,120.5 thousand) and EUR 68.2 million (PLN 261,361.4 thousand) respectively. The margin depends on the Borrower's selected financial ratio. The claim under the loan was not secured.

### **Major post-balance sheet events**

On 17.01.2006, Kredyt Bank S.A. repaid a subordinated loan extended under the agreement of 28.04.2000 with KBC Bank, Dublin Branch and Banco Espirito Santo for the amount of USD 50,000 thousand.

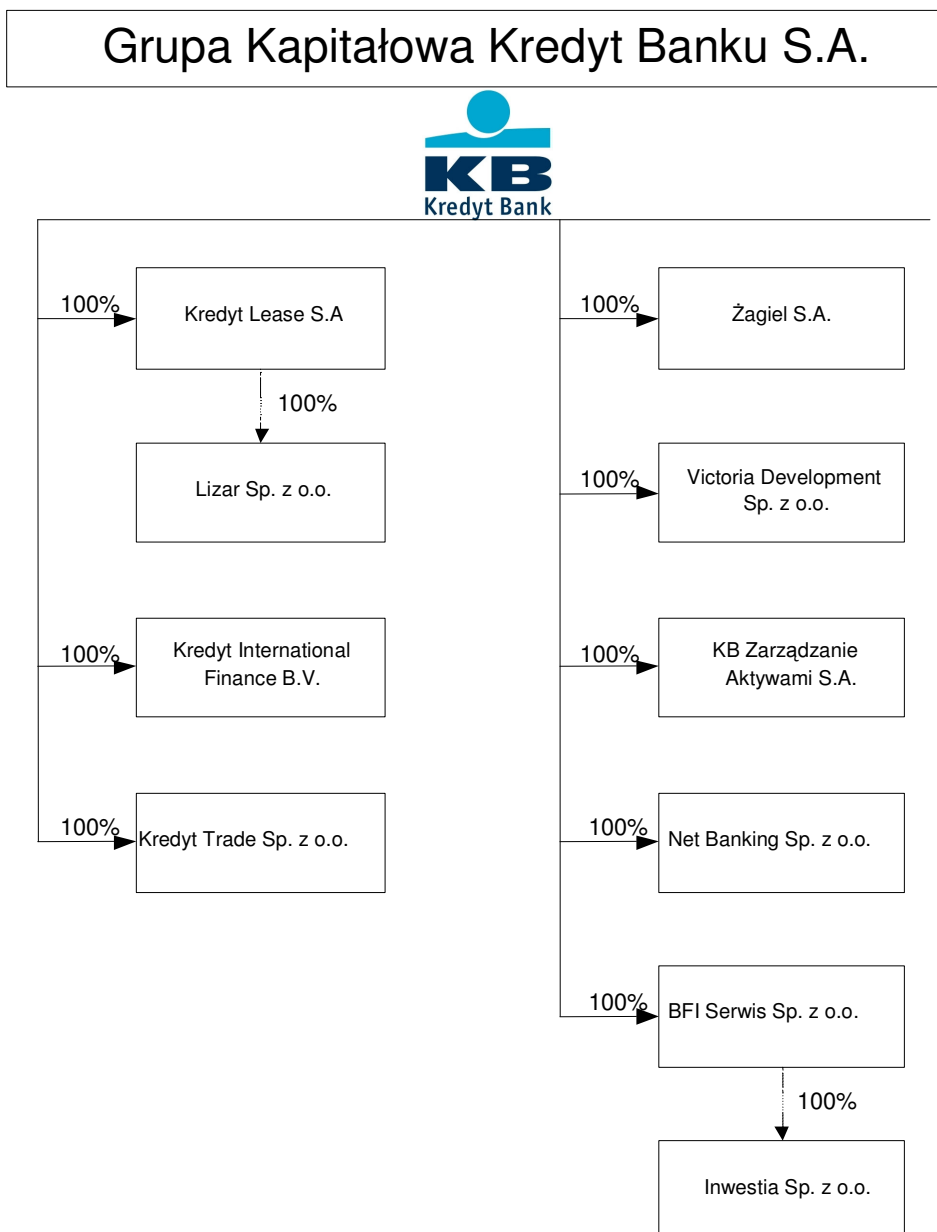
### **Contracts entered into by the Issuer with an entity authorized to audit financial statements**

On 26.07.2005, the Bank entered into an agreement with Ernst&Young Audit Sp. z o.o. in Warsaw, an entity authorized to audit financial statements, on the review of the individual and consolidated half-year financial statement of the Bank and of the Group and the audit and review of the individual and consolidated annual financial statement for 2005. The total remuneration under this agreement amounted to PLN 1,407 thousand net (compared to PLN 1,352.4 thousand in 2004). The remaining, total remuneration under agreements with an entity authorized to audit financial statements, due or paid on accounts other than audit or review, in 2005 amounted to PLN 995 thousand (PLN 110 thousand in 2004).

### 3. The Group's organization and capital relations

#### 3.1. The Group's structure and description

Kredyt Bank S.A. Capital Group is composed of legally separated business entities, whose operations are closely coordinated. The capital relations linking the Group are supported by trading relations, contracts, a common product offer, the Bank's control over the companies' operating and financial



policy and transfer of management staff and know-how. In 2005, the Group continued the restructuring process aimed at adjustment of its composition to the new business model, achievement of the synergy effect through the cooperation within KBC Group and improvement of control over the operations of subsidiaries. The Group's composition and ownership structure as at 31.12.2005 was as follows:

## **Consolidated and non-consolidated companies**

As a result of the adoption of IFRS, the Group determines materiality criteria according to the methodology adopted by the Bank's Major Shareholder.

As at 31.12.2005, the following companies were consolidated: Kredyt Lease S.A., Kredyt International Finance B.V, Kredyt Trade Sp. z o. o., Żagiel S.A. and Victoria Development Sp. z o. o.

Due to the immateriality of their operations and financial figures, the Group fails to consolidate financial statements of the following entities: Lizar Sp. z o.o., KB Zarządzanie Aktywami S.A., Net Banking Sp. z o.o., BFI Serwis Sp. z o.o., Inwestia Sp. z o.o.

Shares held by the Group in the above-mentioned companies are classified as assets held for sale and recognized at cost less any possible impairment charges.

Furthermore, the Group holds controlling interests in Dolwis S.A. and Korporacja Budowlana Inwestycje Sp. z o.o., however, it neither exerts actual control over nor any significant influence upon their financial and operating activities. Hence, they are not members of the Group and are not consolidated. The investments in the shares of these companies were classified to the portfolio of available-for-sale assets and are measured at cost less any possible impairment.

## **Changes in the Group's organization**

In 2005, the restructuring process of Kredyt Bank S.A. Group continued; it was aimed at the reduction of risk by focusing on activities supplementary to the services provided by the Bank to customers, taking advantage of the synergy effect within KBC Group and optimization of the supporting function in KB Group. As compared to the Group's 2004 consolidated financial report, the organization of Kredyt Bank S.A. Capital Group changed as follows:

- On 25.04.2005, as a result of the merger of: Towarzystwo Funduszy Inwestycyjnych Kredyt Bank S.A., WARTA Asset Management S.A. and WARTA Towarzystwo Funduszy Inwestycyjnych S.A., a new company – KBC Towarzystwo Funduszy Inwestycyjnych S.A. (KBC TFI) – was registered, in which Kredyt Trade Sp. z o.o. held 39.6 % of share in capital and votes at the General Meeting of Shareholders of the company. On 25.07.2005, Kredyt Trade Sp. z o.o. sold, to KBC Asset Management N.V., 2,422,605 shares of KBC TFI and, as a result of the transaction, it holds 30.0% share in capital and votes at the General Meeting of Shareholders of the company.
- On 22.12.2005, the Extraordinary General Meeting of Shareholders of PTE Kredyt Bank S.A. approved the company's winding-up report and on 23.12.2005 the financial statement was submitted, along with the resolution of the Extraordinary General Meeting of Shareholders, to the Registry Court for the capital city of Warsaw, with a request to delete PTE Kredyt Bank S.A. from the National Court Register.

## **3.2. Investment plans, including capital investments**

One of the basic objectives of the Group's strategy is to increase its share in the Polish financial services market. Capital investments in entities of the financial sector create potential opportunities for the accomplishment of such goals.

In each such potential case, undertaken measures comply with the law and are analyzed in terms of economic and organizational conditions.

According to the Group's development strategy, adoption of the model of universal banking and insurance group is the best method to attain a significant position on the Polish financial market. It means that the Bank will focus on areas of business other than investment banking.

As at 31.12.2005, capital investments made outside the Group were mainly investments in shares of such companies as KIR S.A., BIK S.A., G.P.W. S.A., SWIFT and shares taken in the debt recovery and restructuring process. As at 31.12.2005, their share in the Group's balance sheet was immaterial.

A detailed list of the Bank's capital investments has been presented in Note 29

### 3.3. Shareholding structure of the Group's parent company

As at 31.12.2005, the Bank's share capital totaled PLN 1,358,294,400 and was divided into 271,658,880 shares with the nominal value of PLN 5.00 each. The Bank's shares are registered shares and bearer shares; they are not preference shares and each share entitles its holder to one vote at the Bank's General Meeting of Shareholders. All Bank's shares are admitted to public trading. The share capital did not change in 2005.

As at 31.12.2005, KBC Bank NV was the only shareholder holding over 5% of votes at GMS.

Shareholder	Line of business	Number of shares/votes at the GMS	Share in votes and share capital (%)
KBC Bank NV*	Banking	232,341,875	85.53%

\*/ By the Resolution of the Commission for Banking Supervision No. 81/KNB/81 of 17 September 2001, KBC Bank N.V. is entitled to exercise no more than 75% of votes at the General Meeting of Shareholders of Kredyt Bank S.A.

The Bank's Management Board is not aware of any contracts under which the proportion of shares held by existing shareholders may change in the future.

### 3.4. Authorities of the Group's parent company

The Bank's Management Board runs the Bank's business and represents it outside. The President of the Bank's Management Board is appointed and dismissed by the Supervisory Board. Vice-Presidents and Members of the Management Board are appointed and dismissed on a motion of the President of the Management Board or upon his/her approval by the Supervisory Board accounting for requirements defined in the Banking Law regulations.

On 09.02.2005, the Supervisory Board of Kredyt Bank S.A. appointed, as of 01.03.2005, Mr. Ronald Richardson for the position of the Vice President of the Bank's Management Board. On 08.06.2005, the Commission for Banking Supervision expressed its consent to the appointment of Mr. Ronald Richardson for the position of the President of the Management Board of Kredyt Bank S.A. Under the

resolution of the Supervisory Board of 31.03.2005, since the date of the approval, Mr. Ronald Richardson has been performing the function of the President of the Bank's Management Board.

Ms. Małgorzata Kroker-Jachiewicz, the previous President of the Bank's Management Board, remained in the Board as its Vice President. Additionally, on 09.02.2005, the Supervisory Board of Kredyt Bank S.A. appointed, as of 01.03.2005, Mr. Krzysztof Kokot for the position of the Vice President of the Bank's Management Board. The Supervisory Board also accepted the resignation of Mr. Fedele Di Maggio from the position of the Vice President of the Bank's Management Board. Mr. Fedele Di Maggio was entrusted with other responsibilities in KBC Group.

As at 31.12.2005, the Management Board of Kredyt Bank S.A. was composed of:

Ronald Richardson	- President of the Management Board,
Krzysztof Kokot	- Vice President of the Management Board,
Małgorzata Kroker-Jachiewicz	- Vice President of the Management Board,
Guy Libot	- Vice President of the Management Board,
Bohdan Mierzwiński	- Vice President of the Management Board.

The Supervisory Board exercises a permanent supervision over the Bank's activities in all areas of its operation. The particular duties of the Supervisory Board include assessment of statements with regard to their compliance with books and documents as well as with the factual status and assessment of motions of the Management Board concerning profit distribution or loss coverage. The Supervisory Board is appointed by the General Meeting of Shareholders. On 09.02.2005, due to the resignation by Mr. Dirk Mampaey from his position in the Supervisory Board of Kredyt Bank S.A., Ms. Rita Docx was appointed a member of the Supervisory Board.

As at 31.12.2005, the Supervisory Board of Kredyt Bank S.A. was composed of:

Mr. Andrzej Witkowski	- Chairman of the Supervisory Board,
Mr. André Bergen	- Member of the Supervisory Board,
Ms. Rita Docx	- Member of the Supervisory Board,
Mr. Françoise Florquin	- Member of the Supervisory Board,
Mr. Feliks Kulikowski	- Member of the Supervisory Board,
Mr. Marek Michałowski	- Member of the Supervisory Board,
Mr. Adam Noga	- Member of the Supervisory Board,
Mr. Józef Toczek	- Member of the Supervisory Board,
Mr. Marko Voljć	- Member of the Supervisory Board.

### 3.5. The Bank's and the Group's shares held by members of management and supervisory authorities

A number and nominal value of shares of the Group's parent company and shares in its subsidiaries and associates held by members of the Management Board and members of the Supervisory Board of Kredyt Bank S.A. as at 31.12.2005 have been presented below.

	Shares of Kredyt Bank S.A.		Shares in subsidiaries and associates	
	Number of shares	Nominal value (in '000' PLN)	Number of shares	Nominal value (in '000' PLN)
Members of the Management Board	5 100	25.5	0	0
Ronald Richardson	5 000	25	0	0
Małgorzata Kroker-Jachiewicz	100	0.5	0	0
Members of the Supervisory Board	24 491	122.5	0	0
Andre Bergen	23 491	117.5	0	0
Marek Michałowski	1 000	5.0	0	0

### 3.6. Remuneration of persons managing and supervising the Group's parent company

Detailed information on remuneration of persons managing and supervising the Group's parent company and contracts entered into by the Issuer and managing persons are presented in Note 53 to the consolidated financial statement of Kredyt Bank Group for 2005.

Employment contracts concluded with three members of the Bank's Management Board stipulate payment of a compensation in the case of resignation or dismissal from the office held without any material reason.

One of the contracts includes a clause concerning a severance pay in the amount of 36 average annual salaries from the last 12 months of the employment contract. The two remaining contracts stipulate a severance pay amounting to 24 average annual salaries from the last 12 months of the employment contract.

All the three contracts include a condition clause that a severance pay is not received if the contract has been terminated due to a recall from an office held resulting from:

- Acting to the detriment of the Bank,
- Commission of an obvious crime or an offence ascertained by a valid court sentence,



- Serious damage to the Bank's assets,
- Violation of a non-competition contract,
- Violation of a company secret,
- Gross violation of the Bank's internal regulations or resolutions by its bodies.

Additionally, one of the contracts includes a clause that a severance pay is not received in the case of resignation from the office held.

Furthermore, it should be emphasized that, pursuant to § 27 of the Bank's By-laws, a Member of the Management Board may be recalled by a material reason only.

### 3.7. Related party transactions

Related party transactions are presented in Note 52 of the consolidated financial statement of Kredyt Bank S.A. for 2005.

## 4. The Group's products, services and areas of operation

### 4.1. The Bank's products, services and areas of operation

In order to improve its sales organization and adjust the product offer to market requirements, the Bank separated two major customer segments: a retail segment, including Small Medium Enterprises and a corporate one. The new segmentation is reflected in existing sales structures.

#### 4.1.1. Retail segment

In 2005, the number of retail customers increased by 6%.

<i>in thousands</i>	<b>31.12.2005</b>	<b>31.12.2004</b>
Individual customers	797	752
SMEs	81	76
Total customers	878	828

#### Major product strategy targets in retail banking

During the year 2005 the Bank continued its market expansion. An emphasis was put to strengthen Bank's market position by promotion of new brand (introduced common graphics logo for all KBC Group entities) new and modified products range and development of wide bank assurance product offer in cooperation with KBC Group entities. Simultaneously with the promotion of the new image and the new common product offer, the Bank embarked on a process of standardizing its branch network which are to facilitate customers' access to the products of all cooperating entities in each outlet. Changes of the product offer focused on:

- modification of the product offer for individual customers by making it more attractive and competitive with special emphasis on the 'family' offer;
- dynamic development of the bancassurance offer in cooperation with WARTA Group;
- modifications to Żagiel's offer;
- expanding cooperation with KBC TFI in area of distributing investment fund units.

### Accounts and payments

The Bank improved its basic offer for individual customers: Ekstrakonto savings accounts and credit cards offer. The cooperation with Towarzystwo Ubezpieczeniowe WARTA S.A., a strategic partner, became closer in terms of banc assurance services. The cooperation in this area was highlighted with joint marketing campaigns in autumn 2005.

The main aim of modifying Ekstrakonto account was to develop the most practical offer on the market for the Bank's customers and their families. In May, the Bank launched the most extensive nationwide ATMs network, in which individual customers may take out money from personal accounts free of charge.

In cooperation with WARTA, the Bank offers a wide range of insurance products linked with current account - "Ekstrakonto". The offered product range includes: accident insurance, 'Ekstrapomoc' assistance block in case of various events of fate (car assistance, medical aid, repairs of household appliances and computers). "Razem" is the scheme marketed by the Bank for customers' families providing products offer which allows for reduction of spending on financial products and services.

The number of newly opened current & saving accounts (ROR) as at 31.12.2005 increased by 10% against 31.12.2004.

<i>in '000' PLN</i>	<b>31.12.2005</b>	<b>31.12.2004</b>
<b>ROR</b>		
Volume (in thousands)	508	460
Carrying amount	766 090	683 348

The Bank has also modified offer for Żagiel customers and since 20 October 2005, in cooperation with Żagiel has started issue and servicing of VISA Electron Żagiel Card.

Modification of the product offer for individual customers should result in increase in market share in 2006.

### Investment funds

At 31.12.2005 asset managed by KBC TFI S.A. amounted to PLN 4,9 billion.

The value of assets acquired through the Bank's distribution network amounted to PLN 1,8 billion.

As of the end of 2005, KBC TFI managed 19 investment funds:

- 5 open-end investment funds (KBC Pieniężny FIO, KBC Papierów Dłużnych FIO, KBC Obligacyjny FIO, KBC Stabilny FIO i KBC Aktywny FIO);
- 3 specialist open-end investment funds (ALFA SFIO, BETA SFIO, KBC GAMMA SFIO);
- 1 close-end investment fund investing in foreign investment funds denominated in US Dollars (KBC Dolar FIZ);
- 9 close-end capital guaranteed funds (KB Kapitał Plus FIZ, KB Kapitał Plus II FIZ, KB Kapitał Plus III FIZ, KB Klik Europa FIZ, KB Klik Ameryka FIZ, KBC Złoty Dolar FIZ, KBC Elita FIZ, KBC Index Nieruchomości FIZ, KBC Byki i Niedźwiedzie FIZ);
- 1 specialist close-end investment fund KBC SIGMA SFIZ, being wound-up.

KBC TFI S.A. is the leader on the Polish market of guaranteed capital funds with 93,6% share in this segment. At 31.12.2005, the assets entrusted into those funds amounted to over PLN 912 million. In cooperation with KBC Asset Management N.V., further actions are taken to expand the product offer. The subscription of investment certificates of another capital guaranteed fund will take place in February 2006.

As at 31.12.2005, the companies of KB S.A. Capital Group did not issue, redeem or repay any debt or equity securities.

## Deposits

The deposit offer for individual customers is still being developed. The volumes on the Savings Account, which is one of the basic depositary products, are growing on a regular basis; as at 31.12.2005, the value of deposits amounted to PLN 1,9 billion, i.e. doubled as compared to 31.12.2004. The number of new Accounts increased by 73% as compared to the analogous period in the previous year.

<i>in '000' PLN</i>	<b>31.12.2005</b>	<b>31.12.2004</b>
<b>Saving Accounts</b>		
Volume (in thousands)	160	93
Carrying amount	1 951 041	854 943

In 2005, the Bank launched 3 editions of special purpose 6-month term deposits 'Efektywna', – PLN 41,5 million, 'Wygodna' – PLN 507,4 million, 'Korzystna' – PLN 212,0 million. The sale of these term deposits was supported with promotional campaign. In addition, 3-month 'Constans' term deposit interest rate offered was increased for the period of summer holidays.

## Credit cards

The cooperation with WARTA related to banc assurance allowed for the launch of the common credit card of the bank and insurance company, first of this type on the Polish market. Visa Gold Card is dedicated to customers who are members of the prestigious 'Klub Klienta VIP' [VIP Customer Club] in WARTA. The card is an ID card for the Club members, offers a number of attractive financial attributes (like discounts on other banking products, e.g. Ekstrakonto, mortgage loans) and enables their holders to take advantage of price reductions offered by the Bank's and WARTA's commercial partners. In

result, WARTA customers enjoy greater financial opportunities, and the Bank has gained access to the partner's best customers database.

In the third quarter of 2005, the Bank extended its credit cards offer with two new cards. One of them is targeted at the mass segment (Visa Flag) and, due to the issue of the card, the Bank will be able to increase its share in this segment of the market. Bearing in mind the perspective customer group, special Visa Student card for students was issued; it enables students with higher average grades to obtain higher limits. At present, the Bank offers credit cards dedicated to all customer groups: from basic cards, through Gold-type cards, to the most prestigious Platinum cards.

At 31.12.2005, the number of issued credit cards increased by 75% as compared to figures recorded at 31.12.2004. The volume of credit card transactions is also growing systematically.

<i>in thousands</i>	<b>31.12.2005</b>	<b>31.12.2004</b>
Credit cards	66	38

### Loans and credits

The sale of retail loans through Żagiel distribution network in the four quarters of 2005 remained stable. The total value of new installment and cash loans during 12 months of 2005 amounted nearly to PLN 1.8 billion. At 31.12.2005, the exposure on installment and cash loans granted through Żagiel amounted to PLN 1 423,6 million. At 31.12.2004 it amounted to PLN 1 405,9 million.

Under the cross-selling strategy realized in the co-operation with WARTA S.A., a significant growth in the sale of life insurance policies to customers borrowing installment loans through Żagiel has been noted; compared with previous 12 months, written premium almost doubled.

<i>in '000' PLN</i>	<b>31.12.2005</b>	<b>31.12.2004</b>
<b>Żagiel – installment and cash loans</b>		
Gross portfolio value	1 423 623	1 405 915

In 2005, the sale of mortgage loans almost doubled. In 2005, the Bank granted mortgage loans of PLN 951.5 million as compared to PLN 505.8 million in 2004.

<b>Mortgage loans</b>	<b>31.12.2005</b>	<b>31.12.2004</b>
Portfolio carrying amount*	2 035 351	1 569 314
Share of loans in foreign currencies in the portfolio carrying amount	57%	46%

\* the item contains: amounts due from private persons, individual entrepreneurs, individual farmers

In March and December, the Bank modified its special purpose loan which, from the spring edition on, is called „Błyskawiczny”. The four editions of this product were launched in 2005 and, as compared to 2004 figures, the value of sold loans increased five times.

### Bancassurance

The total gross written premium for life and property insurances of WARTA Group offered by Kredyt Bank increased in 2005 by 43% as compared to 2004.

In 2005, the Bank launched two new saving & investments products (beside the existing Warta Gwarancja Plus) in the form of life insurance policies with investment funds managed by KBC AM, with capital guaranteed and potential profits linked to indexes growth: Warta Klik Światowy, Warta Zysk Azjatycki.

The growth rate of insurance premium at the sale of life insurance to customers purchasing installment loans through Żagiel reached 200%.

### Changes in the offer for SMEs

In March 2005, the offer for SMEs segment was supplemented with a new attractive product – deposit account to invest financial surpluses. For a customer, it means an attractive interest rate combined with full liquidity of resources. By the end of 2005, customers deposited PLN 122.3 million on such accounts.

In April 2005, the ‘Ekstrabiznes’ package was expanded to cover the whole SMEs segment. This attractive offer is addressed to companies with annual net sales of PLN 6 million. The package offers more loan facilities (working capital loan, investment loan, VISA Business Electron card).

In October 2005, the Bank launched a new investment loan: Kredyt Inwestycyjny - Wspólnota Mieszkaniowa. The loan is designated to finance overhauls or modernization of real estates owned by tenants’ associations. The loan is extended in the Polish zloty for the period of eight years.

Simultaneously, new simplified credit rating methods were developed to rate tenants’ associations applying for thermomodernization loans. The credit rating is based on regularity and timely character of payments to the repairs fund.

During 2005, the sale of loans and deposits for SMEs has been growing.

<i>in '000' PLN</i>	<b>31.12.2005</b>	<b>31.12.2004</b>
Loans for SMEs	688 745	528 878
Current accounts for SMEs	1 009 595	875 231

In June 2005, *Rzeczpospolita* daily awarded the Bank with an honourable mention for the best corporate account for active companies, which supports the positive assessment of the pricing policy towards SME customers. During the assessment, independent experts of *Rzeczpospolita* daily granted the maximum score to Ekstrabiznes account which was found to be the most advantageous

account for companies frequently using bank accounts: making transfers, placing standing orders, disbursing cash at banks or in ATMs and paying with cards for purchased goods.

In 2005, the Bank carried out a number of educational programmes for SMEs customers, among others, on EU grants and rules of financing repairs and thermomodernizations for administrators of real estates and building societies.

#### **4.1.2. Corporate segment**

The Bank offers a full range of services for corporate customers, both traditional banking products and treasury products, trade finance and corporate finance. The offer is tailored both to the specific character resulting from the customer's size and the nature of its operations: large corporations, medium-sized enterprises, state-owned entities, social associations and organizations.

The services are provided through 12 Corporate Banking Centres located in the biggest Polish cities. Relationship Managers maintain direct customer relations in case of specialized products; the employees of the organizational units of the Head Office support them.

The Bank offers a full range of traditional loan facilities, such as investment loans, working capital loans in credit or current account, revolving and non-revolving, payment and foreign currency facilities, export financing, payments under own letters of credit, etc. At the same time, customers may also take advantage of other credit-related services, such as factoring, leasing, bank guarantees and sureties, organization of and services related to the issue of debt securities.

Traditional deposit products, including term deposits, current accounts, payment cards, consolidated current accounts (which make it possible to service multi-branch companies and adjust the liquidity management strategy to the specific nature of a company) supplement transaction banking products such as Bulk Payment System (which makes it possible to identify details of payments, their assignment and settlement against respective settlement accounts of debtors in the customer's accounting system) and cash management products, such as closed payments, disbursements in Bank's Branches, other payments to accounts.

In addition, the Bank offers corporate finance facilities, such as consulting on mergers and acquisitions, privatization of state-owned enterprises, capital restructuring and seeking new investors for companies. Within the above tasks, the Bank also provides partial services, such as: complete assessment of investment projects, assistance in preparation of corporate development strategies, company valuations, due diligence, preparing memoranda, business plans and negotiations on the customer's behalf.

All-inclusive servicing of foreign trade constitutes a separate group of services provided by the Bank through:

- a worldwide network of correspondence banks;
- Nostro accounts in foreign banks and Loro accounts opened in our Bank by foreign banks;
- cooperation agreements with global foreign institutions, e.g. European Investment Bank, European Reconstruction and Development Bank, Visa International;
- fast and safe foreign transactions in the SWIFT system.

The Bank offers, among others, transfers in foreign trade, cheques in foreign trade, documentary letters of credit, guarantees in foreign trade, purchase and sale of foreign currencies and forfeiting.

#### **4.1.3. Money and capital markets**

The Bank performs transactions on the inter-bank market, both domestic and international, on own account and on behalf of customers. Active participation in the inter-bank market makes it possible to obtain competitive quotations, what is the basis for stabilization and development of existing corporate customer base.

The treasury products offer is being expanded and ensures appropriate services both to Private Banking customers and medium-sized and large companies.

The Bank is the Treasury Securities Dealer and Money Market Dealer.

#### **4.1.4. Custody services**

Kredyt Bank S.A. holds an authorization of the Polish Securities and Exchange Commission to manage securities accounts; it is also a direct participant of the National Depository for Securities (KDPW) as a Depository and the participant of the Securities Register (RPW) managed by the National Bank of Poland (NBP).

The custodian services of Kredyt Bank S.A. entail managing accounts of securities, hold in KDPW or RPW, for domestic and foreign, both institutional and private customers. For the special group of customers, i.e. investment funds, Kredyt Bank S.A. also plays a role of a depository and transfer agent.

The Bank also deposits securities not traded on organized market, registered in securities registers and on sub-fiduciary accounts in domestic and foreign financial institutions.

The Bank assists customers in the settlement of sale/purchase transactions related to securities traded on the regulated market (including the stock exchange market) and transactions outside the regulated market (including the inter-bank market); it also intermediates in the exercise of rights incorporated in securities, such as dividends, subscription rights, interest, redemptions, splits, new issues, general meetings of shareholders.

#### **4.1.5. Cooperation with international financial institutions**

Kredyt Bank has established active relations with domestic and foreign banks providing services like FX/MM, Custody, Trade Finance and payments. Due to the base of 35,000 SWIFT keys exchanged with other institutions, the Bank is able to exchange correspondence with banks and service foreign trade in the majority of countries worldwide.

Kredyt Bank manages 8 LORO accounts in foreign currencies and 28 LORO accounts in PLN for 31 foreign banks. Kredyt Bank also provides services for 3 domestic banks, and manages 6 LORO accounts for them. The structure of NOSTRO correspondents, optimized in the previous year, did not change. The network of 17 accounts fully satisfies the clearing needs of Kredyt Bank.

#### 4.1.6. Distribution channels

##### Traditional channels

Customers of Kredyt Bank S.A. are serviced through the network of 333 retail units located all over Poland which, as at 31.12.2005, comprised 80 branches, 233 affiliates, 18 banking outlets and 2 agencies. These units provide a full range of services for retail customers and payment services for corporate customers.

The network servicing retail customers is supplemented with 11 private banking units providing services exclusively to this sub-segment of customers.

Corporate customers are serviced (except for payments) in 12 Corporate Banking Centers located in Białystok, Bydgoszcz, Gdańsk, Katowice, Kraków, Lublin, Łódź, Poznań, Rzeszów, Szczecin, Warsaw and Wrocław. An additional center in Warsaw has been established for strategic customers sub-segment.

##### Electronic channels

The KB 24 system provides electronic access to personal accounts (Ekstrakonto) via the Bank's website – [www.kb24.pl](http://www.kb24.pl) and call center – Tele KB.

To ensure high quality services in KB24, in 2005 the Bank migrated KB24 e-banking system and databases of electronic distribution channels to a new operating system. Databases were also upgraded. The application of up-to-date solutions has increased the performance of the internet banking and the speed of transactions. It has affected the quality of transactions concluded in the Internet, through call centers or ATMs. The new IT platform guarantees the top quality of services and the stability of the servers operations. The above system equipment enabled to:

- expand and upgrade the functionality of KB 24, the website and TeleKB call center;
- change the appearance of KB24 website;
- launch a new website: [www.kredybank.pl](http://www.kredybank.pl) and a new release of CMS 2, a website management system.

At the end of 2005, as compared to 2004 year end figures, the number of KB 24 users increased by 29%.

<i>in thousands</i>	<b>31.12.2005</b>	<b>31.12.2004</b>
KB24 users	165	128

Tele KB is a call center for KB24 users, which accepts phone orders and provides technical support for KB24 users. IVR information and transaction service, a part of Tele KB, identifies customers and makes it possible for them to check balances, print out statements of recent transactions without the assistance of Tele KB consultant. In 2005, the center recorded 528 thousand calls.



VideoTel is a system servicing payment orders placed from office or a customer's house via PC with the use of public telephone systems (including cellular phones) or network adapter in the case of VPN-supported permanent telecommunication connection with the Internet.

As at the end of December 2005, VideoTel serviced 7,292 customers, i.e. 4% less than in 2004. The decrease in the number of customers using VideoTel from April 2005 is a result of the migration of customers using VideoTel system to the KB24 system and remains in accordance with the Bank's assumptions.

#### ATMs

In 2005, considering the fact that the purchase of new equipment and organic network development is a time- and money-consuming process, the Bank signed respective agreements with independent operators and banks to establish 'Twoją Sieć' network. Kredyt Bank customers were offered free cash disbursements in ca. 1,900 ATMs located in the whole territory of Poland.

At the end of 2004, Kredyt Bank offered a network of 493 ATMs, in which Kredyt Bank customers could withdraw money free of charge.

## 4.2. Operations of the Group companies

### Żagiel S.A.

As at 31 December 2005, the share capital of Żagiel S.A. amounted to PLN 23,964 thousand.

Kredyt Bank launched cooperation with Żagiel in 1995. Żagiel S.A. intermediates in the sale of installment loans as well as in the distribution of selected services offered by the Bank and WARTA S.A. The company offers consumer loans, mortgage loans and mortgage cash loans for individuals, leasing, EKSTRABIZNES and EKSTRAKONTO accounts and the issue and servicing of VISA Electron Żagiel card. Within the cooperation with WARTA S.A., Żagiel offers life insurance policies to customers buying installment loans.

Over the years, the company has built up a strong and stable position on the retail sale market. Żagiel is ranked third on the intermediation market in Poland. In 2005, Żagiel S.A. extended loans with the total value of ca. PLN 1.8 billion. Retail loans sold via this company are one of the Bank's most yield-generating assets.

In 2005, a modified process of considering loan applications placed by individual customers was implemented, which made it possible to reduce the time needed to service borrowers. In the case of special purpose cash loans, a credit decision may be taken almost immediately ('Kredyt Błyskawiczny' – 'Flash Loan'), and in the case of mortgage loans, the Bank takes decisions within 48 hours.

Żagiel S.A. was honoured with a few awards and prizes. The company was awarded with the *Most Popular Brand in Lublin* title in 2005 in a vote organized in this region by *Gazeta Wyborcza* daily, Radio Lublin and TVP 3; in the ranking 'Golden Top 100' published by *Kurier Lubelski* daily, Żagiel S.A. was ranked first in terms of profitability; in an annual contest held by *Gazeta Wyborcza Lublin* daily, the company was awarded, for the third time after 2002 and 2003, with 'A Golden Key to Success with one diamond' title in the category of large enterprises; in the contest organized by the Regional Chamber of Commerce in Lublin, the company was awarded a special mention and a title of 'The 2005 Provincial Business Leader'.

### **Kredyt Lease S.A.**

Under the resolution of the General Meeting of Shareholders of 21.07.2005, the company's share capital was increased to PLN 15,000 thousand through the issue of shares. As at 31.12.2005, the company's share capital amounted to PLN 27,501 thousand.

Kredyt Lease is engaged in leasing services, rental and lease of rights and assets, trade in real estate and intermediation in the sale of goods and services. The company focuses mainly on services provided to the Bank, but also offers its services on the market.

In 2005, the company underwent reorganization of the sales and organizational structures. Kredyt Lease's offer is supplementary to the Bank's offer and provides a full range of services for corporate customers and SMEs.

### **Kredyt Trade Sp. z o.o.**

As at 31.12.2005, the share capital of the company amounted to PLN 27,500 thousand.

The company is engaged in intermediary services in real estate trading, substitutive investments, property and technical facility management and administration, as well as consulting services and preparation of economic and financial expert reports, drafting business plans, appraising company value, and holding and conducting training programs.

### **Kredyt International Finance B.V.**

As at 31.12.2005, the share capital of Kredyt International Finance B.V. (KIF) amounted to EUR 18 thousand.

The company was registered on 14.02.2001 to perform and handle the issue of bonds in EUR on foreign markets. KIF B.V. is also involved in sourcing of financial resources for Kredyt Bank S.A. Capital Group on foreign markets.

In 2001, the Company performed abroad a public issue of eurobonds with a 3-year redemption period. The bonds worth EUR 150 million were redeemed on 29.03.2004.

In 2002, the company entered into three loan agreements with KBC Bank NV Dublin Branch, guaranteed by Kredyt Bank S.A. On 07.01.2005, KIF B.V. repaid, before due date, the portion of the loan of EUR 150 million out of the total loan amount of EUR 180 million. KIF B.V. repaid the remaining portion, i.e. EUR 30 million, and the total loan of CHF 200 million on 07.07.2005.

As at 31.12.2005, the companies described below did not operate or were not active.

### **BFI Serwis Sp. z o.o.**

As at 31.12.2005, the share capital of the company amounted to PLN 19,250 thousand. The company is mainly involved in providing financial intermediation and consulting services.

### **Net Banking Sp. z o.o.**

As at 31.12.2005, the share capital of the company amounted to PLN 1,425 thousand. The Company's objects are: software, data processing and activities related to databases as well as the sale of services related to hardware and telecommunication equipment.

### **Victoria Development Sp. z o.o.**

As at 31.12.2005, the share capital of the company amounted to PLN 6,466 thousand. The objects of Victoria Development Sp. z o.o. was servicing the Bank's Head Office with regard to real estate construction, operation and administration. In December 2004, the company disposed of the building in ul. Giełdowa 7/9.

### **KB Zarządzania Aktywami S.A.**

As at 31.12.2005, the share capital of the company amounted to PLN 15,012 thousand. The company's objects are the management of the customer assets upon order and brokerage activities.

### **Inwestia Sp. z o.o.**

As at 31 December 2005, the share capital of the company amounted to PLN 1,751 thousand. The company is involved in providing financial intermediation services (except for granting loans), performing transactions on financial markets upon order and financial consulting.

### **Lizar Sp. z o.o.**

As at 31.12.2005, the share capital of the company amounted to PLN 50 thousand. The company is involved in the lease, rental and leasing of real estate.

## **5. The Group's financial results in 2005**

### **5.1. Income statement structure**

The Group's profit before tax in 2005 amounted to PLN 321,368 thousand as compared to PLN 178,774 thousand in 2004. The Group's net profit in 2005 amounted to PLN 415,878 thousand. The following factors contributed to the material improvement of the financial result as compared to 2004:

- growing business activity as observed over the last months of 2005, following profound restructuring processes in 2004 and in the first six months of 2005 reflected in, among others, an increase in the sale of installment and mortgage loans, the sale of insurance policies and shares of investment funds;
- regular mitigation of credit risk supported by efficient restructuring and debt recovery activities;
- improved quality of working assets;
- effective management of the Group's operating expenses.

The main items from the income statement, in comparable periods, are presented below:

### Income

in '000' PLN	01.01.2005 - 31.12.2005	01.01.2004 - 31.12.2004
Net interest income	753 447	633 927
Net fee and commission income	314 890	513 641
Net trading income and profit from investment activity (including dividend income)	140 538	182 945
Result on other operating income/expenses	11 238	49 098
<b>Total income</b>	<b>1 220 113</b>	<b>1 379 611</b>

### Expenses

in '000' PLN	01.01.2005 - 31.12.2005	01.01.2004 - 31.12.2004
General and administrative expenses and depreciation	-890 825	-1 055 175
Net impairment charges for loan receivables and other assets	-9 167	-145 663
<b>Total expenses</b>	<b>-899 992</b>	<b>-1 200 838</b>

### Tax

in '000' PLN	01.01.2005 - 31.12.2005	01.01.2004 - 31.12.2004
Income tax expense	93 536	-20 032

### Net profit

in '000' PLN	01.01.2005 - 31.12.2005	01.01.2004 - 31.12.2004
Net profit	415 878	156 840

Net interest income generated by the Group in 2005 amounted to PLN 753,447 thousand and was higher by 18.9% than the level recorded for 2004. Such figure was a result of, among others, an increase in the share of working assets in the balance sheet as observed over the last few months and the volatile structure of loan receivables portfolio with a growing share of amounts due from individuals. The increasing interest income is a result of, among others, an effective restructuring and debt recovery activities concerning the impaired receivables portfolio.

Net fee and commission income amounted to PLN 314,890 thousand and was lower by 38.7% in comparison with last year's figures. The lower net fee and commission income is a consequence of adopting by the Group (from 01.01.2005 on) the methodology of effective interest rate to measure financial assets and liabilities recognized at amortised cost without the restatement of comparable

data, what is in line with IFRS 1. The fees and commissions received in cash are withdrawn from the fee and commission income and amortized with the effective interest rate of contracts and classified as interest income. Retail loans as well as long-term mortgage loans are the most substantial portion of fees and commissions settled with the effective interest rate method.

In 2005, systematic growth in net fee and commission income could be observed on a quarterly basis as a result, among others, of an increase in income on the sale of shares in investment funds and of insurance policies. The net income in the fourth quarter was higher by 27.7% than the net income generated in the first quarter of 2005.

Total net fee and commission income in 2005 amounted to PLN 1,068,337 thousand and was lower by 6.9% than net fee and commission income in 2004. The income was affected, to a certain extent, by the reduction of interest rates and changes in exchange rates.

Net trading income and profit from investment activity in 2005 amounted to PLN 139 758 thousand, i.e. ca. 23.3% less than in 2004. Such a discrepancy was caused by generating material one-off income in 2004 related to the restructuring of the Capital Group and the Bank's investment portfolio. Such income was not repeated on a comparable scale in 2005. A sale of shares of Kredyt Bank (Ukraine) S.A. was the main transaction, which resulted in net profit of PLN 36,314 thousand.

Throughout 2005, we observed an increase in net trading income as a result of the extended scale of market transactions concluded to protect against fluctuating foreign currency exchange rates. This item also includes interest income on swaps. As at 31.12.2005, net trading income amounted to PLN 143,812 thousand against PLN 138,611 thousand in 2004.

Result on other operating income and operating expenses recorded in 2005 amounted to PLN 11,238 thousand and was lower than in 2004 due to a high reference base. In 2004, the Group performed, among others, a transaction of non-gratuitous transfer of open pension fund management to an entity from outside the Group which resulted in recognition of PLN 24,000 thousand in 'other operating income'.

In 2005, general and administrative expenses amounted to PLN 890,825 thousand and were lower by 15.6% as compared to 2004 figures. All main cost categories: material costs, depreciation and staff costs, were lower. The reduction of costs was also a result of reducing the Group's size.

The main areas, in which the Group's savings were the most significant as compared to 2004 figures are as follows: depreciation and operation of IT and telecommunication systems; renegotiation of major contracts with service providers, such as security, cash transport, telecommunication services, postal and courier services, car fleet management and reorganization of material supplies in 2004.

Lower staff costs were connected with the implementation of the Bank's restructuring process and the changes resulting from this process with respect to the Bank's HR policy. Under that policy, the main emphasis was placed on the strengthening of sales divisions, centralizing certain functions as well as optimizing the employment in the area of back office and support for business units.

Cost/income ratio (CIR) at 31.12.2005 was equal to 73.0%, what is an improvement by 3.5p.p as compared to last year's level.

In 2005, the Group recorded a slight negative result on net impairment charges for loan receivables and other assets. It amounted to – PLN 9,167 thousand against – PLN 145 663 thousand in 2004. The result is the effect of reduction of credit risk in the Group and the successful implementation of the

restructuring programme concerning non-performing receivables portfolio, which took on the form of income from debt recovery activities.

The continuous positive trend in net operating income generated by the Bank is a proof of the high probability of settlement of retained tax losses and future realization of negative temporary differences. Therefore, as at 31.12.2005, the Bank recognized an excess of deferred tax assets over deferred tax liability amounting to PLN 102,215 thousand. This difference was directly reflected in the Group's net profit for 2005.

## 5.2. Assets structure

The Group's total assets as at 31.12.2005 amounted to PLN 20,841,344 thousand against PLN 20 946 084 thousand as at 31.12.2004 and were down by 0.5%.

Loans and advances to customers and debt securities are the basic items with the largest share in the assets structure.

The major changes in the assets structure in 2005 are as follows:

- decrease in the stake of loans and advances to customers from 54.3% to 46.6%;
- increased share of investment securities in total assets from 18.7% to 32.2%.

The value of particular assets is presented in the table below (in '000' PLN):

	31.12.2005	31.12.2004	Change
Cash and balances with Central Bank	607 090	1 512 591	-905 501
Amounts due from banks	2 229 615	2 699 852	-470 237
Allowance for impairment losses for receivables due from banks	-2 894	-3 194	300
Financial assets at fair value through profit or loss, including held-for-trading assets	703 888	557 760	146 128
Loans and advances to customers	12 306 286	14 105 952	-1 799 666
Allowance for Impairment losses for loans and advances to customers	-2 604 206	-2 740 428	136 222
Investment securities	6 709 711	3 912 871	2 796 840
Equity investments available-for-sale	35 690	35 267	423
Shares in associates measured by the equity method	8 929	0	8 929
Tangible fixed assets	416 400	469 371	-52 971
Intangible assets	111 475	140 187	-28 712
Goodwill of subordinated companies	36 052	36 052	0
Deferred tax assets	112 968	10 435	102 533
Current tax receivables	13 412	5 107	8 305
Other assets	156 928	204 261	-47 333

<b>Total assets</b>	<b>20 841 344</b>	<b>20 946 084</b>	<b>-104 740</b>
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The portfolio of gross loans and advances to customers decreased in 2005 mainly as a result of the repayment of a few major credit exposures. Factors which also affected loan portfolio in 2005 were as follows: the appreciation of the Polish zloty against other major currencies and prudent credit policy aiming at a decrease in receivables concentration and diversification of credit risk.

### Credit portfolio quality

The Group successfully continues the process of decreasing the volume of doubtful receivables portfolio through efficient restructuring and debt recovery activities carried out on the basis of new organizational and procedural solutions implemented in the previous year. Over the previous 12 months, doubtful receivables decreased by over 17.9%. As a result, the quality ratio of the Group's gross receivables portfolio improved by 1.7p.p over the last 12 months, despite the decrease in total gross loans and advances to customers. Over the last 12 months, the Group has written off receivables of PLN 250,802 thousand to provisions.

The Group applies prudence principle when estimating credit risk related to individual credit exposures as well as the portfolio receivables. The coverage of non performing loans with allowances for impairment losses over the last 12 months increased by 8.8p.p. and, as of 31.12.2005, the value of this ratio was among the highest in the sector.

<i>in '000' PLN</i>	<b>31.12.2005</b>	<b>31.12.2004</b>	<b>Change</b>
<b>Gross loans and advances to customers* (net of interest)</b>	<b>12 226 390</b>	<b>14 066 472</b>	<b>-1 840 082</b>
Receivables with no allowance for individual impairment	8 739 256	9 819 191	-1 079 935
Receivables with allowances for individual impairment	3 487 134	4 247 281	-760 147
Interest	79 896	39 480	40 416
<b>Total gross loan and advances to customers</b>	<b>12 306 286</b>	<b>14 105 952</b>	<b>-1 799 666</b>
Impairment charges for loans and advances to customers	2 604 206	2 740 428	-136 222
Impairment charges for receivables with individual impairment allowance	2 515 458	2 688 175	-172 717
<b>Total net loans and advances to customers</b>	<b>9 702 080</b>	<b>11 365 524</b>	<b>-1 663 444</b>
<b>Receivables for which individual allowance for impairment was identified to total gross receivables</b>	<b>28.5%</b>	<b>30.2%</b>	<b>-1.7 p.p.</b>
<b>Coverage of receivables for which individual allowance for impairment was identified</b>	<b>72.1%</b>	<b>63.3%</b>	<b>8.8 p.p.</b>

\* excluding banks

### Loans and credits by customers

The increased share of loan receivables due from individuals in total loans and advances to customers as assumed in the strategy is the most important change in the structure of the Bank's loan portfolio. As at 31.12.2005, it amounted to 44.7%, i.e. increased by 6.3p.p. as compared to 2004 year end figures.

	31.12.2005	31.12.2004	Change
<b>Individuals*</b>	<b>44.7%</b>	<b>38.4%</b>	<b>6.3 p.p.</b>
- overdraft facilities	9.4%	9.4%	0.0 p.p.
- purchased debt	5.6%	6.6%	-1.0 p.p.
- term loans	48.0%	54.9%	-7.0 p.p.
- mortgages	37.0%	29.0%	8.0 p.p.
- realized guarantees	0.0%	0.0%	0.0 p.p.
- other receivables	0.0%	0.0%	0.0 p.p.
<b>Corporate customers</b>	<b>49.3%</b>	<b>52.3%</b>	<b>-3.1 p.p.</b>
- overdraft facilities	15.4%	12.5%	2.9 p.p.
- term loans	79.3%	82.5%	-3.2 p.p.
- purchased debt	0.9%	1.4%	-0.5 p.p.
- realized guarantees	1.0%	0.6%	0.4 p.p.
- other receivables	3.3%	3.0%	0.3 p.p.
<b>Budget</b>	<b>5.4%</b>	<b>9.0%</b>	<b>-3.6 p.p.</b>
- overdraft facilities	0.3%	1.0%	-0.7 p.p.
- term loans	99.7%	99.0%	0.7 p.p.
- purchased debt	0.0%	0.0%	0.0 p.p.
<b>Interest</b>	<b>0.6%</b>	<b>0.3%</b>	<b>0.3 p.p.</b>
<b>Total</b>	<b>100.0%</b>	<b>100.0%</b>	

\* the item contains: amounts due from private persons, individual entrepreneurs, individual farmers, noncommercial institutions providing services for households

### Exposure towards the Group's 10 major institutional customers

The table below presents the share of exposure towards 10 largest corporate customers in the Group's portfolio.

Company	Share (%) in the portfolio as at 31.12.2005	Share (%) in the portfolio as at 31.12.2004
Customer 1	2.7	3.6
Customer 2	2.3	2.0
Customer 3	2.0	1.9



Customer 4	1.9	1.8
Customer 5	1.9	1.6
Customer 6	1.5	1.4
Customer 7	1.4	1.2
Customer 8	1.4	1.2
Customer 9	1.2	1.2
Customer 10	1.2	1.1
<b>Total</b>	<b>17.5</b>	<b>17.0</b>

### Geographical structure of exposure

The Bank's exposure as at 31.12.2005 and 31.12.2004 by provinces was as follows:

Province	Gross loans structure (%)	Gross loans structure (%)
	31.12.2005	31.12.2004
mazowieckie	18.5	23.8
lubelskie	15.8	13.6
śląskie	10.9	9.5
wielkopolskie	9.7	9.2
dolnośląskie	9.1	9.6
pomorskie	7.6	8.0
małopolskie	6.3	5.2
łódzkie	4.6	4.6
zachodniopomorskie	3.8	3.4
podlaskie	3.2	3.1
kujawsko-pomorskie	2.3	2.2
warmińsko-mazurskie	2.3	2.3
podkarpackie	1.7	1.8
świętokrzyskie	1.5	1.3

non-resident	1.1	1.1
lubuskie	0.8	0.8
opolskie	0.8	0.5
<b>Total</b>	<b>100</b>	<b>100</b>

### Exposure in industrial segments

The Bank's exposure as at 31.12.2005 and 31.12.2004 by industrial segments was as follows:

Industry	Exposure (%)	Exposure (%)
	31.12.2005	31.12.2004
Production activities	28.8	27.0
Retail and wholesale; repairs of motor vehicles and articles for personal and home use	22.9	21.5
Real estate administration and lease	14.6	14.3
Public administration and national defense, legally guaranteed social care	8.4	12.7
Financial intermediation	8.1	5.7
Supplies of electricity, gas and water	4.9	5.7
Construction	3.5	3.3
Other services for municipalities, social and individual services	1.4	2.6
Agriculture, hunting and forestry	2.3	1.9
Hotels and restaurants	1.6	1.6
Transport, storing and communication	1.6	1.5
Education	1.2	1.1
Health care and social care	0.5	0.2
Other	0.2	0.9
<b>Total</b>	<b>100</b>	<b>100</b>

### Amounts due from customers by maturities

Loans and advances to customers as at 31.12.2005 and 31.12.2004 by maturities were as follows (in '000' PLN):

	31.12.2005	31.12.2004	Change
- up to 1 month	241 596	1 314 543	-1 072 947
- 1-3 months	645 479	427 357	218 122
- 3-6 months	541 630	522 609	19 021
- 6 months to 1 year	2 632 167	1 931 232	700 935

- 1 - 3 years	1 757 551	1 732 905	24 646
- 3 - 5 years	1 111 266	1 199 684	-88 418
- 5 - 10 years	1 498 527	1 259 624	238 903
- 10 - 20 years	964 944	1 262 614	-297 670
- over 20 years	419 051	347 516	71 535
- past due	2 414 179	4 068 388	-1 654 209
- interest	79 896	39 480	40 416
<b>Total</b>	<b>12 306 286</b>	<b>14 105 952</b>	<b>-1 799 666</b>

### 5.3. Liabilities structure

In 2005, as a result of terminating the restructuring processes of sales divisions, the Group recorded an increase by 3.4% in amounts due to customers, the major item of liabilities.

At the same time, in 2005, the Group recorded, as assumed in the Group's strategy, a significant increase in the value of assets of investment funds managed by KBC TFI sold through the Bank's network. KBC TFI has been established as a result of merger of two companies owned by KB S.A. and WARTA S.A. The value of investment funds assets increased in 2005 by 258% to PLN 1.8 billion. In terms of total assets of investment funds and deposits, the increase in customer resources between 31.12.2004 and 2005 amounted to 12.3%.

Amounts due to customers in total liabilities increased by 2.6p.p. to 69.7%. Another positive change was a decrease of amounts due to banks in total liabilities by 2.1p.p. to 12.3% was another positive change. As at 31.12.2005, amounts due to banks were higher than amounts due from banks, but the surplus was marginal and fluctuated during the year (at the end of September 2005, amounts due from banks exceeded amounts due to them).

The value of particular liabilities is presented in the table below (in '000' PLN):

	31.12.2005	31.12.2004	Change
Amounts due to banks	2 562 167	3 007 090	-444 923
Held-for-trading financial liabilities	220 155	233 932	-13 777
Amounts due to customers	14 533 624	14 061 105	472 519
Debt securities issued	402 435	418 150	-15 715
Securities sold under repurchase agreements	368 701	718 772	-350 071
Income tax	4	5 778	-5 774
Provisions	77 847	37 439	40 408
Deferred tax liability	864	2 060	-1 196
Other liabilities	404 371	345 384	58 987

Subordinated liabilities	589 581	599 286	-9 705
Shareholders' equity	1 681 595	1 517 088	164 507
<b>Total liabilities</b>	<b>20 841 344</b>	<b>20 946 084</b>	<b>-104 740</b>

### Customers' deposits by entities and types

Two tendencies were noticed in the structure of customers' deposits in 2005: an increase in the share of current deposits recorded both for natural and corporate customers and an increase in the share of the corporate segment in total deposits.

A substantial increase of the individual customers' interest, in alternative forms of investing activities, in the shares of investment funds has been observed.

Customers' deposits	31.12.2005	31.12.2004	Change
<b>Individuals*</b>	<b>62.4%</b>	<b>65.3%</b>	<b>- 2.9 p.p.</b>
- in current account	42.4%	27.6%	14.8 p.p.
- term deposits	57.6%	72.4%	-14.8 p.p.
<b>Corporate customers</b>	<b>25.8%</b>	<b>22.1%</b>	<b>3.7 p.p.</b>
- in current account	42.6%	39.8%	2.8 p.p.
- term deposits	54.9%	56.6%	-1.7 p.p.
- loans and advances	2.6%	3.5%	-0.9 p.p.
<b>Budget</b>	<b>11.6%</b>	<b>12.2%</b>	<b>-0.6 p.p.</b>
- in current account	76.7%	79.3%	-2.5 p.p.
- term deposits	23.3%	20.7%	2.5 p.p.
<b>Interest</b>	<b>0.3%</b>	<b>0.4%</b>	<b>-0.1 p.p.</b>
<b>Total**</b>	<b>100.0%</b>	<b>100.0%</b>	

\* the item contains: amounts due from private persons, individual entrepreneurs, individual farmers, noncommercial institutions providing services for households

### Amounts due to customers by geographical regions

Amounts due to customers as at 31.12.2005 and 31.12.2004 by provinces were as follows:

Province	Liabilities due to customers structure (%)	Liabilities due to customers structure (%)
	31.12.2005	31.12.2004
mazowieckie	29.7	27.3
dolnośląskie	9.5	8.3

małopolskie	6.8	7.5
pomorskie	6.8	7.0
śląskie	6.7	8.1
łódzkie	6.4	6.9
podlaskie	6.2	5.7
wielkopolskie	5.9	6.2
lubelskie	5.5	5.7
podkarpackie	4.8	5.0
zachodniopomorskie	3.3	3.4
kujawsko-pomorskie	3.0	3.0
warmińsko-mazurskie	1.9	2.0
świętokrzyskie	1.4	1.6
lubuskie	1.2	1.2
opolskie	0.9	1.1
<b>Total</b>	<b>100</b>	<b>100</b>

### Customers' deposit (by maturities)

Customers' deposits as at 31.12.2005 and 31.12.2004 by maturities were as follows (in '000' PLN):

	31.12.2005	31.12.2004	Change
- up to 1 month	10 780 122	9 090 093	1 690 029
- 1-3 months	1 816 801	2 468 467	-651 666
- 3-6 months	894 819	1 156 233	-261 414
- 6 months to 1 year	677 193	685 962	-8 769
- 1 - 3 years	213 739	384 938	-171 199
- 3 - 5 years	5 049	78 334	-73 285
- 5 - 10 years	106 054	131 944	-25 890
- 10 - 20 years	1 599	3 984	-2 385
- over 20 years		60	-60
- interest	38 248	61 090	-22 842
<b>Total</b>	<b>14 533 624</b>	<b>14 061 105</b>	<b>472 519</b>

### Loans and advances borrowed by the Group

As at 31.12.2005, there were two subordinated loans in the balance sheet of Kredyt Bank S.A. borrowed from KBC Bank N.V. Dublin amounting to USD 50 million with maturity date falling on 17.01.2006 and a loan of EUR 110 million with maturity date falling on 25.05.2008.

In addition, as at 31.12.2005, the following loans were active:

- from KBC Bank N.V. Dublin: EUR 150 million with maturity date falling in July 2009 and of CHF 150 million with maturity date falling in July 2010.
- from BFG amounting to PLN 95.5 million with maturity date falling on 10.10.2007. This commitment was taken over by the Kredyt Bank S.A with the organized part of the banking company led by Polski Kredyt Bank S.A. and confirmed with agreement between KB S.A. and BFG dated on 13.12.2002. The purpose of continuing the returnable financial support by BFG was moderating of consequences of taking over of the mentioned company.

#### 5.4. Off-balance sheet items

The value of particular off-balance sheet items is presented in the table below (in '000' PLN):

	31.12.2005	31.12.2004	Change
Contingent liabilities, granted and received	4 089 190	5 771 653	-1 682 463
1. Liabilities granted, including:	3 577 985	5 256 655	-1 678 670
a) financial	2 451 828	2 085 879	365 949
b) guarantee	1 126 157	3 170 776	-2 044 619
2. Liabilities received	511 205	514 998	-3 793
a) financial	11 831	51 707	-39 876
b) guarantees	499 374	463 291	36 083
Amounts due under sale/purchase transactions	79 905 636	31 099 032	48 806 604
Other	3 057 287	3 649 245	-591 958
- received securities and guarantees	3 057 191	3 649 150	-591 959
- other	96	95	1
<b>Total off-balance sheet items</b>	<b>87 052 113</b>	<b>40 519 930</b>	<b>46 532 183</b>

The substantial decrease in guarantee liabilities as at 31.12.2005 results from the expiry of the guarantee granted by the Bank to KBC Dublin for the benefit of Kredyt International Finance B.V.

#### Loans extended, guarantees and sureties issued, including those granted to the Issuer's related parties

As at 31.12.2005, the Bank issued guarantees with the total value of at least 10% of the Bank's shareholders' equity to two companies and their subsidiaries. The guarantees were issued for the total amounts of PLN 235,735 thousand and PLN 176,601 thousand. Their average maturities as at 31.12.2005 were one year two months and seven months respectively.

As at 31.12.2004, the Bank issued guarantees of the total value of at least 10% of the Bank's shareholders' equity to its subsidiary. The guarantee amounted to PLN 1,874,490 thousand. On 07.07.2005, due to the repayment of secured loans, the above guarantees expired.

The above guarantees were issued on market terms. The Bank's remuneration for issuing the guarantees was also determined on market terms.

## 6. Ratings of the Bank's financial reliability

In 2005, Kredyt Bank S.A. obtained the following ratings of financial reliability:

### Moody's Investors Service

Long-term deposits rating	<u><b>A2</b></u>
Short-term deposits rating	<u><b>P1</b></u>
Financial strength	<u><b>D-</b></u>
Outlook	<u><b>Stable</b></u>

On 19.09.2005, Moody's Investors Service, an international rating agency, upgraded the Bank's financial strength rating from 'E+' to 'D-', which implies stable growth outlook. The agency noted that the upgrade of the financial strength rating was associated with the improvement of the Bank's financial standing. The agency also emphasized the substantial decrease in operating expenses resulting from the restructuring scheme and the high level of the Bank's capital adequacy ratio.

### Fitch Ratings

Short-term rating	<u><b>A</b></u>
Long-term rating	<u><b>F1</b></u>
Support rating	<u><b>1</b></u>
Individual rating	<u><b>D</b></u>
Outlook	<u><b>Positive</b></u>

On 05.12.2005, Fitch Ratings, an international rating agency, increased the individual rating of Kredyt Bank S.A. from D/E to D. The increase in the individual rating was a result of regaining appropriate profitability by the Bank and improvement of the effectiveness of the Bank's functioning. Furthermore, the agency stressed that long- and short-term ratings include the support of KBC Bank NV, a strategic investor, rated by Fitch Ratings at AA- level.

## 7. Corporate governance

Since January 2005, the Group has been bound by the corporate governance rules, adopted by the Stock Exchange, but modified as compared to the 2002 version, for public companies admitted to stock exchange trading set forth in 'The 2005 Best Practices in Public Companies'.

According to the Warsaw Stock Exchange guidelines stating that statements of the companies on the observance of corporate governance should be approved by the General Meeting of Shareholders, on 25.04.2005, under Resolution No. 26, the General Meeting of Shareholders of Kredyt Bank S.A. adopted and obliged the company to observe corporate governance – 'The 2005 Best Practices in Public Companies' approved by the Resolution of the Stock Exchange Board No. 44/1062/2004 of 15.12.2004.

The key assumptions of corporate governance are as follows:

- best practices of General Meetings of Shareholders;
- best practices of Supervisory Boards;
- best practices of Management Boards;
- best practices in relations with third parties and third party institutions.

In the current report of 01.07.2005, the Management Board of Kredyt Bank S.A. submitted, to the Warsaw Stock Exchange, the scope and contents of the corporate governance rules applied by the Bank and set forth in the Resolution of the General Meeting of Shareholders of Kredyt Bank S.A. as of 25.04.2005.

Under the corporate governance rules, the Bank adopted the By-laws of its three governing bodies: the Management Board, the Supervisory Board and the General Meeting of Shareholders. In addition, the Bank, implementing the corporate governance rules, presents on its website, in investor relations section, stock exchange reports, current reports, basic internal by-laws and regulations and other information.

As stipulated in the policy on implementation of the compliance function, i.e. the compliance with law, recommendations and guidelines of the National Bank of Poland, the Commission for Banking Supervision, the Minister of Finance, the Securities and Exchange Commission, the General Inspector of Banking Supervision and internal regulations, adopted by the Management Board of Kredyt Bank S.A., since 30.07.2004, the Bank has been obliged to comply with 'The Code of Ethics for Employees of Kredyt Bank S.A.'

The ethics rules set forth in the Code arise from the general moral standards and are basic guidelines to be observed by the Bank's employees performing their tasks, i.e. honesty, loyalty, professionalism, reliability and due diligence. Each employee is obliged to make every effort and show initiative to continue improving the quality of the customer service in the Bank.

The Ethics, Procedures and Control Unit has been established within the Compliance Department. Its main objective is to supervise the observance of the financial ethics rules, initiating explanatory and auditory proceedings and cooperate with the ethics unit of the Bank's major shareholder.



## 8. The Group's outlook and growth drivers

KB Group holds a strong position among 10 top largest institutions on the banking market. The Bank and its related companies provide a wide range of retail and corporate banking services, services on the money market and indirectly on the insurance market. A developed network of outlets and distribution channels ensures easy access for customers to the Bank's and the Group's services and products.

In the months to come, the rate of economic growth will be one of the external factors contributing to the Group's development. An increase in capital expenditure on fixed assets, absorption of support and the inflow of direct foreign investments will be crucial for corporate banking. In the event of retail banking, the rate of individual consumption growth depends on a decrease in the unemployment rate and increase in salaries fund. From the point of view of financial product prices, the monetary policy of the Monetary Policy Council, especially a possibility of further reduction of interest rates, is of great importance in this respect. The above-mentioned factors are directly reflected in the level of demand for banking facilities.

The banking sector is now competing for household resources with non-banking institutions. The competition is noticeable in the increased popularity of alternative forms of saving money, such as investment funds and investments on real estate markets. As the position of banks becomes relatively weaker in the process of households resources accumulation in the form of deposits, the inter-bank competition in retail banking segment is increasing.

KB Group's long-term goal involves accomplishment of a strong position among institutions on the banking market in Poland by adopting the model of a universal banking and insurance group. The Bank and its Group will focus on building up and fostering its position on the basic financial services markets, seeking to develop sales and stable long-term customer relations, achieve high quality of customer service and high levels of customer satisfaction.

### **The Bank's/Group's strategic goals:**

In terms of their position on the retail market:

- focus on 'mass' and 'upper mass' customers as well as SMEs (including companies with annual sales up to PLN 16 million);
- focus on key products (retail and mortgage loans; credit cards; term deposits and mutual funds; and the most popular products linked to Warta insurance offer)

In terms of their position on the corporate market:

- focus on services to medium-sized companies, including customers of other KBC Group members operating in Poland;
- focus on the increase in customer relations efficiency through the sale of additional products; beside traditional loans and deposits, these are mainly leasing, cash management, trade financing and market risk management instruments.

In terms of their financial standing:

- a medium-term goal entails the achievement of ROE at the level of 17%;

- a medium-term goal entails the achievement of cost/income ratio at the level of 60%.

**Methods of the goals accomplishment:**

- implementation of bancassurance model on the basis of the major shareholder's experience;
- fostering the Bank's new brand;
- increasing network effectiveness and its expansion (the process of creating 120 new outlets launched in 2006), creating mobile sale teams, activating alternative distribution channels;
- high quality of services and customer satisfaction.

The process of changing the Bank's and the Group's brand visualization launched in September 2005 according to the new strategy is listed among the internal factors contributing to the Group's development. Kredyt Bank S.A. and WARTA S.A., as well as other entities in KBC Group operating on the Polish market, introduced similar logotypes, with their colouring and graphics referring to the common shareholder. The change is accompanied by a process of standardizing interiors of the outlets and promotion of the Bank's image and the new, joint product offer.

The new visualization and logo emphasize the close cooperation and the membership of the Bank and the Insurer in the international structure of KBC Group. The Group will become more recognizable and this will also allow it to maximize the synergy effect..

The common goal of KB S.A. and WARTA S.A. is to develop bancassurance and to escalate measures leading to the creation of a banking and insurance group. Both companies are natural partners; their services and products are complementary and ensure a complete offer for customers. The successful accomplishment of the Group's development strategy also depends on the continuance of effective credit risk management and the control and adjustment of functioning costs to the scale of operations.

## **9. Statement of the Management Board**

Under Article 101 clause1 p.4 and p.5 of the Regulation by the Polish Council of Ministers of 21 March 2005 on current and interim information provided by issuers of securities (Journal of Laws of 25.03.2005 No. 49 item 463), the Management Board of Kredyt Bank S.A. hereby makes the following statement:

### **9.1. True and fair view presented in the financial statements**

According to the best knowledge of the Management Board of Kredyt Bank S.A., the annual consolidated financial statement of Kredyt Bank S.A. Capital Group and the annual financial statement of Kredyt Bank S.A. covering the period from 01.01.2005 to 31.12/2005 along with the comparable data were prepared according to the accounting principles effective in the Group and present a true and fair view of the financial standing, assets and financial result of Kredyt Bank S.A. Capital Group. In addition, the Management Board of Kredyt Bank S.A. hereby declares that the annual Management Board's report presents a true picture of the development and accomplishments as well as the

situation (including the description of basic risks and threats) of Kredyt Bank S.A. Capital Group in 2005.

## 9.2. Appointment of the certified auditor for financial statements

The Management Board of Kredyt Bank S.A. hereby declares that the certified auditor to audit the annual consolidated financial statement of Kredyt Bank S.A. Capital Group as at 31.12.2005 was appointed as required by law. This entity and certified auditors performing the audit complied with the conditions on the issue of impartial and independent audit report, as required by the Polish law.

Signatures of all Management Board members

Date 28.02.2006	Ronald Richardson	President of the Management Board .....
Date 28.02.2006	Krzysztof Kokot	Vice-President of the Management Board .....
Date 28.02.2006	Małgorzata Kroker-Jachiewicz	Vice-President of the Management Board .....
Date 28.02.2006	Guy Libot	Vice-President of the Management Board .....
Date 28.02.2006	Bohdan Mierzwiński	Vice-President of the Management Board .....