

PKO Finance AB (publ)

Annual report for the period 2020-01-01 - 2020-12-31

(CID 556693-7461)

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This document is a translation of a document originally issued in Swedish. The only binding version is the original Swedish version.



MANAGEMENT REPORT

The company is a wholly owned subsidiary of Powszechna Kasa Oszczednosci Bank Polski Spolka Akcyjna ("PKO Bank Polski SA").
The company is domiciled in Stockholm.

Business

The business of the company is to directly or indirectly own, manage and trade securities and to conduct other non-licensed financial business including lending and other activities compatible therewith.

During 2008 the company has entered into a "Programme for the issuance of Loan Participation Notes". Under the Programme, the company may issue bonds (Loan Participation Notes) in series. The sole purpose of issuing each series is to finance loans to the parent company. The company charges certain rights under the loans to the parent company for the benefit of the note holders.

In accordance with the "Programme for issuance of Loan Participation Notes", four tranches of Participation Notes denominated in CHF and EUR have been issued during 2010- 2012. Additionally a bond loan for the American market was issued during 2012 based on such documentation binding on the debt market in the United States and in accordance with the Rule 144A in the US Securities Act. In January 2014 an additional bond loan has been issued in accordance with the above-mentioned programme which amounts to EUR 500 000 000. This bond repayment date was January 23, 2019.

All notes issued run with fixed interest and have been used to finance loans to the parent company on basically the same terms.

At the reporting date, there are two active tranches: One in EUR and one in USD (for more information please refer to Notes 5 and 8).

The notes in USD and EUR are quoted on the Luxembourg Stock Exchange (LSE).

In December 2017 EUR 5 500 000 was lent to the group company PKO Leasing Sverige AB, with the maturity date till December 2023. The interest is variable.

The financial year

Lower interest income and interest expenses and the lower balance sheet total are consequences of the EUR strengthening against the US-dollar. Income before taxes is - as it was in 2019 - affected by relatively high costs for advisors that have been used to advice the Company in relation to the income-tax issue described in note 13. Income before taxes is also affected by the strengthening of SEK against the EUR.

The financial position, income and cash flow have not in any material way been affected of the COVID-19 pandemia.
The company has not had any employees.

Multiyear review (KEUR)

	2020	2019	2018	2017
Interest income	43 137	44 565	53 492	55 342
Income before taxes	890	-753	132	202
Equity	11 270	5 547	6 386	6 329
Total assets	947 965	1 024 847	1 451 708	1 411 761

Risks and uncertainties

Market risk

The loans granted to the parent company constitute the main assets of the company and are financed by bond loans in the same currencies and with the same interest and repayment terms. The interest rates on the loans granted to the parent company are fixed as are the interest rates on the bond loans. The loans to the parent company are in all cases financed by bond loans in the same currency. All material cash at banks is held in EUR which is the reporting currency of the company.

Liquidity risks

As mentioned above the company's interest payments on the bond loans and the interest payments from the parent company occur simultaneously (actually the interest payments on the loans to the parent company occur shortly before the interest on the bond loans are due for payment). Consequently, the company will always have access to funds in order to finance its interest payments. See also note 5.

Credit and counterparty risk

PKO Bank Polski SA is the company's main borrower. The financial situation of PKO Bank Polski SA is very good (the Moody's long-term rating is A3) for which reason the credit risk of the company is deemed to be low. Additionally, PKO Bank Polski SA has issued a guarantee in order to secure all obligations of PKO Leasing Sverige AB resulting from the loan agreement with the company. All material cash at banks is placed in SEB, Sweden.

Corporate governance report

Principles for corporate governance

The Company is headed by the Board of Directors and the Managing Director whom exercise their duties as set out according to the Articles of Association, the Instruction for the Managing Director, Rules of Procedures for the Board of Directors and the Company's Act.

Important elements of control and risk-management related to financial reporting

The Company has established routines in order to secure the accuracy of the financial reports which among other procedures include the preparation of quarterly financial reports that -in addition to review by the Board of Directors - also are reviewed by representatives from the parent company.

Parent Company

Details regarding the parent Company, that owns all shares are shown in note 9.

General meetings of Shareholders

The owners decision making rights are exercised at the General Meeting of Shareholders in accordance with law and Articles of Association.

Board of Directors

The Board of Directors work in accordance with law, Articles of Association and based on Rules of Procedure established by the General Meeting of Shareholders. The Board of Directors makes all decisions which it has the right to make and has not established any committees.

In view of the limited activities and low number of transactions the Board of Directors considers the control system described above to be appropriate for which reason Swedish code for Corporate Governance has not been applied.

Future activities of the company

The future activities of the company are linked to the development of the financial markets and the macroeconomic environment. The future activities will also be affected by the final outcome of the tax issue described in note 13.

As a consequence of the recent outbreak of the new Corona virus (COVID 19) the Swedish economic situation is difficult to assess. However as of the day of the publication of this Annual report the outbreak of the Corona virus has not affected net income or cash flow in any material way.

Proposal for appropriation of profits and losses

The following earnings are available for the General Meeting of Shareholders to appropriate:

Retained earnings	EUR	0
The profit of the year	EUR	<u>5 723 120</u>
Total profit of the year and retained earnings	EUR	5 723 120
To be carried forward	EUR	5 723 120

As regards profit and loss and balance sheet see financial reports with comments below.

PROFIT AND LOSS STATEMENT

Amounts in euro.	Note 1,2	2020	2019
Administration and commission revenues from group companies		107 756	110 200
Other operating expenses	Note 3	-249 740	-266 984
Operating income		-141 984	-156 784
Financial items			
Interest income, group companies		43 136 915	44 565 405
Interest expenses		-43 399 758	-45 150 113
Net currency effects		1 295 299	-11 675
Income before taxes and appropriations		890 471	-753 166
Appropriations			
Dissolution of profit equalization reserve		130 614	102 916
Appropriation to profit equalisation reserve		-396 394	-51 897
Income before taxes		624 691	-702 147
Deferred tax income/expense	Note 13	5 365 997	-64 437 867
Current tax expense	Note 4	-267 568	-33 264
Net income		5 723 120	-65 173 277

The comprehensive income of the company equals the net income.

BALANCE SHEET

Note 1, 2

Amounts in euro		2020-12-31	2019-12-31
Assets			
<i>Long-term financial assets</i>			
Loans granted to group companies	Note 5, 6	865 762 731	944 989 809
<i>Current assets</i>			
Loans granted to group companies	Note 5, 6	816 000	816 000
Receivables, parent company	Note 13	66 840 996	64 334 542
Prepaid expenses		13 721	13 119
Accrued income, group companies	Note 7	10 737 006	11 691 882
Cash and cash equivalents		<u>3 794 737</u>	<u>3 002 037</u>
<i>Total current assets</i>		82 202 460	79 857 580
Total assets		947 965 192	1 024 847 388
Equity and liabilities			
Equity			
<i>Restricted equity</i>			
Share capital (500 000 shares with quote value EUR 11,09)		5 547 358	5 547 358
<i>Unrestricted equity</i>			
Retained earnings		0	65 173 277
Net income		<u>5 723 120</u>	<u>-65 173 277</u>
<i>Total unrestricted equity</i>		5 723 119	0
Total equity		11 270 477	5 547 358
Untaxed reserves			
Profit equalisation reserve		755 675	489 894
Liabilities			
<i>Long-term liabilities</i>			
Bond loans	Note 6, 8	863 542 789	941 962 102
<i>Short-term liabilities</i>			
Deferred income tax liability	Note 4, 13	61 535 375	65 059 762
Accrued interest expenses		10 712 887	11 665 414
Other short-term liabilities		306	17 644
Other accrued expenses		<u>78 307</u>	<u>39 871</u>
<i>Total short-term liabilities</i>		72 396 251	76 848 034
Total liabilities		935 939 040	1 018 810 136
Total liabilities and equity		947 965 192	1 024 847 388

Cash-flow statement

Amounts in EUR	2020	2019
Operating activities		
Interest and other payments from parent company	43 484 522	55 496 404
Income taxes	-49 784	-8 019
Payments to suppliers, remunerations to directors	-186 650	-251 243
Other interest income	-14 456	-10 299
Investing activities	-	-
Financing activities		
Repayment of bond loans	0	-500 000 000
Cash flow from financing activities	0	-500 000 000
Cash flow of the period	784 232	855 465
Opening cash balance	3 002 037	2 148 081
Currency difference in cash balance	8 468	-1 509
Closing cash balance	3 794 737	3 002 037

REPORT ON CHANGES IN EQUITY

	<i>Share capital</i>	<i>Retained earnings</i>	<i>Net income</i>	<i>Total equity</i>
Amount 2019-01-01	5 547 358	781 681	57 054	6 386 093
Retained earnings		57 054	-57 054	0
Unconditional shareholders contribution		64 334 542		0
Net income			-65 173 277	-65 173 277
Amount 2019-12-31	5 547 358	65 173 277	-65 173 277	5 547 358
Amount 2020-01-01	5 547 358	65 173 277	-65 173 277	5 547 358
Retained earnings		-65 173 277	65 173 277	0
Net income			5 723 120	5 723 120
Amount 2020-12-31	5 547 358	0	5 723 120	11 270 477

The shares have no nominal values and are fully paid.

NOTES

Note 1 Basis for the preparation of the report

The annual report is prepared in accordance with the Annual Accounts Act and recommendation number 2 from the Financial Reporting Council (RFR 2); Reporting for legal entities. RFR 2 obligates the company to apply International Financial Reporting Standards (IFRS) as adopted by the European Union, to the extent this is possible within the framework of the Annual Accounts Act and taking into account the connection between accounting and taxation. The recommendation indicates exceptions and additions that are needed in relation to IFRS.

The Annual report is based on the assumption of going concern during a foreseeable future.

The functional currency is EUR which also is the reporting currency.

Note 2 Important accounting principles.

New and revised standards – applicable 1 January 2020:

None of the new applicable IFRS or IFRIC interpretations effective for the financial year starting 2020-01-01 has had any material impact of the annual report of the financial reports of the Company.

No new standards have come into effect 1 January 2020. However the following standards have been changed:

IFRS 3 Business acquisitions: The changes aim at clarifying the definition of "business".

IFRS 7, IFRS 9 and IFRS 39 Financial instruments: Amended criteria when hedge accounting is used with the purpose to make it useful when terminating using reference interests (IBOR).

IFRS 8: Accounting policies, errors and estimates in the accounts:

Clarifying the definition of "material" with the purpose of using the concept consistently wherever it is used in IFRS-standards.

Set out below are new and amended standards and interpretations which have been published but comes into effect later than 2021-01-01

At the time of preparing the consolidated financial statements as of 31 December 2020 there are some standards and interpretations which are to take effect 2021 or later. None of these is expected to have a significant effect on the annual financial statements of PKO Finance AB.

The Company is considered to be one business segment

Foreign currency

Transactions in other currencies than EUR have been valued at the exchange rate which prevailed on the day of transaction. As at the reporting date all assets and liabilities denominated in other currencies than EUR have been valued using the exchange rate prevailing on the reporting date according to Oanda. The following rates have been used :

	<u>2020-12-31</u>	<u>2019-12-31</u>
	EUR	EUR
1 SEK =	0,09938	0,09569
1 PLN =	0,21947	0,23472
1 USD =	0,81407	0,89286

Reporting of revenues and expenses

Interest income and expenses are reported in accordance with the effective interest method. Other revenues are reported at the time of earning and to the extent it is probable that the future economic benefits will be made available to the company and that the revenues can be estimated in a reliable way.

Valuation of assets and liabilities

Assets and liabilities are reported at acquisition cost and nominal value respectively if nothing else is stated.

In those cases when it can be expected that the impairment exists, the value of the asset is decreased by an relevant amount of an impairment allowance.

Financial instruments

Loans granted to group companies and bond loans have been reported in accordance with the effective interest method which means that the difference between the discounted (book) value and the nominal values of the loans are amortized over the term over the respective loans. These amortizations are included in reported interest income/expense thus reflecting the effective interest of the respective loans.

The first valuation reporting

Accounts receivable and debt instruments are reported when they are issued. Other financial assets and financial liabilities are reported when the company becomes party to the agreed terms of the instrument. Financial liabilities are classified to accrued cost.

Financial assets

The company removes a financial asset from the balance sheet when the agreed rights to the cash flows from the financial asset ceases or if the company transfers the right to receive the rights to the agreed cash flows by a transaction in which all material risks and rewards connected with the ownership have been transferred.

Financial debts

The company removes a financial debt from the balance sheet when the agreed obligations have been met, are annulled or cease. The company also removes a financial debt when the agreed terms are modified and the cash-flows of the modified debt is materially different. In this case a new financial liability - at real value - based on the new terms is reported.

When a financial liability is removed the difference between the reported value which has been removed and the payment made (including transferred non-monetary assets and assumed debt) in the profit- and loss statement.

Income tax

Reported income taxes includes taxes that are to be paid or received relating to the reported period and adjustments regarding earlier periods. Tax-liabilities/receivables are valued at the amounts, that, in the opinion of the company are expected to be paid to or received from the tax office. Please note however the uncertainty described in note 13 and its effect on the reporting below in this paragraph.

Taxable income can differ from income before taxes as reported in the profit and loss statement as this income excludes revenues and expenses that are taxable or deductible in other periods and it also excludes revenues and expenses that permanently are non-taxable or non-deductible. The tax liability which is described in in note 13 relate to such tax which is uncertain if the company finally will pay.

This liability relates both to such tax which - in a situation where the Company finally is considered liable to pay tax on the capital gains described in note 13 - relates to capital gains realised during 2019 and deferred tax liabilities on unrealized capital gains. The Company has - in its income tax returns for prior periods and for 2019 - not reported net realized capital gains (but present the tax office with a full disclosure)

In accordance with RFR2 no deferred tax liability relating to the company's untaxed reserves is reported.

Share capital

Reported share capital corresponds to registered nominal value.

Estimation of fair value

Fair value of the loans granted to the parent company and of the bond loans have been calculated based on listed value on the Luxembourg stock exchange according to Bloomberg as at the reporting date.

The fair value for the loan to the other group company PKO Leasing Sverige AB is estimated using yield curve and margin model.

For other financial assets and liabilities it is the opinion of the company that the reported values constitute the best possible estimate of fair value, since these assets and liabilities are short-term and have high liquidity.

Estimations and assumptions

In preparing the report the company has made estimates and assumptions. Actual results may differ from these estimates. Such an estimation relates to the final outcome in the tax matter which is referred to in note 13.

Note 3 Other external expenses

	<u>2020</u>	<u>2019</u>
Audit fees KPMG	29 220	26 164
Audit fees PwC	27 330	-
Remunerations to directors	16 739	23 878
Expenses, group companies	0	825
Administration fees	51 885	65 684
Other external fees	104 619	137 277
Bank fees	<u>19 948</u>	<u>13 156</u>
<i>Total other external expenses</i>	249 740	266 984

The remuneration paid to the Board of Directors amounted to 22 318 (2020) and 22 394 (2019).

As in 2019 there are two males and one female in the Board of Directors.

Other external fees include external legal and advisory fees.

Note 4 Reconciliation of effective tax

	<u>2020</u>	<u>2020</u>	<u>2019</u>	<u>2019</u>
	(%)		(%)	
Income before tax but after appropriations		624 691		-702 147
Tax according to current tax rate	21,40%	-133 684	21,40%	-150 259
Non-deductible expenses		-108 279		-183 206
Upward adjustment on dissolution of profit equalisation reserve		-337		-524
Flat-rate interest on profit equalisation reserve		-480		-525
Tax relating to currency gains not included in the accounts (note 13)		5 365 997		-64 437 867
Currency effects		-24 788		731
Reported effective tax	816,15%	5 098 429	9224,80%	-64 771 651

Note 5 Loans granted to group companies

<i>Issued</i>	<i>To be repaid</i>	<u>2020-12-31</u>	<u>2019-12-31</u>	<u>2020-12-31</u>	<u>2019-12-31</u>
		<i>Currency of denomination</i>		<i>Reporting currency (EUR)</i>	
2012-07-25	2022-07-25	€ 49 823 844	€ 49 710 534	49 823 844	49 710 534
2012-09-26	2022-09-26	\$999 567 808	\$999 317 123	813 702 888	892 227 274
2017-12-28	2023-12-25	€ 3 052 000	€ 3 868 000	3 052 000	3 868 000
Total				<u>866 578 731</u>	<u>945 805 809</u>
				Opening balance:	945 805 809
				Final payments/:	-816 000
				Currency effect:	-78 411 077
				Closing balance	866 578 732

Note 6 Financial assets and liabilities

Information on fair values

	2020-12-31	2020-12-31	2019-12-31	2019-12-31
	Reported value	Fair value	Reported value	Fair value
Loans to parent company incl. accrued interest income	874 263 208	955 499 785	953 628 885	1 002 977 216
Accrued administrative fee, parent company	-2 073	-2 073	0	0
Cash and cash equivalents	3 794 737	3 794 737	3 002 037	3 002 037
Bond loans incl. accrued interest expenses	874 255 676	918 958 873	953 627 516	1 002 977 216

Book values are reasonable approximations of fair values in the cases where no fair values are reported for financial instruments above since their terms are short. The information above that relates to Loans and Bond Loans belongs to level 1 in the fair-value hierarchy and have been valued to the latest market value noted on the Luxembourg stock exchange. The Loans to the Parent company are valued at the same value since the parent company loans are pledged as security for the bond loans. The fair value for the loan to the other group company PKO Leasing Sverige AB is estimated using yield curve and margin model.

Structure of maturity for financial debts

	Book value	Maturities up to	Maturities between	Maturities over
	2020-12-31	one year :	and five years	five years
Loans to group companies	866 578 731	816 000	865 762 731	-
Bond loans	863 542 789	-	863 542 789	-

	Book value	Maturities up to	Maturities between	Maturities over
	2018-12-31	one year :	and five years	five years
Loans to group companies	945 805 809	816 000	944 989 809	-
Bond loans	941 962 102	0	941 962 102	-

The amounts relate to contractual non-discounted payments.

For other information concerning risks in financial instruments please refer to the Management report under "Risks and Uncertainties".

Note 7 Accrued income, group companies

	2020-12-31	2019-12-31
Accrued interest income	10 737 006	11 691 882
Accrued administrative fee income	-2 073	0
<i>Total accrued income, group companies</i>	10 734 933	11 691 882

Note 8 Bond loans

<i>Issued</i>	<i>Due for repayment</i>	2019-12-31	2019-12-31	2020-12-31	2019-12-31
		<i>Currency of denomination</i>	<i>Reporting currency (EUR)</i>		
2012-07-25	2022-07-25	€ 49 824 623	€ 49 711 815	49 824 623	49 711 815
2012-09-26	2022-09-26	\$999 541 507	\$999 290 822	813 718 166	892 250 287
Total				863 542 789	941 962 102

Note 9 Parent company

The company is a wholly-owned subsidiary of Powszechna Kasa Oszczednosci Bank Polski Spółka Akcyjna, Warsaw, Poland with corporate identity number 525-000-77-38.

Note 10 Related party transactions

	<u>2020</u>	<u>2019</u>
<i>Cash flow items</i>		
Interest and other payments from parent company	43 484 522	55 496 404
Interest payments from other group companies than the parent company	0	54 617
Repayment of loans from the parent company	0	500 000 000
Repayment of loans from other group companies than the parent company	816 000	816 000
Repayment of bond loan	0	500 000 000
<i>Balance sheet items</i>		
Loans granted to other group companies than the parent company - current assets	816 000	816 000
Loans granted to parent company - long term financial assets	862 710 731	941 121 809
Loans granted to other group companies than the parent company - long term financial assets	3 052 000	3 052 000
Receivable parent company - capital cover guarantee	66 840 996	64 334 542
Accrued income, parent company	10 736 476	11 691 076
Accrued income, other group companies than the parent company	530	806
<i>Profit-and loss items</i>		
Interest income, parent company	43 092 785	44 510 958
Interest income, other group companies than parent company	44 129	54 447
Administration and commission revenues	107 756	110 200
Remunerations to parent company	0	825

Note 11 Proposal for appropriation of profits and losses

The following profit is to be appropriated by the Annual

	<u>2020</u>	<u>2019</u>
General Meeting of Shareholders		
Retained earnings	EUR 0	65 173 277
The profit of the year	EUR <u>5 723 120</u>	<u>-65 173 277</u>
Total profit of the year and retained earnings	EUR 5 723 120	0

The Board of Directors proposes that the retained earnings are appropriated as follows:

To be carried forward	EUR <u>5 723 120</u>	0
	EUR 5 723 120	0

Note 12 Pledged assets and contingent liabilities

	2020-12-31	2019-12-31
Pledged assets		
Loans, group companies	EUR 874 263 208	953 628 885

Note 13 Provisions, deferred tax liability, capital injection

In the beginning of 2018 it was discovered that a strict application of current income tax rules for companies with EUR as their reporting currency, possibly could have the effect that the fluctuations of the exchange rates SEK/EUR during the period between the disbursements and repayments of the intergroup loans are differently taxed than if the same loans had been made by a company with SEK as reporting currency. Due to the doubts relating to taxation of foreign exchange differences on loans granted to the Bank and issue commitments in the territory of Sweden, PKO Finance AB, whose reporting currency is the EUR, applied to the Swedish Council for an advance ruling. PKO Finance AB lends funds obtained from bonds issued to PKO Bank Polski ("Bank") and at the same time recognizes receivables from the loans and liabilities relating to the issue.

Changes in foreign exchange rates have a symmetrical impact on the valuation of such receivables and liabilities, because foreign exchange differences on the valuation of loans granted are matched with the opposite foreign exchange differences on the valuation of liabilities in respect of the bonds issued. According to the individual ruling obtained by PKO Finance AB from the Swedish Council for Tax Rulings (Skatterättsnämnden) on 14 March 2019, a company for which EUR is the reporting currency should tax the EUR/SEK exchange differences on the loans (SEK/EUR) between the maturity date and repayment date. At the same time it is not possible to recognize a tax cost related to foreign exchange differences on the company's liabilities in respect of the bond issue at the maturity date. If the Council's ruling would gain legal force, it would mean that a different approach is applied

in Sweden to companies reporting in EUR compared with companies reporting in SEK (which can also include foreign exchange differences on liabilities in their tax settlements), and this would increase the economic risk and hamper effective hedging of the currency risk.

In the opinion of the Company, such an approach would be contrary to Article 63 of the Treaty on the Functioning of the European Union (TFEU) related to the need to ensure free flow of capital in the EU or Article 49 and 54 of TFEU related to the freedom of business activities.

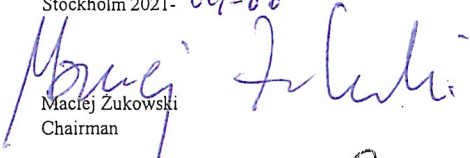
On 3 April 2019, the company appealed to the SAC against the Council's ruling and on 1 July submitted extended arguments to dismiss the case. In its opinion of 23 August 2019, the Swedish Tax Office (Skatteverket) took a negative stance on the company's appeal. The Company sustained its position in the response to the opinion submitted to the SAC

on 25 September 2019. In addition, on 10 October 2019, the Company submitted complementary documents to its appeal in which it emphasized, among other things, the importance of the resolution for companies operating in the territory of Sweden and reporting in euro. On May 4, 2020 the SAC resolved to remove (set aside) the ruling of the Council for Tax Rulings. During 2020 the STA has accepted the company's tax return for 2019. The STA has also accepted the re-assessed tax returns for 2015 and 2016. In all tax returns the company has provided extensive disclosures regarding the above mentioned tax issue and its possible hypothetical effects on the company's taxation.

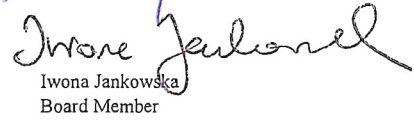
Note 14 Events subsequent to the end of the financial year

There are no reportable events subsequent to the end of the financial year.

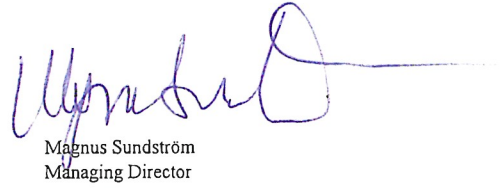
Stockholm 2021- 04-06



Maciej Zukowski
Chairman



Iwona Jankowska
Board Member



Magnus Sundström
Managing Director

Our audit report was issued 2021-
PricewaterhouseCoopers AB

Susanne Sundvall
Authorized auditor