

**Report  
on application by PKO BP SA of corporate governance rules in the year 2007**

prepared in accordance with §29 of the Stock Exchange Regulations and Resolution No. 1013/2007 of the Management Board of the Stock Exchange in Warsaw dated 11 December 2007 concerning defining the scope and structure of the report on application of corporate governance rules by listed companies

On 4 July 2007, the Supervisory Board of the Securities and Exchange Commission in Warsaw S.A, based on its Resolution No. 12/1170/2007, accepted new rules of corporate governance in the form of regulations called "*Dobre Praktyki Spółek Notowanych na GPW*" („Good practice of companies listed on the Stock Exchange in Warsaw”). The new rules of corporate governance became effective on 1 January 2008.

The Bank will take all possible steps to ensure that the recommendations and rules of corporate governance are applied to the widest extent. Where the given rule is either persistently not applied or incidentally breached, the Bank will inform the market about this fact in the manner defined in §29 of Regulations of the Stock Exchange in Warsaw.

Up to the date of publication of this report, the Bank has not informed the public about incident of violation of any specific corporate governance rule defined in the document called „*Dobre Praktyki Spółek Notowanych na GPW*”.

**I. Corporate governance rules applied by PKO BP SA in the year 2007**

In 2007, PKO BP SA complied with all corporate governance rules adopted based on Resolution No. 44/1062/2004 of the Stock Exchange Council dated 15 December 2004 concerning adoption of corporate governance rules by listed entities who are issuers of shares, convertible bonds or senior bonds with priority of conversion into shares admitted to public trading on the official market, except for rules No. 5, 28 and 38, with which PKO BP SA complied partially, and rule No. 20 with which it did not comply at all.

**Rule No. 5:** *Attendance of a shareholder proxy at annual general meeting requires that the proxy's right to act on behalf of the shareholder is documented properly. One should assume that the document in writing, confirming the right to represent the shareholder, complies with appropriate binding laws and does not require any additional confirmations, unless its authenticity or prima facie validity rises doubts of company's management board (upon entering the proxy onto the annual general meeting attendance list) or chairman of the annual general meeting* – was complied with by the Bank partially.

Written authorisation is required, on invalidity penalty, to ensure participation of shareholder proxy at the Annual General Meeting of PKO BP SA and his ability to exercise voting right, issued by authorized persons, in accordance with a copy of appropriate register, or in the case of natural persons – in accordance with the provisions of the Civil Code. The signature on the authorization issued by the shareholder who is a natural person should be confirmed by a notary public. The right to represent the shareholder who is not a natural person should result from a copy of appropriate register presented upon preparation of the list of attendance at annual general meeting (filed as original document or a copy authenticated by a notary public), or alternatively from a sequence of authorizations. The name of the person issuing authorization on behalf of the shareholder who is not a natural person should be included in the current copy of the register appropriate to the given shareholder.

**Rule No. 28:** *The supervisory board should act in accordance with its by-laws which should be made available to the public. These by-laws should provide for establishing at least two committees: audit and remuneration committee. Audit committee should be composed of at least two independent members and of at least one member with qualifications and experience in accounting and finance. The tasks of the committees should be defined in detail in the by-laws of the supervisory board. The committees established by the supervisory board should file with the [supervisory] board annual reports on their activities. The reports should be made available by the company to the shareholders.* – was complied with by the Bank partially.

The Supervisory Board of PKO BP SA acts in accordance with its by-laws. The Bank included the content of the Supervisory Board by-laws on its Internet website. The by-laws of the Supervisory Board provide for the possibility of establishing standing Committees, in particular the Remuneration and Audit Committee, and define their tasks. The internal regulations of the Bank do not require that the Audit Committee is composed of two independent members. The Committee files with the Supervisory Board of the Bank an annual report on its activities within the timeframe that allows accounting for the content of such report in the assessment of the financial position of the Bank.

**Rule No. 38:** *Remuneration of members of management board should be determined on the basis of transparent procedures and policies, after taking into account its incentive character and after ensuring effective and smooth management of the company. Remuneration should match the size of business and reasonably relate to its actual financial results as well as to the scope of responsibility attached to the function held, after taking into account the level of remuneration of management board members of similar businesses on similar market.* – was complied with by the Bank partially.

The procedures and policies used to determine remuneration of the Bank's Management Board Members are transparent. The level of remuneration is adjusted to the provisions of the act dated 3 March 2000 concerning remuneration of persons managing certain corporate entities (Journal of Laws No. 26, item 306 with subsequent amendments). Given the above, the level of remuneration is not of incentive nature and does not relate to the size of the Bank's business, does not reasonably relate to the financial results of the Bank, does not relate to the scope of responsibilities attached to the Management Board Member function and does not account for the level of remuneration of management board members of other banks.

**Rule No. 20:**

- a) *Independent persons should account for at least half of the members of the supervisory board. Independent members of the supervisory board should be free from any relations with the company, its shareholders or employees, as said relations could have a material impact on the ability of such independent members to take unbiased decisions;*
- b) *Detailed criteria of independence should be defined in the company's articles of association;*
- c) *Without the consent of at least one independent member of the company's supervisory board, no resolution should be passed in the following matters:*
  - *any type of allowance or benefit granted by the company or its related parties to supervisory board members;*
  - *approval to entering by the company or its related entity into a significant contract with the company's related party, member of the company's supervisory or management board or with entities related to said persons;*
  - *appointment of the company's certified auditor.*
- d) *where one shareholder holds a block of shares giving the right to over 50% of the total number of votes, the supervisory board should be composed of at least two independent members, including the independent chairman of the audit committee, if such committee has been established.*

– was not complied with by the Bank.

Provisions of the Bank's Articles of Association and of other internal regulations of the Bank do not justify the institution of independent Supervisory Board Member

## **II. Annual General Meeting of the Bank, its manner of functioning and fundamental powers; the rights of shareholders and the manner of their execution**

Annual General Meeting of PKO BP SA is convened as ordinary or extraordinary meeting in accordance with the provisions of the Code of Commercial Companies and the Bank's Articles of Association, and based on the policies defined in the by-laws of the Annual General Meeting (hereinafter "the AGM").

The fundamental powers of the AGM, apart from other matters defined in the binding laws, include adopting resolutions concerning the following matters:

- 1) appointment and dismissal of Supervisory Board Members;
- 2) approval of by-laws of the Supervisory Board,
- 3) determining the manner of buyout of shares and the amount of consideration for the shares subject to buyout,
- 4) creation and liquidation of special funds established from net profit appropriation,
- 5) disposal by the Bank of property items or perpetual usufruct right to property, from which the Bank conducts its business,
- 6) issuance of convertible bonds or other instruments giving the right to acquire or take up the Bank's shares.

Allowed to participate in the Annual General Meeting of the Bank are beneficiaries of rights attached to registered shares, as well as pledgees and usufructuaries having voting rights, who have been entered in the Register of Shares at least one week prior to holding the AGM, or holders of bearer shares, if they deposit with the Bank, at least one week prior to the date of the AGM at the latest, registered depository certificates issued by the entities maintaining the securities accounts and do not collect them prior to the closing of the Annual General Meeting.

The shareholder who is a natural person may participate in the AGM, exercise his voting right in person or by proxy. The shareholder who is not a natural person may participate in the AGM and exercise his voting right through a proxy authorized to file statements of will on his behalf, or by proxy.

To be valid, the authorisation shall be executed in writing and attached to the minutes of the AGM. The signature on the authorisation issued by the shareholder who is a natural person should be authenticated by a notary public. The right to represent the shareholder who is not a natural person should result from a copy of appropriate register presented at the time of the preparation of the AGM attendance list (filed as original or a copy authenticated by a notary public), or alternatively from a sequence of authorisations. The name of the person/ persons issuing authorisations on behalf of the shareholder who is not a natural person should be included in the current copy of appropriate register of the given shareholder.

Management Board Member or Bank employee may serve as proxy at the AGM of the Bank.

Drafts of resolutions proposed by the AGM and other important materials are presented to the shareholders together with the justification and opinion of the Supervisory Board before the AGM, within the timeframe that allows reading them and preparing their assessment.

The Bank's shareholder has the right to file with the Chairman of the AGM proposals for changes or supplements to drafts of resolutions included in the AGM agenda, and these should be drafted in writing, separately for each resolution draft, and should include justification. Such proposals, after being presented to the AGM by the Chairman, are put to the vote. The AGM participant requesting to include his objections towards the given resolution in the AGM minutes may concisely justify his standpoint.

Removing from the AGM agenda or desisting, at the request of the shareholders, from further discussing the matter included in the AGM agenda requires that the AGM resolution is adopted by the majority of  $\frac{3}{4}$  votes, after prior consent of all those shareholders present at the AGM who applied for including the matter in the agenda.

Resolutions of the AGM are adopted by an absolute majority of votes, unless the binding laws or the Articles of Association of the Bank provide otherwise.

The AGM adopts resolutions by way of open vote, with the proviso that votes by secret ballot are ordered in the following circumstances:

- 1) elections,
- 2) applications for dismissal of members of the Bank's Management or Supervisory Board or liquidators,
- 3) applications for bringing the Bank's liquidators or members of the Management or Supervisory Board to justice,
- 4) in personal matters,
- 5) on demand of at least one shareholder present or represented at the AGM,
- 6) in other cases defined in binding law regulations.

A shareholder may not, either personally or by proxy, or while acting in the capacity of a proxy of another person, vote on resolutions concerning his liability towards the Bank on whatever account, including the acknowledgement of the fulfillment of his duties, release of any of his duties towards the Bank, or any dispute between him and the Bank.

Shareholders have the right to ask questions, through the Chairman of the AGM, to the Members of the Bank's Management or Supervisory Boards, the Bank's auditor or the persons whose presence at the AGM is considered indispensable by the Management or Supervisory Boards of the Bank.

For each of the agenda point, each shareholder has the right to one own speech and one reply. Shareholders may, during the course of discussion on each of the agenda points, apply for closing the list of speakers or closing the discussion on the given agenda point.

### **III. Composition and the manner of functioning of the authorities of PKO BP SA and their committees**

#### **1. Supervisory Board**

The Bank's Supervisory Board is composed of 6 to 11 members appointed for a joint term of office of three years. Members of the Supervisory Board are appointed and dismissed by the Annual General Meeting.

As at 31 December 2007, the composition of the Bank's Supervisory Board was as follows:

1. Marek Głuchowski – President of the Supervisory Board
2. Urszula Pałaszek – Vice-president of the Supervisory Board
3. Tomasz Siemiątkowski – Secretary of the Supervisory Board
4. Maciej Czapiewski – Member of the Supervisory Board
5. Jerzy Michałowski – Member of the Supervisory Board
6. Agnieszka Winnik-Kalemba – Member of the Supervisory Board

Supervisory Board acts based on the by-laws decided by the Supervisory Board and approved by the AGM. Meetings of the Supervisory Board are convened at least once a quarter.

Supervisory Board adopts resolutions by an absolute majority of votes with the presence of at least half of the Members, including the President or Vice-president of the Supervisory Board, except for resolutions concerning those matters that are required to be accepted by, apart from

the quorum indicated, the qualified majority of 2/3 of total votes. Excluded from the vote are those members of the Supervisory Board to whom the given voted matter relates.

In 2007, the following three Committees operated within the Supervisory Board of PKO BP SA: Audit Committee, Informatization and Strategy Implementation Committees.

Each Committee is composed of at least three members chosen by Members of the Supervisory Board from within its own circle.

Committee Meetings are convened as ordinary meetings not less often than once every two months. Meetings are convened by the Committee Chairman or Supervisory Board Member.

In the extraordinary mode, Committee meetings are convened by the President of the Supervisory Board on his initiative or at the request of the Supervisory Board Member or the Bank Management Board. Minutes are prepared from the meetings and the Committee Chairman presents the Supervisory Board, at its next meetings, with resolutions, conclusions and recommendations.

Each Committee presents the Bank's Supervisory Board with an annual report on its activities, with the proviso that the Audit and Informatization Committees are required to file their reports within the timeframe that allows the Bank to account for the content of those reports in the process of annual assessment of the financial position of the Bank.

**Supervisory Board Audit Committee** was established in order to exercise permanent supervision over the financial audit of the Bank and of the capital group. Included in the tasks of the Audit Committee are in particular:

- 1) overseeing appropriate implementation of the financial reporting policies of the Bank,
- 2) monitoring the work of internal auditors of the Bank,
- 3) presenting the Supervisory Board with recommendations as regards remuneration for the Bank auditors,
- 4) review of periodic and annual financial statements of the Bank (separate and consolidated), with special attention being paid to the following issues:
  - changes in binding accounting norms, policies and practices;
  - major areas of professional judgment;
  - significant post-audit adjustments;
  - statements relating to going concern;
  - compliance with binding accounting policies,
- 5) discussing post-audit issues, objections and doubts,
- 6) analysis of management letter issues forwarded by certified auditors and management responses to those issues,
- 7) preparation of recommendations to the Supervisory Board, which relate to assessment of management Board conclusions concerning profit appropriation (including in particular dividend policy) and issuance of securities,
- 8) review of management accounting system,
- 9) advisory and assessment services to the Supervisory Board concerning the financial audit of the Bank.

**Bank Informatization Committee** was established with a view to supervising information and telecommunication systems at the Bank, including implementation of the Integrated Information System.

As regards monitoring the functioning of the IT and telecommunication systems at the Bank, including monitoring the implementation of the integrated IT system, the following are included in the scope of activities of the Bank's Informatization Committee:

- 1) issuing opinions on the strategic directions of informatization at PKO BP S.A.,

- 2) analysis of the status of works aimed at implementation at the Bank of significant products and services supported by IT applications,
- 3) issuing opinions on the IT priorities adopted by the Bank,
- 4) issuing opinions on the principles of cooperation between the IT and other functions at the Bank as regards realization of key business processes,
- 5) feasibility study of IT projects relating to new applications with the budget of more than PLN 5 million,
- 6) issuing opinions on annual investment plans relating to the IT function,
- 7) analysis of the progress of works on implementation of strategic IT solutions,
- 8) legitimacy analysis of the use of outsourcing services in the IT area
- 9) issuing opinions on significant IT infrastructural projects,
- 10) issuing opinions on the model of organization of the IT function at the Bank.

**Strategy Implementation Committee** was established in order to exercise permanent supervision over implementation of the *Strategy of PKO BP SA for the years 2007-2012*.

Included in the scope of activities of the Committee concerning implementation of the Bank's strategy are, in particular, the following:

- 1) analysis of the progress of work relating to implementation of strategic initiatives, the realization of which is prerequisite to meeting the objectives defined in the Bank's Strategy,
- 2) analysis of the results of implementation of strategic initiatives, proposing supplementary or correcting measures,
- 3) issuing opinions on periodic reports on realization of the Bank's Strategy,
- 4) presenting to the Supervisory Board of the Bank recommendations for the activities required to be taken by the Bank to achieve objectives defined in the Bank's Strategy, where its realization is endangered,
- 5) discussing all contentious issues and doubts resulting from the analysis of the process of implementation of the Bank's Strategy,
- 6) rendering advisory and opinion-forming services to the Supervisory Board of the Bank as regards implementation and realization of the Bank's Strategy.

## **2. Management Board of the Bank**

The Management Board of the Bank is composed of 3 to 9 members appointed by the Supervisory Board of the Bank for a joint term of office of three years. Appointment of two members of the Management Board, including President of the Management Board, requires approval by the Polish Commission for Banking Supervision.

As at 31 December 2007, the composition of the Management Board of the Bank was as follows:

1. Rafał Juszczak – President of the Management Board,
2. Berenika Duda-Uhryn – Vice-president of the Management Board,
3. Robert Działak – Vice-president of the Management Board,
4. Mariusz Klimczak – Vice-president of the Management Board,
5. Wojciech Kwiatkowski – Vice-president of the Management Board,
6. Aldona Michałak – Vice-president of the Management Board,
7. Adam Skowroński – Vice-president of the Management Board,
8. Stefan Świątkowski – Vice-president of the Management Board.

The manner of functioning of the Management Board is defined in the by-laws decided by the Management Board and approved by the Supervisory Board.

Management Board makes decisions in the form of resolutions, which are passed by an absolute majority of votes of those present at the Management Board Meeting. In the case of a voting tie, the President of the Management Board has the casting vote. For all matters outside the scope of ordinary Bank business to be effected, resolution of the Management Board is required.

In 2007, the following Committees established by the Bank's Management Board were operational, with Members of the Management Board acting as members of these Committees:

- 1) Asset Liability [Management] Committee (the „ALCO“)
- 2) Credit Committee
- 3) Committee for the Project of Integrated IT System
- 4) Steering Committee for the Integrated IT System
- 5) Steering Committee for the Branch Modernization Program (operated until 31 December 2007)
- 6) Steering Committee for the activities adapting the Bank to the requirements of the Capital Accord Directive and the requirements of IAS 39
- 7) PKO BP SA Corporate Governance and Commercial Supervision Committee (operated until 31 December 2007)

#### **IV. Basic characteristics of the Bank's internal control and risk management systems used in the process of preparation of financial statements**

The Bank operates the internal control system which is an element of the Bank management function, and which is composed of the following items: control mechanisms, functional internal control and internal audit (institutional control).

Internal control system covers the entire activities of the Bank. The objective of the internal control system is to support decision processes which contribute to ensuring the following: the Bank's effectiveness and efficiency, truth and fairness of its financial reporting and the compliance of Bank's operations with binding laws and internal regulations of the Bank.

Control mechanisms cover policies, limits and procedures relating to operating activities of the Bank and to the activities aimed at verifying the correctness of the tasks performed, such as preparation of the financial statements. These are embedded in both the internal regulations and the Bank's IT system.

Functional internal control function is exercised on a permanent basis in all organisational units and in the Head Office of the Bank in the following manner:

- at the stage of legislative works, by way of defining in the internal regulations the manner and mode of realization of tasks, and appropriate control activities which guarantee the correct course of their realization,
- by employees in the course of their activities concerning the scope of business of organisational teams and units,
- at the stage of verification, by employees holding managerial functions or persons authorised by said employees, by way of verification of the correctness of the tasks carried out, and in particular of their compliance with binding laws and regulations, internal regulations of the Bank and prudence norms.

Internal audit function is performed by the Internal Audit Department. The objective of the Internal Audit Department is to deliver to the Management and Supervisory Boards of the Bank independent and objective information and assessments, especially about the following:

- adequacy and effectiveness of the internal control system, including the effectiveness of control mechanisms,

- Bank management system, including the effectiveness of business risk management,
- truth and fairness, completeness and the current status of the Bank's financial reporting and management information,
- quality of internal regulations and functionality of accounting and reporting systems,
- compliance with binding laws and regulations and internal regulations of the Bank.

The objective of audit function is also to indicate directions for the activities that serve to enhance the quality and effectiveness of realized tasks, including by way of briefings or instructions on matters within audit scope.

Audit plan is developed based on, among others, the results of prior audits, information concerning functioning of the Bank, risks identified in individual areas of the Bank's business and in the processes realized, including in the process of the preparation of the financial statements.

The control and risk management (in respect of the process of preparation of the financial statements) systems used are based on control mechanisms embedded in the functionality of the reporting systems, on the on-going verification of compliance with the books of accounts and other documents underlying the financial statements and with the binding laws concerning accounting principles and financial statements preparation.

The process of the preparation of the financial statements is subject to cyclical multi-level functional control, in particular concerning the correctness of accounting reconciliations, merit-based or substantial analysis or truth and fairness of financial information. In accordance with the internal regulations, the financial statements are accepted by the Management of the Bank and the Audit Committee established by the Supervisory Board of PKO BP SA.

Information included in the financial statements is prepared in accordance with International Financial Reporting Standards, after taking into account all data available.

Information concerning objectives and risk management policies as well as quantitative information relating to individual risk types is included in annual and periodic financial statements. The information referred to above comprises:

- 1) credit risk (including the risk of credit concentration),
- 2) market risk (interest rate, currency, derivatives and financial institutions credit risks as well as liquidity risk),
- 3) operating or business risk,
- 4) capital adequacy.

On an annual basis, in a separate non-financial reporting document, disclosed is the full scope of information relating to capital adequacy, in accordance with Resolution No. 6/2007 of the Commission for Banking Supervision.