



**2005**  
**Annual Report**  
**of**  
**ING Bank Śląski S.A.**  
**Capital Group**

**Katowice, April 2006**

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## **BANK MANAGEMENT BOARD**

### **Status as of 31 December 2005**

Brunon Bartkiewicz	– Chief Executive Officer
Krzysztof Brejda	– Executive Vice-President
Ian Clyne	– Executive Vice-President (as of 1 March 2005)
Grzegorz Cywiński	– Executive Vice-President
Donald Koch	– Executive Vice-President
Michał Szczurek	– Executive Vice-President
Maciej Węgrzyński	– Executive Vice-President
Benjamin van de Vrie	– Executive Vice-President

## **SUPERVISORY BOARD**

### **Status as of 31 December 2005**

Andrzej Wróblewski	– Chairman
Cornelis Leenaars	– Deputy Chairman
Jerzy Rokita	– Secretary
Anna Fornalczyk	– Member (as of 9 June 2005)
Hans van der Noorda	– Member (as of 9 June 2005)
Marcus van der Ploeg	– Member (as of 9 June 2005)
Igno van Waesberghe	– Member (as of 9 June 2005)
Lech Węclewski	– Member

## Chairman's Statement

Ladies and Gentlemen,

On behalf of the Supervisory Board, I am pleased to present you with the results of ING Bank Śląski for the year 2005.

Let me begin by noting that, in accordance with the resolution passed at the General Shareholders Meeting, as of 9 June 2005, our Supervisory Board is composed of eight members, including four independent ones. With such a representation of independent members on the Board, we will be able to take adequate care of the interests of minority shareholders in the Bank's activity. Their number increased following the sales of approximately 13% of ING Bank Śląski S.A. shares by ING Group in March 2005, to fulfil the recommendations of the banking supervision authorities.

Over 2005, the Supervisory Board continued to keep track of the commercial and financial performance of ING Bank Śląski S.A., and closely followed the progress of works related to the reorganisation and expansion of the Bank's infrastructure. Being regularly updated on the status of the initiatives, we saw that the project works ran according to schedule, and the key deliverables were achieved. What is particularly noteworthy are the results of projects aimed at simplifying procedures for offering of key products, further automation of the operating area and successful implementation of a new IT technology in the entire branch network. All of these initiatives will contribute to further improvement of customer service quality and efficiency of our operations.

It also gave us great satisfaction to see that ING Bank Śląski S.A. successfully continued to improve and reinforce its position on the Polish banking market. In December 2005, the total assets of the Capital Group of the Bank amounted to PLN 42.1 billion, an increase of 1/5 over the end of the previous year. For yet another year in a row, ING Bank Śląski S.A. was the fastest-developing institution among the largest commercial banks in Poland.

Gains in deposits value were the premier source of expansion of ING Bank Śląski S.A. With attractive changes to the product offer, easier access to the Bank, and extensive marketing activities, the deposit volume as at the end of 2005 reached PLN 30.7 billion, up by more than 16% on a year earlier.

In 2005, ING Bank Śląski S.A. was challenged by lack of clear effects of the actions taken on the credit market and a relatively limited growth of new lending. At the end of 2005, the credit receivables of the Bank totalled PLN 9.9 billion, down by approximately 5% from December 2004. The continuing downward trends in terms of the credit exposure value in 2005 was the main reason behind the stabilisation of the result on core operations of the Capital Group of ING Bank Śląski S.A., which remained at the same level as a year earlier.

In 2005, the Capital Group of ING Bank Śląski S.A. earned net profit of PLN 549.5 million compared with PLN 399.0 million a year earlier. The growth was mainly aided by a one-off factor, whereby the level of costs due to impairment loss was

adjusted to the condition of the credit portfolio, and to the effective regulations in terms of credit risk management.

At the request of the Management Board, we will recommend that the General Shareholders Meeting pass a resolution approving the dividend of PLN 27.5 per one share. We hope that the shareholders of ING Bank Śląski S.A. will find that an adequate return on their investment. I would like to stress at the same time that the dividend payout will neither lower the security of operations of ING Bank Śląski S.A. nor reduce its development potential.

On behalf of the Supervisory Board, I would like to assure you that ING Bank Śląski is well-prepared for further development, and will strive to fulfil its mission and key strategic objectives. The consistent re-engineering of organisational structure and procedures; effective cost management and tailoring of the product and service offer to the preferences of individual clients will provide ING Bank Śląski with a sharp competitive edge. At the same time they will also enable further improvement of the commercial and financial performance of the Bank, thus allowing it to maintain the upward trend in terms of the company's value.

Herewith I would like to thank the Management Board and all employees of ING Bank Śląski for their efforts last year to reshape the organisation and deliver this performance. I want to assure our Shareholders that in all our efforts we are guided by unwavering commitment to increase the value of our Bank.

## Chief Executive's Review

Dear Shareholders,

2005 was yet another significant year for the development of ING Bank Śląski S.A. and reinforcement of its position among the leaders of the Polish banking market.

It was predominantly a period of major qualitative changes in the Bank's operations going forward to put the idea of a "Customer-Friendly Bank" into practice. In my opinion, the most important changes in that area are the ones invisible to an outsider, notably the changes in the area of operations and sales support. As part of numerous projects, which covered most of the core areas of the Bank's operations, we have thoroughly analysed the processes related to the sales of products and services to find ways of simplifying, automating and centralising them, whenever possible. We have defined new solutions for those processes striving, first of all, for service excellence and improved efficiency of our operations. Throughout 2005, we were working on a process, which we had been preparing for several years, namely the replacement of the IT platform in our branches with state-of-the art technology. The process was successfully completed, and it will not only facilitate the works related to the improvement of our offer and the launch of new products and services, but it will also aid processes related to the management of our IT infrastructure. We have terminated the revisualisation process at Bank branches with success, which was connected with their modernisation in many branches, improving the comfort of servicing our Clients. Early 2005, we introduced a new incentive system, which is closely related to the performance of the Bank's strategic objectives. We also commenced works on a new remuneration system.

In 2005, ING Bank Śląski S.A. was also a visible player on the market who dynamically developed in a number of important areas, such as: retail deposits, credit cards, investment funds, and EU credit facilities. Our biggest accomplishment in that respect is, in my opinion, the successful implementation of our strategy for acquiring deposits from retail clients, which was adopted mid-2004. Continued works to enhance our deposit offer, as well as adequate and as wide as possible communication of newly introduced interesting changes to our clients proved fruitful, as they helped add more than four billion zlotys to the funds deposited by households in the accounts of our Bank. With these results, the Bank became one of the top three largest banks in which Polish households deposit their savings.

2005 did not, however, see the reactivation of lending at ING Bank Śląski S.A. Although we were able to increase our credit exposure in terms of some key products, such as PLN mortgages, EU credit facilities and towards certain groups of clients (for example, corporate clients of mid-sized and large corporates segment), at the end of 2005 the Bank's lending was lower than a year earlier. The level of lending activity at ING Bank Śląski S.A. was determined both by the market situation, which was characterised by a relatively low demand for loans from businesses, and by the credit policy pursued by the Bank, including lack of FX-loans for individual clients and the principles adopted by the Bank in terms of credit risk assessment. I would like to emphasise that boosting of lending, which would enable us to better match the assets

and liabilities on our balance sheet and use the funds acquired from our clients more efficiently, remains high on the agenda of ING Bank Śląski S.A.

Net profit generated by the Capital Group of ING Bank Śląski S.A. in 2005 reached PLN 549.5 million compared with PLN 399.0 million earned a year earlier. With decreasing interest rates, fiercer competition on the market and a relatively low level of lending at the Bank, the result on banking activity totalled PLN 1,649.4 million, so it was similar to the result generated in 2004.

The year 2005 was yet another year of stringent cost discipline for the Capital Group of ING Bank Śląski S.A. The cost containment programmes we completed enabled us to make considerable cost savings. I would like to stress at this place that the pursuit of the long-term goals of the Bank had priority over the short-term benefits from the cost reductions. As considerable outlays were made on the development and reorganisation of our organisation, the Bank's Group saw some increase of its operating costs.

The overall very good financial result delivered by the Capital Group of ING Bank Śląski S.A. in 2005 was largely determined by the adjustment of the impairment loss-related costs to the current condition of the Bank's credit portfolio. In view of the continued improvement of the credit risk management quality at the Bank, considerable incomes generated upon restructuring of the loss loans portfolio transferred to the off-balance sheet records and better financial standing of the clients, in 2005 the balance due to loss impairment was positive and amounted to PLN 118.0 million compared with expenditure of PLN 151.9 million a year earlier.

At the end of 2005, which was a good year both for the Polish economy and for ING Bank Śląski S.A., we are optimistic about the future. The restructuring process, which has been conducted for several years now, put the Bank in a good position so that it will be able to take part in the expected economic growth. We are planning to expand our commercial activity dynamically, improve the efficiency of our operations, and systematically raise the value of our institution.

I would like to thank our Clients for their loyalty and I hope that in the future they will also appreciate our efforts aimed at establishing long-lasting relations to the mutual satisfaction of both parties. Thanking the Shareholders for their trust in ING Bank Śląski S.A., I would like to assure them that we will continue to strive for an on-going growth of the Bank's value.

Let me also gratefully acknowledge the hard work and commitment of the employees whose knowledge and skills are a precious asset of the Bank.

On behalf of the Management Board, I would like to thank the Supervisory Board for our close and effective co-operation and their support of our activities.

## **Supervisory Board's Report on Operations of the Capital Group of ING Bank Śląski S.A. in 2005**

In 2005, the Capital Group of ING Bank Śląski S.A. earned net profit of PLN 549.5 million compared with PLN 399.0 million in 2004. The following factors contributed to its growth:

- Stabilisation of income on core operations – in 2005, the result on banking operations totalled PLN 1,649.4 million compared with PLN 1,661.3 million a year earlier.
- Sustenance of cost discipline – in view of considerable outlays related to the reorganisation of the institution, the total costs of the Bank's capital group amounted to PLN 1,109.4 million, up by 8.2% from 2004.
- Generation of a positive balance in terms of impairment loss – in 2005, the improvement of the macro-economic environment and reinforcement of functions related to the credit risk management resulted in a significant positive balance of impairment losses. It amounted to PLN 118.0 million, whereas a year earlier the Bank disclosed in its income statement a negative provisioning balance of PLN 151.9 million.

Therefore, the major determinant of the Bank's net result in 2005 was a one-off gain related to the adjustment of the risk costs to the current good condition of the Bank's credit portfolio, positive results of restructuring of the credit portfolio moved to the off-balance sheet records and introduction of new standards of credit risk management.

The Supervisory Board positively evaluates the initiatives taken in 2005 in an effort to re-organise the institution and strengthen the sales forces. ING Bank Śląski S.A. completely transformed its operational environment by implementing a new centralised model of operational service and replacing the IT environment in all of its branches. The Bank also reviewed the processes related to the sales of key products both to retail and corporate clients, in a bid to simplify and standardise them; next, target solutions were defined in that regard, and actions were taken to gradually implement them. All of these changes should help improve the operational efficiency and competitive edge of the Bank in terms of its offer and quality of customer service.

In 2005, ING Bank Śląski S.A. has also produced good results in its expansion on the deposit market. In December 2005, the volume of funds deposited in the accounts of ING Bank Śląski S.A. reached PLN 30.7 billion, up by PLN 4.3 billion. It was one of the best results among the Polish banks in terms of deposit acquisition, which helped the Bank cement its position on the market.

While giving a positive opinion on the performance of ING Bank Śląski S.A. in 2005, the Supervisory Board uphold their standpoint expressed in their 2004 report on the Bank's operations where it was stated that the Bank needed to boost its lending. The Bank has accumulated adequate funds that should enable it to develop lending dynamically, both on the retail and corporate market. Credit activity is a crucial element in establishing long-lasting and valuable relationship with the clients, and should therefore become one of the main factors in the improvement of the Bank's financial results in the future.

In the opinion of the Supervisory Board, the development strategy, which has been consistently followed over the last few years, provides a solid foundation for ING Bank Śląski S.A. to benefit from the expected economic growth, develop its commercial activity and improve its financial results.

## Polish Economy in the Years 1999–2005

Specification	1999	2000	2001	2002	2003	2004	2005
(%) GDP growth	4.1	4.0	1.1	1.4	3.8	5.4	3.2
Budget Deficit (% of GDP)	-2.2	-2.0	-5.3	-5.0	-4.5	-3.9	-3.1
Money Supply 3M (in PLN billion)	268.9	300.8	328.4	321.6	339.8	369.5	412.3
Increase of Industrial Output (%)	4.4	7.1	-0.2	1.5	8.7	12.3	4.0
Inflation (CPI) measured Dec./Dec. (%)	9.8	8.5	3.6	0.8	1.7	4.4	0.7
Unemployment Rate (%)	13.1	15.1	17.5	18.0	20.0*	19.1*	17.6
PLN/USD exchange rate (year-end)	4.1483	4.1432	3.9863	3.8388	3.7405	2.9904	3.2348
PLN/EUR exchange rate (year-end)	4.1689	3.8544	3.5219	4.0202	4.7170	4.0790	4.0254
3M WIBOR (year-end)	19.20	19.45	11.91	6.87	5.60	6.64	4.60

\* Upon the inclusion of the number of individual farmers pursuant to the results of the 2002 National Census of Population and Households and the 2002 General Census of Agriculture.

## ING Bank Śląski S.A.: Abbreviated Information concerning the Financial Results of Capital Group for the Years 2004– 2005

	31.12.2005	31.12.2004	Growth rate (2005/2004)
Net total assets in PLN million	42,126.9	35,473.1	118.8
Liabilities to customers in PLN million	32,823.6	27,638.3	118.8
Loans and advances to customers in PLN million	9,902.9	10,407.9	95.1
Financial assets at fair value and investment financial assets in PLN million	17,078.2	11,661.4	146.5
Off-balance sheet liabilities in PLN million	128,753.8	114,770.8	112.2
Bank's equity in PLN million	2,999.2	2,762.1	108.6
Result on banking activity in PLN million	1,649.4	1,661.3	99.3
Total costs <sup>1</sup> in PLN million	1,109.4	1,025.2	108.2
Gross profit in PLN million	705.8	489.0	144.3
Income tax in PLN million	139.4	79.0	176.5
Net profit in PLN million	549.5	399.0	137.7
Solvency ratio (%)	18.6	15.7	
Gross profit/Total costs (%)	29.1	21.8	
Net profit/Net total assets (%)	1.3	1.1	
Net profit/Proprietary capital and equity (%)	18.3	14.4	
Total costs/Result on banking activity (%)	66.2	62.6	
Profit per share in PLN	42.23	30.67	138.6

<sup>1</sup> Operating costs with depreciation.

## I. POLISH ECONOMY IN 2005

### Major Economic Trends

The period of the economic boom that resulted from dynamically growing demand due to the Poland's accession to the European Union was followed by a slowdown of the economic growth early 2005. Compared with high growth rate observed in the first half of the previous year, the economic growth rate in Poland over the first half of 2005 was at 2.4%. In the second half of the year, the Polish economy sped up a little. Courtesy of favourable trends observed in terms of domestic demand, the economic growth rate reached 3.9%, and the Gross Domestic Product went up by 3.2% over the entire 2005. The rate of development observed in Poland in 2005 was higher than the average for all EU Member States, however, it was lower than the average development rate recorded for the new Members.

The growing share of domestic demand in the economic growth resulted mainly from the investment outlays, which kept going up over the last few months. On the whole, the gross outlays on non-current assets for the whole of 2005 were 6.2% higher than a year earlier. By contrast, consumer demand grew at a slightly slower pace; nevertheless, it must be noted that the renovation relief, which was in effect until the end of the year, and the growth of salaries in the last quarter made the consumer demand in 2005 higher by 2.4% than in 2004.

Good performance in terms of economic growth was also helped by positive trends in the area of foreign trade. Still, the contribution of net exports to development kept shrinking, and it is estimated that on the whole net exports contributed 1.3% percentage point to the economic growth rate over the entire 2005.

In 2005, the total volume of sales abroad in EUR was nearly 1/5 higher than a year earlier. The imports were up by almost 13%. The fact that the high growth rate of exports continued for yet another year, despite the appreciation of the Polish currency, proved high competitiveness of Polish companies.

In 2005, Poland's current-account deficit was EUR 3.9 billion, down by EUR 4.5 billion over the last year. Apart from the decrease of the foreign trade deficit, the current-account deficit was also helped by the surplus in the trade in services and growth of current transfers.

Considering the slower growth rate of revenue from overall activity compared with the growth of the corresponding tax-deductible costs, in 2005 we observed a deterioration of basic financial ratios of companies. In 2005, some 76.0% of all companies disclosed net profit in their financial statements (versus 77.4% year earlier). The gross profit margin ratio totalled 4.9% (versus 6.0% in the last year). By contrast, financial liquidity of companies went up – some 42.7% of all companies revealed current ratio above 20%, up from 39.9% a year earlier.

The economic revival translated into job growth. At the end of December 2005, the number of unemployed totalled 2,773,000, down by 7.6% from a year earlier. In

consequence, the jobless rate went down to 17.6% (from 19.1% in December 2004). Despite the improvement on the labour market, the businesses continued to show little propensity to increase salaries. Due to the growth observed in the last quarter of 2005, the mean monthly pay in real terms in the enterprise sector gained 1.2% on a year-to-year basis (in 2004, it was 0.8%).

The impact Poland's accession to the European Union had on the price rises slowly diminished. In December 2005, the prices were 0.7% higher than a year earlier (due to deflation observed in the last two months of the year, among other things). The decrease in inflation level resulted from the stabilisation of food prices and strong PLN, which counteracted the rise in petroleum prices in global markets. At the same time, the base inflation ratios level showed that there were no threats in Poland that would suggest an increase of inflationary phenomena in the future.

After a period of strengthening observed in the first months of the year, the PLN exchange rate to the major currencies remained stable over the rest of 2005. Polish currency benefited from good results in foreign trade, inflow of foreign capital and EU subsidies. It must be noted that the PLN exchange rate to base currencies was affected by the trends taking place on the global markets, i.e. the continuing appreciation of USD against EUR in view of positive news on the American economy. Throughout 2005, the PLN gained 1.3% to EUR, and lost 8.2% in relation to USD. The foreign exchange rates for the Polish currency were as follows:

	31.12.2004	31.12.2005
PLN/USD	2.9904	3.2348
PLN/EUR	4.0790	4.0254

The positive tendencies characterising the domestic economy in 2005 were positively reflected in the state budget. The inflows from the income tax, the VAT, profits and dividends, which were considerably higher than a year earlier, warranted growth of budget incomes to PLN 180.4 billion. Budget expenditures closed at PLN 207.9 billion. As a result, in 2005, the budget deficit totalled PLN 27.5 billion, down by 33.6% from a year earlier.

### Monetary Policy

In the period from March to April 2005, there were two cuts of NBP interest rates (by 100 base points in total) by the Monetary Policy Council (MPC). The interest rates were cut in an effort to enhance the risk balance for future inflation. In April, the interest rate cut coincided with the change of the Council bias from "soft" to "neutral". At the end of June 2005, based on information indicating a considerable slow-down of the economic growth rate and the evaluation of the risk balance for future inflation, the Monetary Policy Council made another cut (by 0.50 p.p.) and changed to soft bias again. Between July and August, the MPC made two further rate cuts (by 0.50 p.p. altogether). Thus, at the end of December 2005 the interest rates were as follows:

- reference rate – 4.50%,
- rediscount rate – 4.75%,
- lombard rate – 6.00%,
- deposit rate – 3.00%.

The decrease of the official interest rates was followed by the market rates. As a result, WIBOR 3M went down from 6.64% in December 2004 to 4.60% at the end of 2005.

## **Banking Sector**

2005 was a very good year for banks operating in Poland. The improved financial standing of the society at large resulted in growing demand for banking services; the quality of credit portfolios continued to improve, while the banks' profits kept growing.

After years of stagnation, the activity of banks increased considerably in 2005. In December 2005, the assets of the Polish banking sector totalled PLN 589.2 billion, up by 9.0% from the end of 2004.

Along with the decrease in unemployment level and increase of pay in the businesses sector, the households savings accumulated in bank accounts started slowly to gain. At the end of December 2005, deposits and long-term liabilities<sup>2</sup> of households totalled PLN 223.2 billion, up by 7.8% from the end of 2004. Deposits of institutional clients<sup>3</sup> reached PLN 143.5 billion, up by 18.8% from December 2004. These figures were, on the one hand, a sign of good standing of businesses, while, on the other hand, they were a proof of the continuing low investment activity of companies.

At the same time, the lack of visible interest in investments affected lending to institutional clients, which - at the end of December 2005 - amounted to PLN 156.3 billion, similar to the level recorded at the end of 2004. Credit receivables of the banking sector from households totalled PLN 141.3 billion (up by 22.4% from December 2004). Increase was observed primarily in terms of debts due to housing loans, cash loans and credit card debts. As regards the housing loans, following the appreciation of PLN early in the year and considerable differences between the interest rates of PLN loans versus FX-loans, the clients tended to prefer loans in foreign currencies, which accounted for some 80% of housing lending growth.

The trend of credit portfolio improvement observed in 2004 continued in 2005. The share of default loans in credit receivables from the non-financial sector went down from 15.6% at the end of 2004 to 10.8% in December 2005. Apart from better financial standing of borrowers, the improvement was caused by the application of the International Accounting Standards (IAS 39) by the largest banks for the assessment of the credit portfolio.

According to preliminary estimates, the banking sector netted PLN 9.2 billion versus PLN 7.1 billion a year earlier.

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<sup>2</sup> According to preliminary information total deposits including those above 2 years.

<sup>3</sup> Total deposits for the following entities: enterprises, non-monetary financial institutions, non-profit institutions serving households, local government institutions, social securities funds.

Good financial results recorded by banks in 2005 were driven by the gains in terms of balance-sheet and transactional volumes, which in turn translated into higher results on the core activity of the sector over 2004. The banks' profits also grew as a result of lower-than-last year balance of provisions write-offs/impairment losses, first of all for receivables classified as loss or doubtful.

2005 also saw the increase of operating costs of the banks, mainly as a result of growing staff costs. The increase of pay, which took place in a number of banks, was the consequence of better commercial results. Better performance, in turn, translated into pay rises for those groups of employees whose salaries were in direct relation with the sales level. Mid-sized and small retail banks, which spent considerable funds on the development of their network, also contributed considerably to the growth of the operating costs of the banking sector. In contrast, some large universal banks continued measures to rationalise their organisational structures and reduce or control their headcount levels.

The financial results of the banking sector in 2005 were also affected by the application of the International Accounting Standards/International Financial Reporting Standards (IAS/IFRS) for the consolidated reports of banks and the possibility of applying the Accounting Act for standalone financial statements. The implementation of receivables and liabilities measurement at amortised cost upon application of the effective interest rate and the introduction of impairment losses had a major impact on the banks' results. It is, however, hard to estimate the exact impact of those changes on the results of the banking sector due to the possibility of prospective application of certain IAS/IFRS standards, under IFRS 1. In these circumstances, the results for 2004 are not fully comparable with those for 2005. Nevertheless, it is important to note that the impairment losses decreased considerably in relation to the specific provisions level recorded in the previous years. This situation is, however, not only caused by the change of accounting standards, but also by the considerable improvement of the economic and financial standing of borrowers.

Between May 2004 and December 2005, 103 credit institutions declared their intention - by the intermediary of relevant supervisory authorities – to conduct cross-border activity in the territory of Poland. The Polish banking sector did not feel the increased competition from those institutions in 2005, as most of them have not started operations yet.

After five years of decreases, in 2005 the number of employees in the banking sector went up again, along with the growth of the scale of business and number of clients. According to preliminary estimates, nearly 3,000 FTEs were added to commercial banks over 2005. Despite a quick development of electronic banking systems, the number of bank branches has also increased. The plans of branch network development (mainly in the form of small sales units) announced by some banks indicated at the same time that the upward trend in terms of branch number may continue in the nearest future.

## Capital Market

2005 was the best year in the 15-year-history of the Warsaw Stock Exchange, which recorded all-time-highs in terms of trading volumes. During the year the main indices broke records several times, and listed companies paid out dividend of unprecedented levels.

Throughout 2005, the main stock exchange index, WIG, went up by 33.7%, whereas WIG20, the index of top twenty companies gained 35.4%. All sector indices recorded gains. Thanks to the boom on the raw materials market, the shares of companies operating in the metallurgical and chemical sectors recorded spectacular gains (up by 77% and 60%, respectively).

During the trading sessions in 2005, some PLN 173.1 billion worth of shares, up by 59.8% from the year earlier, changed hands. The forward contracts market also developed dynamically, with the trading volume going up by 89.7%. The options market, launched in 2004, also did well (trading went up by 223.1%).

The positive situation on the capital market, which continued from 2004, encouraged issuers to obtain capital via the stock exchange. Public offerings were very popular, and in many cases reductions of subscriptions exceeded 90%. Among the issuers there were 35 companies debuting on the stock market, and in terms of debuts number, only the London Stock Exchange and the pan-European platform Euronext did better than the Warsaw Stock Exchange.

Apart from the gains of stock exchange indices, the yield on stock exchange investments was further enhanced by record dividends paid by the companies – in 2005, 77 companies paid approximately PLN 7.9 billion in dividend to their shareholders.

At the end of 2005, the value of companies listed on the stock exchange reached PLN 424.9 billion, up by 45.7% from December 2004. In consequence, the importance of the stock exchange in the Polish economy grew considerably – the value of listed companies made up for over 30% of the Gross Domestic Product, an increase of approximately 20% on the year.

There were also considerable qualitative changes in the stock-exchange operations, following:

- The enactment on 29 July 2005 of three acts regulating the capital market operations anew. First of all, the new law strengthened the oversight of the market and harmonised the rules with the regulations effective in the EU.
- The introductions of new instruments on the WSE, i.e. forwards on Treasury bonds and options on shares.
- The admission of the first seven remote members; five of which have already started their operations.
- The decrease of admission fees – in an effort to activate the market and improve the competitiveness of the individual instruments, the stock exchange lowered the fees charged from the members twice (they were lowered by 14% altogether).
- The extension of the trading session.

The bull market had a positive impact on the financial standing of brokerage houses. After a period of low financial results, the profits of brokerage houses went up for the second year straight. New entities entered the market, as four new brokerage houses and two banks offering brokerage services in their outlets received the permission of the Polish Securities and Exchange Commission.

As at the end of December 2005, the assets of investment funds reached PLN 61.3 billion, up by over 63% from the end of December 2004. Several factors contributed to the market success of the investment funds, including:

- a relatively low level of interest rates on bank deposits, which was particularly visible in terms of high yield on investments on the capital market,
- the introduction of new types of investment funds on the market,
- the operations of banks, which – due to high commission on the sales of participation units – were even more willing to encourage their clients to invest their funds into investment funds, even at the expense of their bank deposits,
- intense advertising and promotional activities of investment companies.

Higher popularity of funds encouraged the investment companies to extend the funds offer and establish new investment fund companies. In 2005, the Polish Securities and Exchange Commission gave their consent to establishing 4 new investment fund companies and launching 42 new investment funds. The new funds included a securitisation fund, for the first time in Poland, and a hedge fund.

In 2005, investors in the units of investment funds could yield 22.9% on the average. Other funds also performed well. The average yield on the mixed funds, which invest some of the assets in corporate shares, was 18.1%, whereas the units of stable growth funds gained 11.6% over the year.

The structure of investment assets changed following differences in the yields of return on investments. The share of mixed and stable growth funds went up (up from 35% in December 2004 to 42% at the end of 2005), mainly at the expense of debt securities funds (drop from 22% to 17%).

## **II. MAJOR EVENTS IN THE OPERATIONS OF ING BANK ŚLĄSKI S.A. CAPITAL GROUP IN 2005**

### **Changes in the Composition of the Capital Group**

As at 31 December 2005, the Capital Group of ING Bank Śląski S.A. comprised the following companies:

- ING Securities S.A.,
- Śląski Bank Hipoteczny S.A.,
- ING BSK Development Sp. z o.o.,
- ING Nationale-Nederlanden Polska PTE S.A.,
- Solver Sp. z o.o.,
- Centrum Banku Śląskiego Sp. z o.o.

On 15 November 2005, ING Bank Śląski S.A. signed an agreement for the sale of all its shares in ING Services Polska Sp. z o.o. with its registered office in Katowice to Alegon Belegging B.V. with its registered office in Amsterdam, owned in total by ING Bank N.V. The selling price was fixed at PLN 16,000,000 and the agreement covered 27,899 shares of ING Services Polska Sp. z o.o. of the nominal value of 500 each and the total nominal value of 13,949,500.

The Capital Group of ING Bank Śląski S.A. consists of entities, whose business is of key significance in pursuit of strategy of its development. They operate in various segments of the financial market or in its infrastructure zone. As a parent company of the Capital Group, ING Bank Śląski S.A. takes key decisions pertaining to both operations and financial matters of the entities forming the group by fulfilling the control functions in the supervisory authorities of those companies. Their business is strictly co-ordinated, and capital interconnections are often strengthened with the trade relationships and concluded contracts. The companies being part of the Capital Group hold accounts at ING Bank Śląski S.A., on which they make standard settlement operations, and also deposit their free funds on term deposits. The Bank also provides lends funds for the business of some companies (Centrum Banku Śląskiego, Śląski Bank Hipoteczny). The transactions of ING Bank Śląski S.A. with subsidiaries are performed on an arms' length basis.

In 2005, activities were continued to improve the business efficiency of the Bank Capital Group. That was done by the more intensified usage of the synergy opportunities resulting from the Group structure. This is one of the reasons why the Bank entered into new co-operation agreements with ING Securities S.A. and Śląski Bank Hipoteczny S.A.

## **Reorganisation of ING Bank Śląski S.A.**

In 2005, ING Bank Śląski S.A. operated in line with the strategy adopted in 1H 2004, assuming the reinforcement of the Bank's position on the market and increase of the institution value. The main instruments of its realisation include:

- An attractive product offer resulting from a simple and transparent structure of products and competitive prices.
- Brand attributes, used during nationwide campaigns promoting the Bank's key products.
- Sales model based on the multi-channel distribution system and client-focused organisational structure.
- High risk management culture, at the same time taking into consideration the Bank's objectives related to its development.
- Efficient cost management system, supporting the improvement of the Bank cost efficiency.

At the beginning of 2005, the Bank launched the "Retail 2006" Project. The activities taken thereunder aimed, on the one hand, at increasing the services quality by boosting the service efficiency and speeding up the processes. On the other hand, they were to increase the efficiency of the Bank operations due to the reduction of workload and simplification of the service process. The Bank conducted a detailed analysis of the processes related to the sale of individual products and services designed for individual clients, defined their target shape and at the same time set priorities in terms of the implementation of proposed modifications. The first effects of actions taken as part of that project could be observed in September 2005, when the Bank offered its clients to open accounts by Internet and phone, without the need to visit the Bank branch. The Retail 2006 Project will be completed as scheduled; i.e. in 1H 2006. Also the Best Service Program was adjusted to the new market challenges. This is a training programme addressed to the retail network employees – Account Managers and other managers in the Bank branches.

As for the wholesale banking area, the Bank completed the Credit Process Efficiency Improvement Project that had been started in the middle of 2004. The Project was to streamline and shorten the credit process for corporate clients. In 2005, upon completing the design phase, the Bank gradually implemented new solutions in terms of granting corporate loans (including new procedures and IT applications) in all of the Bank Regions. Also some works were conducted on the reconstruction of the Wholesale Division. As part of those works, the Strategic Clients Department was reorganised, the Wholesale Products Development Department was finally created and the Wholesale Marketing Department was established. In autumn 2005 – following the phase of analyses and development of the target solutions – the Wholesale 2006 Project was launched. Its main objective is to implement a new operating model for the corporate client service. Also the wholesale training project and the Wholesale Academy were launched.

The PORCO Project (Project for the Optimisation of the Regional Operating Centres) that started in December 2004 introduced material changes to the Bank's operational sphere. The PORCO Project aimed at developing simpler, cheaper, more convenient and secure methods of working in the operations area. In 2005, the Bank started to implement the new organisational model, assuming the centralisation of some

operating activities, prepared auxiliary applications to launch the processes in the new structure and implemented the new transport model.

In March 2005, after long preparations, the Bank started the migration of IT environment in the branches to a new platform, based on the latest technology. That process covered, first of all, standardisation of the systems and applications as well as replacement of hardware. The migration of IT environment in the branches to the new platform – as part of which approximately 5,900 PCs in all the Bank branches were replaced – was completed in October 2005. The new technology created conditions for optimisation of processes related to management of the users' working environment as well as the reasons for development of IT tools supporting sale of bank products.

As of 2005, a new incentive system, based on Key Performance Indicators, has been binding in ING Bank Śląski S.A. The new system is transparent and strongly oriented on the execution of the Bank's commercial tasks. In spring 2005, the Bank launched the project, which aims at the thorough reconstruction of the basic salary system, based on the new method of valuating positions.

### **Acquisition of Deposits**

As for the deposit market, in 2005, ING Bank Śląski S.A. operated according to the new strategy for acquiring deposits. It aimed mainly at significant strengthening of the position of ING Bank Śląski S.A. on the deposit market, above all by the following:

- ensuring simplicity and transparency of the deposit offer,
- a significant increase of competitiveness and attractiveness of the offer for a wide range of customers,
- priority character of the Open Savings Account (OKO),
- facilities in access to deposits, e.g. by making additional distribution channels available,
- supporting the deposit acquisition process with intensive marketing activities.

The actions taken by ING Bank Śląski S.A. in 2005 on the deposit market proved very successful. The Bank increased its deposit base considerably, strengthened its share in the deposit market and consolidated its position of the fourth deposit bank in Poland. The Bank was so successful because of the good results related to the acquisition of households' savings.

At the end of December 2005, the total value of funds accumulated by the Capital Group of ING Bank Śląski S.A. amounted to PLN 30,673.1 million, up by 16.1% than in December 2004. It is estimated that the funds deposited with the Bank Capital Group represented 8.4% of the total value of funds entrusted to the banking sector (8.1% at the end of 2004).

The structure of deposits of ING Bank Śląski S.A. Group

	31 December 2004	31 December 2005
Households	15,101.0	19,151.0
Corporate entities	9,076.2	8,513.1
Financial entities (other than banks)	1,037.3	1,624.5
Entities of the government and self-government sector	1,195.1	1,384.5
<b>Total</b>	<b>26,409.6</b>	<b>30,673.1</b>

During 2005, the stability of deposit base improved. As at the end of December 2005, the value of funds acquired from households achieved the level of PLN 19,151.0 million as compared with PLN 15,101.0 million as at the end of 2004, and its percentage in the total value of funds deposited at the Bank went up to 62.4% (52.7% at the end of 2004). The growth was possible as a result of success that the Bank achieved in terms of selling the Bank's key deposit product; i.e. the Open Savings Account (OKO). At the end of December 2005, the value of funds deposited in OKO accounts amounted to PLN 12,775.3 as compared with PLN 6,363.7 million in December 2004 (up by approximately 101%).

## Lending

At the end of December 2005, the total value of loans and other receivables of the Capital Group of ING Bank Śląski S.A. from clients amounted to PLN 9,902.9 million against PLN 10,407.9 million in December 2004 (down by 4.9%). It is estimated that at the end of 2005 the Bank Capital Group held a 4.2%-share in the market of credit receivables of the banking sector.

The value of credit receivables shown in the balance sheet of the Capital Group of ING Bank Śląski S.A. as of the end of December 2005 was affected by the following factors:

- continuing relatively low demand for loans on part of corporate customers,
- sale of the portfolio of retail loans granted by the Bank in co-operation with one of the credit intermediaries (worth approximately PLN 148 million),
- the credit policy binding at the Bank, in particular the credit risk assessment principles adopted by the Bank and the lack of FX loans in the offer addressed to the retail clients, which limited the scale of the Bank expansion on the market of housing loans.

The structure of loans and other receivables from the clients of ING Bank Śląski S.A. Group

	31 December 2004	31 December 2005
Households	3,385.3	3,238.7
Corporate entities	6,614.5	5,926.1
Financial entities (other than banks)	529.2	829.2
Entities of the government and self-government sector	386.4	426.0
Other receivables	287.8	288.0
Impairment loss	-795.3	-805.1
<b>Total</b>	<b>10,407.9</b>	<b>9,902.9</b>

The main part of the credit portfolio of the Bank Capital Group was represented by receivables from corporate entities<sup>4</sup>. As at 31 December 2005, the value of loans of corporate entities amounted to PLN 5,926.1 million against PLN 6,614.5 million at the end of 2004.

In the conditions of a decreasing total credit exposure, in 2005 ING Bank Śląski S.A. reported activation of lending in terms of some key products (e.g. PLN mortgage loans and loans related to the credit cards) as well as with regard to some market segments (i.e. in relation to the corporate clients from the segment of large and mid-sized companies).

### Structure of Shareholding of ING Bank Śląski S.A.

Fulfilling its commitment made towards the Banking Supervision Commission regarding the reduction of shares of ING Bank N.V. in ING Bank Śląski S.A. to 75%, on 18 March 2005 ING Bank N.V. sold 1,661,141 shares of ING Bank Śląski S.A. through the agency of the Stock Exchange. The said shares were sold in the following tranches:

- 150,886 shares under the Retail Investors Tranche, where:
  - 149,282 shares under the Privileged Sub-tranche at PLN 431 per share,
  - 1,604 shares under the Basic Sub-tranche at PLN 440 per share,
- 1,510,255 shares under the Institutional Investors Tranche at PLN 440 per share.

The principal shareholder did not change its strategy towards ING Bank Śląski S.A. after ING Group fulfilled its commitment towards the Banking Supervision Commission. ING Bank N.V. still considers Poland – next to the countries of Benelux – as the underlying market for its business. However, selling a part of shares in ING Bank Śląski S.A. by ING Group increased the liquidity of the Bank's shares listed on the Warsaw Stock Exchange.

According to the information obtained by ING Bank Śląski S.A., the structure of shareholding of ING Bank Śląski S.A. is as follows:

<sup>4</sup> The figures comprise the receivables of the Capital Group from enterprises and non-profit institutions serving households.

Name of Shareholder	Number of shares and votes at GSM	Share in equity and total votes at GSM	Number of shares and votes at GSM	Share in equity and total votes at GSM
	31 December 2005		31 December 2004	
ING Bank N.V.	9,757,500	75.00%	11,418,641	87.77%
Commercial Union OFE BPH CU WBK	830,000	6.38%	700,000	5.38%
Others	2,422,500	18.62%	891,359	6.85%
<b>Total</b>	<b>13,010,000</b>	<b>100.00%</b>	<b>13,010,000</b>	<b>100.00%</b>

## Observance of Good Practices of the Corporate Governance

On 17 February 2005, the Management Board of ING Bank Śląski S.A. presented a declaration on accepting the “*Best Practices in Public Companies in 2005*” to be observed by the Bank including a commentary on their application. The above-mentioned declaration received a positive opinion of the Bank Supervisory Board. Afterwards, the declaration was accepted by the General Shareholders Meeting on 9 June 2005.

In line with the declaration, the Bank observes all the rules stipulated in the “*Best Practices in Public Companies in 2005*”, especially:

- the Bank’s target is to have all the activities of the company’s bodies aimed at the long-term development of the company;
- it creates the conditions for the execution of rights of the majority shareholder to take into account the interests of the minority shareholders;
- being a company with the majority shareholder holding the stake, which ensures more than 50% of the total number of votes, that Bank has at least two independent members in its Supervisory Board.

Moreover, the Compliance Manual accepted in the year 2004 is binding in the Bank. It was introduced in order to counteract the risk of infringing good reputation of ING Bank Śląski S.A., ING Group or any of its entities as a result of non-compliance with the ethical and legal norms by the employees.

## Changes in the Management Board and Supervisory Board of ING Bank Śląski S.A.

In 2005, there were the following changes in the composition of the statutory authorities of ING Bank Śląski S.A.:

- At the meeting of 11 February 2005, the Supervisory Board of ING Bank Śląski S.A. appointed Mr. Ian Clyne to the position of the Executive Vice-President of ING Bank Śląski S.A., effective as of 1 March 2005.
- On 29 April 2005, the Supervisory Board appointed the Management Board of ING Bank Śląski S.A. for the new tenure in the so far composition; i.e.:
  - Mr. Brunon Bartkiewicz Chief Executive Officer,
  - Mr. Krzysztof Brejda Executive Vice-President,

- Mr. Ian B. Clyne Executive Vice-President,
- Mr. Grzegorz Cywiński Executive Vice-President,
- Mr. Donald Koch, Executive Vice-President,
- Mr. Michał Szczurek Executive Vice-President,
- Mr. Benjamin van de Vrie Executive Vice-President,
- Mr. Maciej Węgrzyński Executive Vice-President.

The tenure of the Bank Management Board started as of the date of the General Shareholders Meeting of ING Bank Śląski S.A. approving the Bank's financial statement for the year 2004; i.e. on 9 June 2005, and it will last until the date of the General Shareholders Meeting approving the Bank's financial statement for the year 2009.

- On 9 June 2005, the General Shareholders Meeting of ING Bank Śląski S.A. accepted the resignation of Mr. Erik Dralans from his capacity as member of the Supervisory Board. At the same time, the following individuals were appointed to the Supervisory Board: Ms. Anna Fornalczyk, Mr. Hans van der Noordaa, Mr. Marcus van der Ploeg and Mr. Igno van Waesberghe. Since 9 June 2005 the Supervisory Board of the Bank have worked in the following composition:

- Mr. Andrzej Wróblewski Chairman, Independent Member,
- Mr. Cornelis Leenaars Vice-Chairman,
- Mr. Jerzy Rokita Secretary, Independent Member,
- Ms. Anna Fornalczyk Member, Independent Member,
- Mr. Hans van der Noordaa Member,
- Mr. Marcus van der Ploeg Member,
- Mr. Igno van Waesberghe Member,
- Mr. Lech Węclewski Member, Independent Member.

### **Ratings of ING Bank Śląski S.A.**

As at the end of December 2005, the financial credibility ratings for ING Bank Śląski S.A. received by the largest rating agencies were as follows:

#### **Moody's Investors Service Ltd.**

Long-term deposits	A2
Short-term deposits	P-1
Financial strength	D+
Long-term and short-term deposits rating outlook	Stable

On 22 July 2005, Moody's Investors Service Ltd. informed the Management Board of ING Bank Śląski S.A. about the increase of the financial strength forecast from D (with positive outlook) to D+ (with stable outlook). Other ratings were sustained on the unchanged level.

According to the communication of the Moody's Agency, the higher rating of the financial strength of ING Bank Śląski S.A. reflected positive effects of restructuring and improvement in the risk management area, which was confirmed by the higher quality of assets and lower risk costs. While changing the Bank's rating, the Agency also took into consideration the results achieved in terms of the cost control, successes

in the deposit acquisition area, a high level of solvency ratio and concentration on activities supporting the sale of the bank products.

Although ING Bank Śląski S.A. improved its financial results, the Agency pointed to the negative impact of the decreasing credit portfolio on the interest result and the result due to the fees and commissions. It also indicated that the income growth was reported in trading operations, subject to volatility. At the same time, the Agency emphasised that the increased activity in that area did not raise the Bank's exposure in terms of market risk.

The Moody's Agency stated also that the effects of implementing the new strategies in the area of retail and mortgage loans will be reflected in the Bank results with some delay. However, while developing the retail business, ING Bank Śląski S.A. is exposed to a very strong competition. According to the Agency, whether the financial strength rating of ING Bank Śląski S.A. continues to increase depends on the Bank's capacity to develop its credit portfolio while sustaining the risk control. It is also determined by the growth of revenues and strengthening of the Bank's market potential.

The rating of the Moody's Investors Service Ltd. was not prepared at the request of ING Bank Śląski S.A.

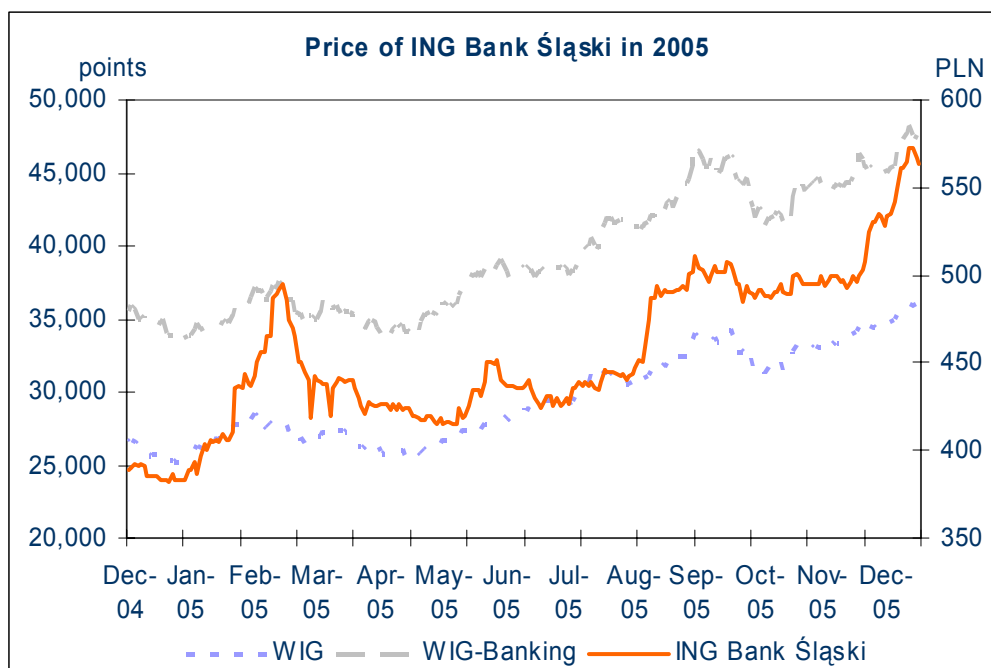
#### **Fitch Ratings Ltd.**

Long-term liabilities	A
Outlook for sustaining the above rating	Positive
Short-term liabilities	F1
Individual rating	D
Support rating	1

On 24 March 2005, the Fitch Ratings Ltd. informed the Bank Management Board about raising the outlook for long-term rating of ING Bank Śląski S.A. from Stable to Positive. This resulted from the change of long-term sovereign outlook for Poland that took place on 23 March 2005 from BBB+ to Positive. The improvement of rating for Poland reflected a few good tendencies present in the economy, such as positive impact of some structural reforms on the results of foreign trade and macroeconomic stability. At the same time, the Agency informed that the long-term rating and rating of ING Bank Śląski S.A. support took into account the potential support of the Bank's foreign investor i.e. ING Group.

#### **Price of ING Bank Śląski S.A. Shares**

On 31 December 2004, the price of ING Bank Śląski share was PLN 389 versus PLN 564 as on 30 December 2005. Therefore, the rate of return on investments in the shares of ING Bank Śląski S.A. was 45.0% in 2005, or 50.0% upon including the dividend paid out. By comparison, the sub-index for the Banks sector went up by 32.0%.



At the end of 2004, the market value of ING Bank Śląski S.A. was PLN 7,338 million, whereas the P/BV ratio was 2.06.

## ING Bank Śląski S.A. in Society

### *Activity in favour of culture and arts*

As in the previous years, in 2005, ING Bank Śląski S.A. continued co-operation with the most prestigious cultural institutions as well as supported major events of cultural life all over the country. When selecting the undertakings and projects to give support to, the Bank tried to select the ones strongly rooted in the Polish tradition and culture as well as the ones promoting the works of Polish artists.

In 2005, ING Bank Śląski S.A. became the patron of the following cultural events:

- Cycle of concerts *“Sygnowano Moździerz”* [“Signed Moździerz”], organised by the Artist Centre *“Fabryka Trzciny”* in Warsaw. The cycle-opening concert was held in the Salesians’ Basilica in Warsaw. That concert – dedicated to the memory of Pope John Paul II – featured outstanding Polish jazz musicians of the young generation: Leszek Moździerz (piano) and Adam Klocek (cello). For the following concerts held on the stage of *Fabryka Trzciny* Leszek Moździerz invited the Chamber Philharmonic Orchestra (conducted by Wojciech Rajski), American jazz pianist Uri Kaine and Adam Smolik. The cycle was finished by the concert of *Trio Leszka Moździerza* [Leszek Moździerz’s Trio], including also such outstanding European jazzmen, as Lars Danielsson and Zohar Fresco.
- The cycle of jazz concerts *“Jazz i okolice”* [“Jazz and the like”] performed together by *Górnośląskie Centrum Kultury* [Upper Silesia Cultural Centre] and club *“Żak”* in Gdańsk. The performers were among others: Bill Frisell, Eliot Sharp, Moreno Veloso, Marc Ducret, Otomo Yoshihide, Uri Caine and Joey Baron.

- The concert tour “The Time”, promoting the album of Leszek Możdżer under the same title. During that tour Leszek Możdżer’s Trio gave concerts in eight cities. The last one was the gala concert in Gdańsk, during which the artist was awarded the Platinum Disc by *Związek Producentów Audio Video w Polsce* [Polish Society of the Phonographic Industry].
- Celebration of the 75<sup>th</sup> anniversary of the Karol Szymanowski Academy of Music in Katowice, including the jubilee feast connected with the award of the *Doctor Honoris Causa* degree to one of the most outstanding graduates from that university - Krystian Zimerman.
- Theatre Festival in Nowy Sącz taking place in *Teatr Robotniczy im. Bolesława Barbackiego* [Bolesław Barbacki Workers Theatre]. The performances featured renown Polish theatrical groups, like: *Teatr Roma* [Roma Theatre] in Warsaw, *Teatr Ochoty* [Ochota Theatre] in Warsaw, *Teatr Powszechny im. Zygmunta Hübnera* [Zygmunt Hübner People’s Theatre] in Warsaw, *Teatr Kwadrat* [Kwadrat Theatre] and *Teatr im. Stefana Jaracza* [Stefan Jaracz Theatre] from Łódź.
- 7<sup>th</sup> edition of Nationwide Festival of Directors’ Art “Interpretations 2005”, which was held in *Teatr Śląski im. Stanisława Wyspiańskiego* [Stanisław Wyspiański Silesia Theatre] in Katowice.
- 15<sup>th</sup> Music Days in Mikołów. The Festival was first held in 1991 and since then has featured the most outstanding soloists and bands from Poland and abroad. It is dominated by symphonic music, organ and chamber music and selected concerts are recorded by the Polish Radio and Polish Television.
- Together with ING Nationale-Nederlanden Polska ING Bank Śląski S.A. was the patron of the 3<sup>rd</sup> edition of the Silent Cinema Day organised by *Filmoteka Narodowa* [National Film Library]. As part of that day, the Warsaw cinema “Iluzjon” presented the greatest stars of the silent cinema from the period 1920-1930.
- The Festival of Krzysztof Kiesłowski Films in Holland. The Bank – together with ING Lease Polska and ING Bank N.V. – ING Bank Śląski S.A. participated in the organisation of the Festival in the memory of the 10<sup>th</sup> anniversary of the director’s death. During that festival – next to the films review – also some lectures were given and films were shown for young people. Besides, some exhibitions of film posters and pictures and discussions with the participation of renown critics were organised.

ING Bank Śląski S.A. also supported some cultural events important for local communities, such as: Jazz Festival and the 30<sup>th</sup> Festival of the Ukrainian Children Bands in Koszalin, celebration of the 140<sup>th</sup> anniversary of Katowice, “Life passions” (cross-section exhibition showing interesting people) and activity of *Teatr Współczesny* [Modern Theatre] in Szczecin (in the artist season 2004/2005).

ING Bank Śląski S.A. is an industrious member of the ING Polish Art Foundation. Its primary objective is to promote the Polish modern art, especially the work of young artists. The Foundation collects works representing different trends of modern art and different artistic techniques (painting, drawing, graphics and photography), figurative and abstract art. In 2005, the works by Elżbieta Jabłońska and Grzegorz Sztwiertnia were added to the collection.

### **Charity**

In the year 2005, ING Bank Śląski S.A. pursued the broadly understood charity works via the ING for Children Foundation (formerly known as the Foundation of ING Bank Śląski). The Foundation mission can be expressed in the slogan “Equal chances for the Polish children”.

The explicit focus of charity on part of ING Bank Śląski S.A. on children is a response to the global programme for helping children, announced by the CEO of ING, Michel Tilmant “ING Chances for Children”. The ING for Children Foundation was established on the initiative of CEO Brunon Bartkiewicz, ambassador of ING Group for Helping Children in Poland.

The Foundation of ING Bank Śląski S.A. concentrates its activities on the education of children and youth from the poorest parts of Poland. However, the definition of poor area is not only limited to geographic terms, but also to social, welfare and health terms. Primarily the Foundation deals with chronically ill children or children from the marginalised families. Besides, the Foundation undertakes the following actions:

- helps particularly gifted children,
- supports initiatives in terms of economic education and entrepreneurship allowing young people to gain knowledge and skills to realise their professional plans in the realities of market economy,
- has patronage over the work of ING volunteers.

### **Health and Social Care**

As each year, some health care institutions received significant help from the Bank. The charity donations were made, among others, to: Polish-American Institute of Paediatrics in Kraków-Prokocim, *Klinika Intensywnej Terapii i Patologii Noworodka Śląskiej Akademii Medycznej* [Neonatal Intensive Care and Pathology Clinic at the Silesian Academy of Medicine] in Zabrze, traumatic and orthopaedic ward for children and youth in *Wojewódzki Szpital Chirurgii Urazowej* [Province Traumatic Surgery Hospital] in Piekary Śląskie and children’s oncology hospitals.

### **Education**

In 2005 – as part of activity aimed at equalising the children’s chances – ING Bank Śląski S.A. granted its support to the following education centres:

- primary schools – in Hoszów and Manasterc in Bieszczady and in Węgleszyn in Świętokrzyskie Province,
- special schools – no. 6 in Katowice and in Siemianowice Śląskie,
- School Complex at the Province Paediatrics Centre “Kubalonka” in Istebna,
- Special Education and Upbringing Centres in Sanok and Lesko.

The Bank organised education and rehabilitation holidays for the children from all the above-mentioned outlets. Apart from that, to improve the children’s conditions for learning and rehabilitation, it gave them some hardware, furniture and office stationery.

Within its projects for social responsibility the Bank undertook the following actions:

- in May 2005, it launched a free internet café in Katowice-Załęże designed for the children from that district,

- supported the 3<sup>rd</sup> Poland-wide Festival of the Children's Expression, during which the exhibition of works of the children and youth from special schools (drawings and sculptures) was presented in the audiovisual room in the Head Office building in Katowice,
- participated in the "Entrepreneurship Day" 2005 organised by the Youth Entrepreneurship Foundation,
- took part in program "Passport to Entrepreneurship", i.e. the training program for people, who want to run economic activity on their own account.

Also some universities, academic associations and foundations supporting science were given support of ING Bank Śląski S.A. Some of them were: University of Economics in Cracow (Economics and Public Administration Department), University of Silesia (Law and Administration Department), Institute of Physics at the University of Silesia in Katowice (celebration of the World Year of Physics), and the University of Economics in Katowice (starting an Internet cafe).

In 2005, the Bank involved itself in the preparation of the 6<sup>th</sup> Forum of the Linguistic Culture, an enterprise organised by the Polish Language Council at the Presidium of the Polish Academy of Sciences and the University of Silesia. The Forum meeting, which was held under the name "*Polish Linguistic Policy In View of Poland's Membership in the European Union*", was attended by linguists, sociologists, political scientists and specialists representing Poland in the European Union and using Polish language in the European Union organisations.

#### Social programmes

In September 2005, on the initiative of ING Bank Śląski S.A., the first-in-Poland programme propagating the techniques of bibliotherapy "*W towarzystwie Lwa*" ["In the company of the Lion"] was launched. It was developed for children staying in hospitals at oncology and haematology wards all around Poland.

As part of that campaign, the small patients from all eighteen oncology wards in Polish hospitals received the book called: "*Lucjan Lew, jakiego nie było*" ["Lucian the Lion one of its kind"]. During the meetings with the children the book was read by their nurses and volunteers, including celebrities from the world of culture and art. Also some common games and plays with Lucian the Lion were organised. The children accepted the book and considered the meetings with Lucian the Lion as great fun.

The survey made at the oncology wards revealed that the book was also helping the children's parents and psychologists to take some actions to eliminate tension, stress and fear that the children struggle with during the hard illness.

In 2005, ING Bank Śląski S.A. also co-operated with other foundations, whose statutory objectives are consistent with the direction of social and charity activities of the Bank, for example the following:

- *Fundacja dla Ludzi Potrzebujących Pomocy „Gniazdo”* [Foundation for People in Need "Gniazdo"] implemented the "Programme for Helping Children and Youth" from the marginalised families,

- *Fundacja Młodzieżowej Przedsiębiorczości* [Youth Entrepreneurship Foundation], which prepares children and youth for life in the circumstances of market economy and in citizen's society,
- *Stowarzyszenie „Serce dla Dziecka”* [“A Heart for the Child” Association]
- *Fundacja „Wspólna Droga”* [“United Way Polska”],
- *Polska Akcja Humanitarna* [Polish Humanitarian Organisation] and
- *Krajowy Fundusz na Rzecz Dzieci* [Polish Children's Fund].

#### Social Commitment of Employees

ING Bank Śląski S.A. also encouraged its employees to undertake social and charity activity. The key undertakings in 2005 organised with employees included:

- Two honourable blood donation campaigns run together with the Regional Centre for Blood Donation and Blood Treatment in Katowice.
- Fund raising to help tsunami victims in Asia, where the funds were handed over to the Polish Humanitarian Organisation.
- “Orange Bracelet” Campaign, in the course of which silicon bracelets were sold with an inscription “I give children a chance”. The collected funds in the amount of nearly PLN 50 thousand were designated for the purchase of medical equipment for the children's oncology wards all around Poland.

#### **Awards and Distinctions**

In 2005, the activity and products of ING Bank Śląski S.A. gained common acceptance and were highly evaluated, both by clients and experts, which was proven by the awards and distinctions received by the Bank:

- November 2005, Distinction in the *Złote Spinacze* [Golden Paperclips] competition in the Corporate Social Responsibility (CSR) category for the “In the Company of the Lion” social programme;
- November 2005, Special Distinction in the *Arts & Business Awards* for overall activities to promote and develop art and culture in Poland.
- October 2005, awarded the title of the Benefactor of the National Museum in Cracow by the Minister of Culture in recognition of the co-operation with the Museum on two exhibitions “*Leon Wyczółkowski 1852-1936*”, an exhibition celebrating the 150<sup>th</sup> Anniversary of the Artist's Birthday and “*Painters of Reality*”.
- September 2005, The best bank for small companies in the ranking Forbes monthly and third place in the ranking of the best retail banks.
- June 2005, first place in the KOMPAS competition, “*Visibility at Universities*” category, a ranking organised under the auspices of *Rzeczpospolita* daily, MillwardBrown SMG/KRC and the Student Research and Consulting Group of the Warsaw School of Economics (SGH) in Warsaw.
- April 2005, CEDRYK Prize, awarded by *Centrum Ekspresji Dziecięcej* [Children's Expression Centre], functioning at the Library of Silesia, for help and commitment in the organisation of the 3<sup>rd</sup> Poland-wide Festival of Children's Expression.
- April 2005, Diamond Sponsor for supporting the program of the President of the Republic of Poland “*Internet at Schools*”.

### **Selection of Certified Auditor of ING Bank Śląski S.A.**

On 29 April 2005, the Supervisory Board selected KPMG Audyt Spółka z o.o. with its registered office in Warsaw at 51 Chłodna Street (licence of the National Chamber of Certified Auditors no. 458) to be the certified auditor carrying out the audit of the financial statements of ING Bank Śląski S.A. for the period from 30 June 2005 to 30 June 2008.

ING Bank Śląski S.A. has made use of the services provided by KPMG in the field of auditing the financial statements since 1990.

	<b>Accounting year ending on 31 December 2005</b>
Remuneration for the audit in regard to the parent company (1)	PLN 1,510,000
Remuneration for the audit in regard to subsidiaries (2)	PLN 235,000
Remuneration for related services (3)	PLN 1,344,000

- (1) Remuneration for the audit covers the amounts paid to KPMG Audyt Sp. z o.o. for the professional services related to the audit of the unit and consolidated financial statement of the dominant entity (agreement of 12 August 2005) and review of the interim unit and consolidated financial statement (agreement of 12 August 2005).
- (2) Remuneration for the audit shall cover the amounts paid to KPMG Audyt Sp. z o.o. for its professional services related to the audit of financial statements of subsidiaries.
- (3) Remuneration for related services covers the amounts paid to KPMG Audyt Sp. z o.o. They cover validation services related to the audit or review of financial statements of the dominant entity and subsidiaries that were not included in item 1.

### **Remuneration for the Members of Management Board and Supervisory Board of ING Bank Śląski S.A.**

In 2005, the total amount of remuneration (understood as the value of remuneration, bonus, cash benefits, in-kind benefits or any other benefits) paid by ING Bank Śląski S.A. to the Management Board members amounted to PLN 14,725,000. The total amount of remuneration and bonuses paid out or due for 2005 given here is the gross amount of remuneration paid out or due and payable for the period from January to December 2005 and the 2004 bonus, which was paid out in 2005 at the total amount of PLN 1,494,000. Furthermore, in 2005 the Bank established a provision of PLN 2,574,000 for the bonus payable for that year.

The members of the Bank Management Board and other people being the employees of ING Bank Śląski S.A. receive neither remuneration nor bonus for holding any functions in the authorities of subsidiaries and affiliates of the ING Bank Śląski Capital Group.

Remuneration of members of Management Board of ING Bank Śląski S.A. in 2005 (PLN 000)

Name	Period from - to	Remuneration and bonuses	Benefits	Total
Brunon Bartkiewicz	01.01.05-31.12.05	1,437	985	<b>2,422</b>
Krzysztof Brejda	01.01.05-31.12.05	1,266	323	<b>1,589</b>
Ian Clyne	01.03.05-31.12.05	899	1,086	<b>1,985</b>
Grzegorz Cywiński	01.01.05-31.12.05	1,234	299	<b>1,533</b>
Donald Koch	01.01.05-31.12.05	1,000	923	<b>1,923</b>
Michał Szczurek	01.01.05-31.12.05	1,097	268	<b>1,365</b>
Benjamin van de Vrie	01.01.05-31.12.05	1,033	793	<b>1,826</b>
Maciej Węgrzyński	01.01.05-31.12.05	1,436	646	<b>2,082</b>
<b>Total</b>		<b>9,402</b>	<b>5,323</b>	<b>14,725</b>

In 2005, the total amount of remuneration (defined as above) paid by ING Bank Śląski S.A. to the Supervisory Board members amounted to PLN 1,058,000.

Remuneration of members of Supervisory Board of ING Bank Śląski S.A. in 2005 (PLN 000)

Name	Period from - to	Remuneration and bonuses	Benefits	Total
Andrzej Wróblewski	01.01.05-31.12.05	272	-	<b>272</b>
Cornelis Leenaars	01.01.05-31.12.05	164	-	<b>164</b>
Jerzy Rokita	01.01.05-31.12.05	194	-	<b>194</b>
Lech Węclewski	01.01.05-31.12.05	122	-	<b>122</b>
Anna Fornalczyk	09.06.05-31.12.05	69	-	<b>69</b>
Hans van der Noordaa	09.06.05-31.12.05	57	-	<b>57</b>
Marcus van der Ploeg	09.06.05-31.12.05	57	-	<b>57</b>
Ignó van Waesberghe	09.06.05-31.12.05	57	-	<b>57</b>
Erik Dralans	01.01.05-09.06.05	66	-	<b>66</b>
<b>Total</b>		<b>1,058</b>	-	<b>1,058</b>

### III. ING BANK ŚLĄSKI S.A. ON BANKING MARKET IN 2005

ING Bank Śląski S.A. is one of the largest universal banks in Poland. At the end of December 2005 the balance sheet total of the Bank was PLN 42,084.0 million, which accounted to 7.2% of assets of the Polish banking sector. During 2005, the Bank increased its share in the assets of the banking sector by 0.7 percentage points and at the end of the year was the fourth biggest bank in Poland.

Reinforcement of market position by ING Bank Śląski S.A. was the consequence of a steady expansion of activity in the primary markets of banking services; i.e. in retail banking, wholesale banking and also on money and capital markets.

#### **Retail Banking**

##### *Scope of the Offer and Changes Introduced*

ING Bank Śląski S.A. offers its individual clients a state-of-the-art and comprehensive range of products. It covers maintenance of personal accounts, clearing, deposit and credit products, bank cards (debit, credit and pre-paid) as well as products and services of other ING Group members, such as: mutual funds, lease and brokerage services.

In 2005, ING Bank Śląski S.A. introduced essential changes to its basic product addressed to individual clients; i.e. personal account – the so-called Lion Account. In order to simplify the offer of personal accounts, assure its transparency and make it even more easily accessible, in March 2005, the Bank withdrew some options of the Lion Account from the market, expanded a range of services available within the package via electronic channels (implementation of SMS Package) and modified the Table of Fees and Commissions so as to promote the electronic distribution channels. Modification of Accounts was accompanied by a simplification of the client service process; e.g. a few general terms and conditions in force were replaced with just one and the principles of co-operation both for the personal account, debit cards and electronic banking systems were defined.

To encourage clients to open Lion Accounts, ING Bank Śląski S.A. held various nationwide marketing and promotional campaigns using all sorts of mass media. For example, in October, a campaign promoting the Student Lion Account was run at many universities and colleges. Its main message was that the Account could be opened in an easy and simple manner, both via electronic distribution channels and at traditional bank outlets.

The Open Savings Account (OKO Account) remained the Bank's key deposit product in 2005. With the savings account the clients may make additional deposits and withdraw them without losing interest. The OKO Account is offered both in PLN as well as EUR and USD. Throughout 2005, the Bank was active in encouraging clients to deposit funds in savings accounts. For instance, in May 2005, the Bank offered an increase of the interest rate for new funds accumulated in OKO accounts by 2 percentage points. This interest rate was offered for two months and promoted within a nationwide multi-tool marketing campaign.

Throughout the year, the Bank also improved other deposit products; e.g.:

- in February 2005, the Deposit and Fund Package was introduced (in co-operation with ING TFI), where the client's funds are deposited in 50% on a term deposit of fixed interest rate and in 50% in participation units of the ING TFI mutual fund selected by the client,
- the offer of FX deposit products was modified; as part of the modifications, the Open Savings Account OKO in a foreign currency was introduced, the deposits of variable interest rate and fixed interest rate for the period of 3 and 6 months were put on hold, but a 24-month deposit in USD with fixed interest rate was introduced.

In September 2005, access to the Bank was made easier for clients, as the process of automated account opening via Internet and over the phone was substantially modified. Account opening using those channels was combined with a concurrent order of a debit card, HaloŚląski phone service and ING BankOnLine electronic banking system.

The credit offer of ING Bank Śląski S.A. for individual clients includes mortgage, housing and car loans, loans for the purchase of securities, overdraft and a wide range of occasional credit facilities. Only PLN loans are offered to individual clients. In 2005, the Bank introduced the following changes to its credit offer for individual clients:

- lessened the rules of granting the Lion Account overdraft, by enabling the clients to request the credit limit being double monthly net income pursuant to the statement of remuneration already at the time of account opening,
- introduced the loan for purchase of securities in public offering in the form of a credit line assigned for 12 months, which allowed for multi-drawing of funds in the contractual period and reduced the costs of loan disbursement,
- modified offer of car loans, among others, extended the tenor, reduced the required downpayment, simplified procedures, made loans available at the car dealer premises,
- offered new types of occasional loans (Springtime and Holiday).
- made it possible to request a cash loan via Internet and over the phone.

As part of its retail activity, ING Bank Śląski SA also services small businesses. In accordance with the rules in force at the Bank, the small business segment comprises both individuals running a business activity, partnerships and companies, and also non-profit entities, with annual income from the net sales or annual budget at disposal worth up to EUR 800 thousand.

Throughout 2005, ING Bank Śląski S.A. remodelled its offer for small businesses. First of all, as of 1 February 2005, the Bank launched a new clearing and deposit offer for small business. It comprises the PROFIT Lion Account for small business (for individuals running a business activity on their own and partnerships) and PROFIT+ Lion Account (for companies). New current accounts offered by the Bank feature, first of all, a summary opening procedure (a current account, a savings account and electronic banking services are provided under one agreement) and account maintenance and electronic transfer fees that are attractive for clients. The said bundles also comprise a savings account in USD, and also EUR and USD deposits. At

the time when a new deposit offer was launched, the Bank also rendered its clients service by a Small Business Service Team, separated in the Call Centre structure.

As of the beginning of March 2005, the Bank recommended a new lending offer and a new sales and service model to small businesses. It is composed of a credit line in the current account and a cash loan for small business. The latter combines the features of investment and working capital loans. The new offer is simple, transparent and has attractive price terms. Standardised rules of client's credit capacity assessment – based on scoring, evaluation in the Credit Information Bureau and information found in the client databases – enabling acceleration and streaming of the lending process are an important attribute thereof.

The new lending offer for small businesses was proposed along with a new centralised model of sales and small business service, whereunder:

- the network of branches is the primary distribution channel of credit facilities, while the branch employees were freed from performance of the back-office operations and made to sell products in an active manner instead,
- credit platforms, equipped with relevant IT tools, in charge of making all-inclusive credit risk assessments, taking credit decisions and drawing up credit agreements,
- central back-office performs operational activities as well as monitoring and debt collection.

The changes made in the offer for small businesses were also communicated to clients in the course of nationwide promotional campaigns. They demonstrated much interest in the modifications, which was reflected in the higher number of new accounts opened for small business.

### ***Service of Up-scale Customers***

ING Bank Śląski S.A. has significant assets being a state-of-the-art offer of products and services, professional advisers, a new system of client service and international brand, making it possible to meet high requirements of up-scale customers.

Through dedicated account managers, up-scale customers have got an access to sophisticated services, including term products of the money market and securities, like forwards and NDFs, Buy-Sell-Back transactions based on State Treasury bills and transactions on other debt securities not subject to public offer. Good co-operation of the Bank with ING Securities, ING Investment Management and ING Investment Funds Corporation also allows it to offer other asset management services.

In 2005, the Bank continued the works initiated in 2004, aimed at developing the new quality service concept and the product offer for up-scale clients. Upon an analysis of the up-scale clients' preferences in the aspect of banking services, ING Bank Śląski S.A. adopted the following segmentation of the Private Banking clients:

- assets held of at least PLN 100,000 or their equivalent in a foreign currency, or
- average monthly inflows to a current account of at least PLN 7,500.

In 2005, the Bank introduced essential changes, both in the service principles and product offer in the Private Banking area. The Bank:

- Prepared a new VIP account – a package of products dedicated specially to the Private Banking segment and based on the current account.
- Recommended subsequent subscriptions to the Investment Term Deposit and launched the Investment Insurance Deposit on the market (together with ING NN Poland).
- Appointed the dedicated VIP Call Centre Team of operational and service character, whose tasks include provision of comprehensive information and client service as well as operational support for account managers.
- Initiated the process of opening the state-of-the-art Private Banking Centres, complying with top standards as to service convenience and confidentiality. In December 2005, the Bank opened two first new Centres, while the process of establishing new Private Banking Centres will be completed in 2Q 2006.
- Continued an analysis of the Private Banking portfolio structure on the basis of the introduced segmentation criteria, which shall constitute the basis for further efforts to enhance the attractiveness of the Private Banking offer.

### ***Housing Needs Finance***

Pursuant to the lending policy in force, housing needs finance is one of the priority lines of ING Bank Śląski S.A. operations. This is reflected in a broad range of housing and mortgage loans in PLN offered to clients, among others.

In 2005, the Bank undertook multilevel actions stimulating sales of mortgage loans, for instance:

- it launched new products on the market: a Mortgage Credit Line, being a combination of a current account with the credit limit secured with a mortgage and a consolidation loan,
- made mortgage loans more available by concluding agreements regarding sales of mortgage loans with chain intermediaries; however, due to the popularity of FX-denominated loans among clients, the results of such co-operation were rather limited,
- supported sales of products with marketing actions; the Bank run an Autumn marketing campaign of PLN mortgage loans accompanied by a special pricing offer (0% of commission for mortgage and construction-mortgage loan extension, no fees for loan prepayment), among others,
- conducted comprehensive training programmes, including programmes for the employees at the Call Centre, Mortgage Banking Advisors and credit intermediaries (especially, representatives of ING Nationale-Nederlanden Polska),
- prepared a product manual with an all-inclusive description of the Bank's policy as to mortgage loans,
- implemented a system of appraisal of work and standards of service rendered by mortgage advisors, based on *mystery shopper* analyses.

### **Deposits**

As at 31 December 2005, the value of household deposits at ING Bank Śląski S.A. amounted to PLN 19,151.0 million, up by PLN 4,050.0 million, or 26.8% from December 2004. At the end of 2005, 8.5% of household deposits in the banking sector were accumulated in accounts at ING Bank Śląski S.A. (versus 7.2% in December 2004). These results caused the Bank to move to the position of the third largest bank on the market of household deposits.

The results produced in respect of acquisition of funds from retail clients show that the actions taken within the new strategy of the deposit acquisition were efficient. The Bank generated very good results as to growth of funds deposited in the Open Savings Account (OKO Account) in particular. Throughout 2005, the volume of funds accumulated in OKO accounts went up from PLN 6,363.7 million to PLN 12,775.3 million (up by 101%).

Deposits of private individuals form the core component of household deposits at the Bank. At the end of December 2005, they totalled PLN 18,030.5 million, up by PLN 3,805.9 million, or 26.8%, from December 2004.

To provide its clients with a wide array of savings products, ING Bank Śląski S.A. also distributes units of ING TFI investment funds. As at the end of 2005, net assets of ING TFI acquired by intermediation of ING Bank Śląski S.A. totalled PLN 2,237.8 million (versus PLN 1,063.7 million at the end of 2004). It represented approximately 46% of the total value of assets of open-end investment funds managed by ING TFI.

Throughout 2005, ING Bank Śląski S.A. closed approximately 130,000 inactive personal (ROR) accounts. At the end of 2005, the number of personal accounts maintained by the Bank totalled 1,002,200 versus 974,800 at the end of 2004. In December 2005, ING Bank Śląski S.A. was number six on the market of personal accounts with a 6.1%-share in terms of their total number.

As at the end of December 2005, 112,300 small businesses held a current account at ING Bank Śląski S.A., out of which 107,000 had a Small Business Lion Account. Making the clearing and deposit offer for small business more attractive resulted in an approximately 16%-increase of the number of current accounts held by the clients from that segment.

### **Lending**

As at the end of December 2005, the household credit receivables of ING Bank Śląski S.A. totalled PLN 3,138.5 million. The Bank held a 2.2%-share in the household credit receivables of the banking sector. Over 2005, the Bank's credit exposure towards households went down by PLN 124.1 million. This drop resulted from the following, among others:

- Sale of the credit portfolio of approximately PLN 148 million, extended in co-operation with the credit intermediary Finplus.
- Adopted credit policy, pursuant where to the Bank offers PLN loans to retail clients only, while clients prefer FX ones (notably in the area of housing loans being the most dynamic market part).

At the same time, the Bank gradually built its position in the PLN mortgages. Such mortgages do not pose any FX-risk, which is advantageous both to the borrowers and the Bank. In December 2005, the credit receivables of ING Bank Śląski S.A. due to PLN mortgages totalled PLN 683.4 million versus PLN 462.5 million at the end of 2004.

Within its retail activity the Bank grants loans to individual clients, first of all. At the end of December 2005, the receivables of ING Bank Śląski S.A. due to the loans extended thereto amounted to PLN 2,353.9 million and constituted 75.0% of credit receivables from households.

### **Bank Cards**

ING Bank Śląski S.A. offers to its individual clients, first of all, debit cards (Maestro and VISA Electron), embossed credit cards (MasterCard, VISA Classic and VISA Gold) and Maestro prepaid cards (such as the Gift Card, the Traveller's Prepaid Card, the Gift Vouchers, etc.).

In October 2005, the Bank issued a cut-out and semi-translucent VISA e-card – the first card of that type to be offered in Poland. The e-card is a combination of a virtual card to be used for Internet payments and a physical card that can be used to pay for purchases at any merchant.

By the end of December 2005, ING Bank Śląski S.A. issued 1,303,000 payment cards to its individual clients, which placed the Bank on the fourth position in the bank cards market, with a 7.8%-market share.

Credit cards are among the strategic products of the ING Bank Śląski S.A. retail offer. The Bank puts emphasis on the sale of embossed credit cards, that would be safer and of wider use, such as: Visa Classic, Visa Credit Gold and MasterCard Credit. These cards were rendered available to the clients at the beginning of 2004. The number of credit cards from the new offer issued by the Bank went up from 31,700 as at the end of 2004 to 117,900 cards at the end of December 2005. In total, the Bank issued 124,700 credit cards by the end of 2005.

For the small business segment ING Bank Śląski S.A. issues debit cards (Maestro Business), charge cards (VISA Business and Eurocard/MasterCard Business Gold) as well as prepaid Maestro ones (e.g. Business Trip Card). In December 2005, the Bank extended its card offer for small businesses by adding a MasterCard Business debit card settled in EUR thereto.

## **Wholesale Banking**

### ***Scope of Offer and Modifications Introduced***

ING Bank Śląski S.A. provides corporate clients with one of the most innovative offers of banking services and products on the market.

The Bank offers a wide range of deposit products addressed to corporate clients, such as: current accounts in PLN, USD and EUR (inclusive of the Pro-Business and Pro-Business Plus packages), a consolidated account, savings products, PLN standard

deposits, and also non-standard deposits in PLN, EUR and USD, as well as deposit products of investment nature (the Investment Term Deposit).

The Bank's deposit offer is accompanied by a wide range of clearing services, inclusive of Mass Payment Identification System (SIMP), cash collection, direct debit and Business-to-Business Direct Debit (GOBI). The clearing products based on electronic banking allow for the effective payment management, thus improving the efficiency of corporate finance management.

The ING Bank Śląski S.A. credit offer for corporate clients covers among others: overdraft, a working capital loan, a cheque loan, an investment loan, an indexed loan, a loan to finance export receivables insured by KUKE S.A., preferential loans with subsidies from the Agency for Modernisation and Restructuring of Agriculture as well as loans for financing of the projects connected with the EU pre-accession or structural funds. The offer of traditional loans is supplemented with other forms of business funding, including leasing and finance of commercial properties.

ING Bank Śląski S.A. also offers custody services. The custody services are purchased, first of all, by domestic mutual and pension funds, insurance companies and asset management institutions. The Bank also co-operates with Polish brokerage houses and renders custody services to foreign financial institutions, especially to global custodians, international dealers and brokers.

In 2005, the Bank adopted a new product strategy for corporate clients and introduced the following changes to the offer of products and services addressed to those clients:

- Introduction of the Plus Pro-Business Package, whose basic elements – apart from the current account – are the electronic banking system ING BankOnLine and debit payment cards. This package is characterised by a considerable flexibility (prices depend on the scale of operations on a given account, for instance) and may be supplemented with deposit and credit accounts as well as clearing services.
- Integration of the Autodealing system with the internet banking system ING BankOnLine. Due to this modification the clients may directly negotiate the FX exchange rates and use the negotiated exchange rate for currency conversions between their accounts.
- Offering to corporate clients a possibility of depositing their surplus funds on the Investments Term deposits – an investment product with a guaranteed interest rate, whose actual rate of return depends on the exchange rates or SE indices.
- Implementation of new principles of co-operation with ING Lease (Poland) and gradual offering of leasing services at corporate branches.
- Upgrade of custody products; for instance, the following services were rendered in that connection: service of derivatives purchased by clients as well as service of remote members and foreign securities.
- Modification of the EU-related offer by extending the deadline of validity of a credit promise by 12 months, among others.
- Providing the option of order dispatch during the third ELIXIR clearing session.

At the end of 2005, the Bank undertook works in order to enhance the offer in respect of various forms of asset-based lending, such as: leasing services, factoring and financing of commercial real estates. These services – due to a lower risk as compared to traditional loans – are attractive for a larger group of corporate clients. At the end of 2005, the Bank was involved in the works the purpose of which was incorporation of the factoring company Handlowy-Heller in the ING Group structures. Integration pertained to development of a new marketing strategy for that company, among others.

In December 2005, the works aimed at improving the Cash Collection service, launching 5-year working capital loans and a new system of internet banking for strategic clients were in their final phase.

### ***Changes to Client Service***

In 2005, the Bank was carrying out intensive works aimed at improving the sales model at the outlets dedicated to servicing corporate clients and enhancing the quality of services provided. They comprise, first of all:

- Restructuring of the Strategic Customers Department in line with the sector division, which allowed for the creation of knowledge centres on individual sectors. The new structure should contribute to fostering relationship with clients and facilitating accomplishment of sales target of the Bank.
- Completion of the establishment of the corporate sales network, whose task is to service clients from the mid-sized companies segment. Striving to satisfy the needs of those segment clients, the Bank equipped network employees with adequate tools and banking procedures and employed extra specialists in charge of assistance and consulting as to the matters related to cash management and FM products.
- Actions aimed at upgrading qualifications of the sales forces (including extensive training programmes, raising salaries and employment of extra Account Manager assistants).

Throughout 2005, the Bank established the fundamentals of appropriate support of sales processes with marketing actions in the corporate banking market in that it created a Wholesale Marketing Department and a Wholesale Products Development Department. The new Wholesale Marketing Department prepared a marketing strategy of the Bank in the corporate banking market and held a few marketing campaigns, among others, the one promoting EU-related programmes and the offer for mid-sized enterprises, accompanying launch of the Pro-Business Plus Package onto the market.

ING Bank Śląski S.A. was actively involved in the process of pre-financing and co-financing of projects run by beneficiaries of aid funds from the European Union. The Bank also co-operated with institutions managing and implementing individual EU programmes; for instance: the Polish Agency for Enterprise Development (PARP) and the Association of Polish Banks (ZBP). Bank representatives participated in the works of the Working Team “Structural Funds” at ZBP (they advised programme documents) and attended the meetings of the PARP Working Team for Evaluation of Projects for Actions as part of the Sectoral Programme – Increase of Competitiveness of Enterprises. The Bank also run a cycle of seminars devoted to EU programmes for entrepreneurs in all Corporate Regions of the Bank that were attended by

approximately 700 entrepreneurs in total. Manuals and informational brochures presenting investment grant programmes for various entities were also prepared. In addition, a research into the modes of EU funds utilisation by entrepreneurs was financed.

During the last months of 2005, the Bank was also involved in the organisation of renowned conferences for entrepreneurs operating in the sectors with a large potential of growth.

In mid-2005, the 2006 Corporate Project started. The Bank analysed the existing rules of corporate client service and estimated the capacity for improvement of the model in place. The plan of implementation of the solutions developed was defined and works to streamlining the product offer were commenced.

Based on the positive experiences gathered while the Strategic Clients Department functioned under the new structure and the information collected from other ING Group units, at the end of 2005, the Bank took a decision to apply a sectoral approach also for other segments of corporate clients (i.e. big and mid-sized companies).

### ***Deposits and Settlements***

As at 31 December 2005, the institutional clients' deposits<sup>5</sup> in the Bank totalled PLN 11,814.8 million. It is estimated that in December 2005, ING Bank Śląski S.A. held an 8.1%-share in the market of institutional clients' deposits.

Deposits of corporate entities<sup>6</sup> formed the major part of institutional clients' deposits accumulated at the Bank. They deposited the funds worth PLN 8,519.2 million in accounts at ING Bank Śląski S.A., which accounted for 72.1% of the total value of institutional clients' deposits.

An essential share in the Bank's liabilities was also held by the funds obtained from the non-monetary financial institutions; i.e. insurance institutions, pension funds, mutual funds and leasing companies. Their value was PLN 1,911.1 million and represented 16.2% of total deposits of institutional clients. Deposits of entities of the government and self-government sector amounted to PLN 1,384.5 million (or 11.7% of total corporate deposits).

Making the clearing and deposit offer of ING Bank Śląski S.A. more attractive resulted in an increase of the number of current accounts held by corporate clients. For instance, in December 2005, 5,138 Pro-Business packages were held by the clients from the segment of mid-sized companies; up by more than 10% than a year earlier. Corporate clients also showed more and more interest in electronic distribution channels and state-of-the-art clearing systems, reflected by the following:

- the number of clients with access to internet banking grew from 3,100 in December 2004 to 6,400 at the end of 2005,

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<sup>5</sup> Figures cover the Bank's liabilities towards: enterprises, non-profit institutions serving households, non-monetary financial institutions, government and local government units, social security institutions.

<sup>6</sup>Sub-sector of corporate entities comprises the following types of entities: state-owned enterprises and partnerships, private enterprises and partnerships and co-operatives and non-profit institutions serving households.

- the number of Mass Payment Identification System installations for the companies co-operating with several off-takers (such as insurance companies, power supply plants and mobile telecommunications companies) went up from 95 at the end of 2004 to 179 in December 2005.

### ***Lending***

As at the end of December 2005, credit receivables of ING Bank Śląski S.A. from institutional clients <sup>7</sup> totalled PLN 7,688.8 million versus PLN 8,050.0 million in December 2004. It is estimated that at the end of 2005 the Bank held a 5.1%-share in the market of institutional loans.

The Bank's credit exposure towards institutional clients at the end of 2005 was determined both by the situation observed on the corporate loans market (small interest in loans in view of the low investment level) and the credit policy binding at the Bank, especially the adopted high thresholds of accepted risk.

The Bank's receivables due to the loans extended to corporate entities amounted to PLN 6,167.7 million and represented 80.2% of the Bank's credit exposure towards corporate clients. An essential share in the Bank's credit portfolio was also held by the loans extended to the non-monetary financial institutions – the credit liabilities of clients from this sector towards the Bank amounted to PLN 829.2 million (or 10.8% of Bank's credit receivables from institutional clients).

Throughout 2005, ING Bank Śląski S.A. was gradually establishing its position in the area of EU grant programmes. As at the end of December 2005, the overall value of the loans extended and credit promises issued in respect of EU loans was PLN 633.2 million (versus 189.8 million at the end of 2004). The Bank also increased its credit exposure towards the clients from the segment of large and mid-sized companies – by 8.6% approximately versus the 2004 year-end.

At the end of 2005, the credit portfolio was dominated by PLN loans, which represented 82.6% of total corporate loans; their share in the portfolio grew by 4.9 percentage points from the end of December 2004.

As at 31 December 2005, ING Bank Śląski S.A. held 5 significant exposures; i.e. the value of which constituted 10% or more of the total value of the Bank's equity, in the following amounts: PLN 456.2 million, PLN 383.6 million, PLN 372.0 million, PLN 300.3 million and PLN 282.5 million. Two entities from this group were related with ING Bank Śląski S.A. by capital.

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<sup>7</sup>Figures cover due from companies, non-profit institutions serving households, non-monetary financial institutions, government and self-government institutions, social security companies.

## Money and Capital Markets

In 2005, ING Bank Śląski S.A. maintained its strong position in the Polish money market, among others, by sustained care to assure the top quality of services rendered to clients and presenting a high degree of professionalism in co-operation with other participants of the financial markets. The Bank had the Status of the Money Market Dealer, and at the end of the year NBP classified it in number one in terms of the Dealer's Activity Index (IAD). The Bank also acted as a Dealer of Treasury Bonds.

In the money market, the Bank paid special attention to development of operations with clients and continued works to expand the range of and improve products and services. Special attention was paid to making the offer more flexible, which enabled the Bank to satisfy individual needs of clients. For instance, the Bank:

- extended the offer for corporate clients with REPO and REVERSE REPO transactions,
- offered Investment Term Deposits to corporate clients by selling another subscription of that Deposit that was connected with the WIG and EUROSTOXX option and
- prepared individually addressed structures, consisting of the products already offered that were subsequently sold to clients as bundles. At the same time, the growing demand for the products of that type encouraged the Bank to separate binary options, being a component of the structures built, from the existing variety of products.

Since the market launch (as of February 2005), ING Bank Śląski S.A. has been participating in trading of futures for Polish bonds on the Warsaw Stock Exchange. In 2005, the Bank also started the process of taking over the function of the Excellence Centre within the ING Group in respect of FX options in HUF, SKK and CZK.

The Bank is also an active player on the short-term debt securities market. In December 2005, ING Bank Śląski S.A. was classified on the fourth position with an 11.9%-share in the debt due to the issue of the short-term debt securities.

To enhance the quality of the way in which larger and larger volumes of own funds are handled and to manage this portfolio more actively, the Bank reorganised the Treasury and FM Division. The function of the Bank's liquidity management was separated from the one dealing with proprietary operations in financial markets. Special organisational units dedicated to perform these tasks were established.

## **IV. BUSINESS OPERATIONS OF ING BANK ŚLĄSKI S.A. CAPITAL GROUP COMPANIES**

### **ING Securities S.A.**

ING Securities S.A. is one of the largest brokerage houses in Poland. In 2005, it held the following shares in the transactions of the Warsaw Stock Exchange ING Securities S.A.:

- stock market<sup>8</sup> – 11.8% (third position),
- bond market – 3.7% (sixth position),
- futures market – 5.3% (seventh position),
- option market – 13.0% (third position).

The Brokerage House of ING Bank Śląski S.A. services investors' operations both on the Warsaw Stock Exchange and on the largest world financial markets, including but not limited to New York, Chicago, London, Paris and Frankfurt. The offer covers all products of capital market available for individual investors in Poland, i.e. brokerage in stock exchange transactions, OTC and in foreign markets, investment loans, lending securities, analytical service, investment recommendations, assets management, and sales of participation units of the mutual funds.

At the end of December 2005, ING Securities S.A. maintained 41,200 investment accounts, including 4,800 internet ones. Throughout 2005, the Company acquired a few important clients in the segment of institutional investors.

In 2005, the offer of the Bank's Brokerage House on the secondary market was enhanced by the following:

- a loan for purchase of shares in public offering in the form of a credit line, rendered to clients for 12 months (in co-operation with ING Bank Śląski S.A.),
- distribution of GTFI mutual funds.

ING Securities S.A. offers its services to individual investors at 17 Client Service Points and two co-operating brokerage houses POLONIA NET S.A. and the Brokerage House of Nordea Bank Polska S.A. In the year 2005, ING Securities S.A. commenced co-operation with ING Bank Śląski S.A. under a new contract that made it possible to open 305 temporary Points of Instruction Acceptance at Bank Branches. ING Securities S.A. also has fully-fledged remote distribution channels such as Internet and phone services. ING Securities S.A. is the only brokerage house in Poland that guarantees instruction execution in Internet within 3 seconds; otherwise it reimburses the commission charged.

In 2005, services were made more accessible and the quality of service by ING Securities S.A. was enhanced thanks to:

- installation of a system of central registration of phone instructions at the network of Client Service Points,

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<sup>8</sup> Trade in shares and stock rights.

- launch of a procedure of investment account opening by mail, initiated by the client over the phone or via internet.

As far as the capital funding is concerned, the Company offers services that are not only related to the service of issues in the public- or non-public market but also others (such as maintaining the deposit of non-public companies, acting as the Issue Sponsor) as well as comprehensive financial and legal advisory services connected with the capital funding.

Throughout 2005, ING Securities S.A. pursued the following projects, among others:

- it serviced the sale of ING Bank Śląski S.A. shares, worth PLN 729 million, by ING Group,
- serviced a new issue of shares, worth PLN 17.9 million, by the Ferrum Steelworks,
- participated in the consortia offering securities: Grupa Lotos S.A. (market share of 9.75%), Zakłady Chemiczne Police S.A. (market share of 8.4%), Polmos Białystok S.A. (5.2%) and also of Zelmer S.A., Interia S.A., Opoczno S.A., and Puławy S.A.,
- serviced the call for subscription for the shares of Jupiter S.A. and ORFE S.A.,
- acted as a broker in OTC transactions in shares of: Polkomtel S.A., PPRM S.A. and Star Foods S.A.,
- advised CEDS at the purchase of 61% of shares of Polmos Białystok S.A. from the State Treasury,
- participated in the project of buyout of own shares by Agora Company,
- signed an agreement with Bank Gospodarstwa Krajowego for broking in the sales of minority shares in public companies, listed on the Warsaw Stock Exchange.

In 2005, ING Securities S.A. generated net profit of PLN 33.1 million compared to PLN 21.6 million a year earlier.

### **Śląski Bank Hipoteczny S.A.**

In 2005, Śląski Bank Hipoteczny S.A. focused its operations on making final arrangements and preparations to implement a new strategy of development, adopted in autumn 2004.

In contrast to previous years – when ŚBH S.A. specialised in financing residential estates for individual clients, – as of 2005 it functions as a Centre of Excellence in Commercial Real Estate Funding under the capital group of ING Bank Śląski S.A. the new rules of co-operation of Śląski Bank Hipoteczny with ING Bank Śląski S.A. were defined in two agreements concluded in the course of 2005. These are: the Master Co-operation Agreement with the Bank – specifying sales of ŚBH S.A. commercial loans in the corporate network of the Bank – and the Master Agreement on Co-operation as to Syndicated Mortgage Loans.

While striving to perform new functions, in 2005, ŚBH S.A.:

- run product training sessions for Account Managers of the Corporate Banking Centre of ING Bank Śląski S.A.,
- developed a Developers' Bundle with ING Bank Śląski S.A.,
- took efforts to establish its image as the institution financing the commercial real estates.

After a few-month interval, the first commercial loans were disbursed by ŚBH S.A. and the first syndicated loan agreement was signed, in which ŚBH S.A. and ING Bank Śląski S.A. participated. Since the beginning of 2005, Śląski Bank Hipoteczny has not been winning any new retail clients; it has been servicing the "old" portfolio of housing and construction-mortgage loans only. In connection with intensified marketing activities of other banks granting mortgage loans to individual clients, ŚBH S.A. observed the process of prepayment of the loans drawn.

In 2005, Śląski Bank Hipoteczny reported a net loss of PLN 0.6 million (in 2004, it was PLN 1.6 million).

### **Centrum Banku Śląskiego Sp. z o.o.**

Centrum Banku Śląskiego Spółka z o.o. is the owner of edifices in Katowice, at 34 Sokolska St. and 50 Chorzowska St. It deals with the lease of space in the said buildings. In total, the Company administers almost 35,000 square metres of office and commercial space.

In 2005, Centrum Banku Śląskiego continued its previous actions, aimed at winning new tenants. These comprised preparation of offices ready for occupation, takeover of costs of room arrangement and application of flexible terms of payment. The Company also allocated substantial funds to raise the standard and security level of the real estates owned.

Marketing activities led to winning of a few large tenants and increasing the space leased by the previous ones. As a result, in December 2005, the share of the space leased in the total space owned by the Company increased to 92% (88% at the end of 2004).

Centrum Banku Śląskiego closed the year 2005 with the net profit of PLN 19.1 million (versus PLN 29.9 million in 2004). The Company reports positive flows from current operating activity, while the final financial result is to a high degree conditioned by the EUR exchange rate affecting the costs of EUR loan service, used to finance the main assets of CBS.

### **ING Nationale-Nederlanden Polska Powszechnie Towarzystwo Emerytalne S.A. [ING Nationale-Nederlanden Poland Pension Fund Company]**

ING Nationale-Nederlanden Polska Pension Fund Company manages ING Nationale-Nederlanden Polska Open Pension Fund that was established pursuant to the licence of the Supervision Office over the Pension Funds dated 26 January 1999.

2005 was yet another good year for ING Nationale-Nederlanden Polska Open Pension Fund Company, both in terms of gains in members number and in terms of performance.

In 2005, the Fund acquired over 129,000 new members and more than 34,000 members who switched from other pension funds. The good results generated in the field of acquisition made the number of ING Nationale-Nederlanden Polska OFE members reach the level of 2,210,500 as at the end of 2005. As far as the number of members is concerned, the Fund occupied the second place on the market, servicing 18.9% of all members of pension funds (versus 17.6% as at the end of 2004).

Great loyalty of Fund members was, first of all, the consequence of very good investment results, a high quality of service and ownership of fully-fledged distribution channels. Leads and clients of the Fund are provided service by approximately 2,000 Insurance-Financial Representatives and at a few hundred outlets of ING Nationale-Nederlanden Polska S.A. and ING Bank Śląski S.A. Clients can contact the Fund over the phone (infoline, SMS and WAP) and internet as well.

Over 2005, the value of net assets of the Fund grew by approximately PLN 5.6 billion and as at the end of December 2005 totalled PLN 19.7 billion. With a 22.8%-share in the value of net assets of open-ended pension funds (up by 0.3 p.p. from a year earlier), ING Nationale-Nederlanden Polska OFE was on the second place on the market in terms of assets. Increase of the Fund's assets was the consequence of the sound and consistent investment policy pursued by the team of experts, relatively high average contribution paid by its members and one of the highest shares in the market of the members paying contributions.

In 2005, ING Nationale-Nederlanden Polska OFE won the first position in the ranking of the pension funds best in terms of investments made. The yield rate was 16.4% (while the average of all funds was 14.0%). ING NNP OFE was also first in terms of investment results produced in the period from 30 December 2001 to 30 December 2005.

Operations of ING Nationale-Nederlanden Polska OFE in 2005 were highly appreciated by the market. On 1 December 2005, the Fund for the third time in a row was honoured with a prestigious award of the IPE Investment & Pensions Europe monthly – Best Pension Fund of the Year 2005. The IPE monthly granted awards for the fifth time, based on the opinions gathered from independent consultants of the financial market in Europe.

In its income statement for 2005, ING Bank Śląski S.A. recognised its share in the profits of Nationale-Nederlanden Poland Pension Fund Company in the amount of PLN 26.7 million.

### **ING BSK Development Sp. z o.o.**

ING BSK Development Sp. z o.o. deals with consulting as to running business and management, proprietary lease and intermediation in trading of real estates as well as commissioned management of real property.

The Company was established in August 2004. In February 2005, ING BSK Development signed an agreement with Centrum Banku Śląskiego Sp. z o.o. to lease the edifice at 34 Sokolska Street in Katowice with the total functional area of 18,811 square meters for sub-lease.

The Company sub-leases space to such entities as: ING Bank Śląski S.A., ING Securities S.A., ING Lease (Polska) Sp. z o.o. and ING Real Estate Sp. z o.o.

In 2005, ING BSK Development Sp. z o.o. recorded a positive net result of PLN 44,000 (in 2004, it reported a net loss of PLN 54,000).

#### **Solver Sp. z o.o.**

Organisation of recreation for the Bank's employees and their families in the retreat centres in Krynica, Wisła and Głębinów forms the core business of Solver Sp. z o.o.

In the year 2005, the net result of Solver Sp. z o.o. was PLN 9,000, whereas in the previous year it was PLN 4,000.

## V. MANAGEMENT OF KEY RISKS

### Credit Risk

#### *Credit Policy and Procedures*

Under the sector policy currently in effect, in 2005 the Bank funded business entities belonging to the industry sectors of moderate credit risk. Due to the economic revival, accession of Poland to the European Union and inflow of aid funds, after a period of tough restrictions on financing of some sectors, in 2005 the Bank alleviated the requirements relating to some entities classified to the sectors previously deemed as more risky. These included the meat processing sector (since this sector eliminated the delay in implementation of the EU requirements) and developers (improvement of financial results). The Bank was also more willing to extend long-term credit facilities since it started to co-finance the EU projects. However, in the year 2005 the Bank maintained in force its principles in regard to origination of FX and indexed loans for corporate clients. Such loans were only offered to entities getting earnings in the loan currency.

Throughout 2005, the Bank updated the sector analyses prepared for individual sectors of the economy. The aforementioned analyses were to facilitate the process of credit applications review and the credit decision-taking process. They specify the minimum requirements for the preferable risk profile and stipulate the lending terms, collateral forms and recommended types of financing the business of clients operating in a given sector.

With regard to the credit policy for retail clients, the Bank maintained the principle of offering PLN loans only, and at the same time:

- Simplified the credit offer for individual clients, among others by reducing the number of products offered and setting out a list of top-priority and supporting products.
- Strived to tighten the credit co-operation with the current clients, by offering additional credit products (credit cards, cash loans). This process was based on the concept of preliminary acceptance made on the grounds of analysis of cash flows on personal accounts, value of the deposits held and their relation to the credit exposures.
- Completed the centralisation of acceptance process for individual clients and small business.
- Totally revised the policy for small business, i.e. it standardised the product offer, introduced statistical tools for risk measurement and centralised the decision-taking process. Actions were also initiated to centralise the management of the small business credit portfolio (monitoring and debt collection).
- Introduced changes to the strategy of recovering overdue payments by monitoring repayments more intensively and taking actions to recover the overdue receivables.
- Implemented the methodology of calculating assets impairment and covering the related loss with provisions, pursuant to the International Accounting Standards.

Due to the implementation of International Accounting Standards as of the beginning of 2005 and the continuation of works on the Bank's adjustment to the Basel II Accord requirements, the Bank introduced the following changes to the tools for risk measurement and monitoring:

- At the beginning of the year a new model for assessment of the corporate client credit risk was implemented in the branch network, where the risk categories are associated with a specific probability of default (PD). An element of this model is the process of appeal, applicable to certain cases where the risk category determined by the model is different from risk assessment given by the branch network representatives. In such cases the final risk category is assigned by the Bank Head Office Appeal Committee.
- The collateral policy was updated, by modifying the Severity Rating System for the purpose of calculating the loss given default (LGD), among others.
- The methods for calculation and update of the provisions for credit receivables were introduced, based on the tools applied in the ING Group, especially for the portfolio of individual significant financial assets (ISFA).
- In order to streamline the works connected with the implementation of the New Capital Accord requirements the Bank established a new body to co-ordinate actions in regard to cover on an end-to-end basis the risks of pillar 1 (credit, market and operational risk) and the risks of pillar 2 (interest rate risk in the bank book, liquidity risk, concentration risk, transfer risk, business risk, etc). It will also determine the organisational framework and procedures relating to the management of internal capital and the Bank's capital adequacy. There were also continued works aiming at implementation of procedures assuring high quality of system data required for the capital requirement estimation process.
- In the retail area the Bank implemented portfolio management for the assessment of credit risk in the small business segment. In the acceptance process for small business there was introduced the generic system of statistical risk assessment and works on acceptance behavioural model for the probability of default (PD) were completed in regard to overdrafts of individual clients (this model will be verified in the aspect of the New Capital Accord). Works were also continued on the new IT application supporting the credit process in the retail area.

In connection with the works aimed at validation of risk measurement tools, planned for the year 2006, the Bank was building the database which covered not only the information determined by the model, but also the list of exceptions from the model resulting from the expert decisions of the Appeal Committee. The functional control system was also implemented. Due to the considerable automation of the risk classification process and calculation of the provisions level, the system is monitoring the quality of data inputted to the IT systems.

### ***Organisation of the Credit Process***

In 2H 2004, the 'Improvement of Credit Process Efficiency' Project was launched at ING Bank Śląski S.A. Its main target was to streamline and shorten the credit process for corporate clients. In the course of project works, the co-operation of all credit process participants was considerably changed, among others. They (notably Risk employees) were equipped with new IT tools and applications to monitor the credit process. Electronic transfer of documents was also ensured, which was related to the

concurrent standardisation and unification of the credit documentation. The new solutions were gradually implemented over the year in all Regions of the Bank.

In order to further streamline the credit process for strategic clients the Bank decided to replace the process of taking credit decisions by the Bank Credit Committee with the system of taking dual-signatory decisions by the higher-rank representatives of the commercial and risk areas (Signatory Approval Process - SAP). This solution is in line with the philosophy of ING Group in this regard.

In the retail area, the Bank finalised the works on standardisation of the credit process and transferring taking decisions and service after granting a loan to the Head Office units (central sales platforms). In order to support the activities of the said units the Bank also developed risk management analytical units at the central level. The Bank also re-established co-operation with external companies in the process of recovery of retail debt claims and commenced the works connected with the sale of inactive portfolio of retail debt claims to the securitisation fund.

At the end of 2005, the Bank established the Credit Risk Inspection Department whose duties include among others: rendering independent, objective opinions about efficiency, adequacy and effectiveness of the activities of units originating loans and assessing the credit risk, identification of credit risks which may possibly cause losses for the Bank and co-operation with other departments in the Risk Division in regard to the credit policy.

#### ***Quality of the Credit Portfolio and Provisioning***

Implementation of the International Accounting Standards resulted in the revision of the principles for reporting the credit portfolio quality as well as provisioning. According to the International Accounting Standards the following are established: asset impairment loss, write-off for the Incurred But Not Reported losses (IBNR) as well as provisions for the off- balance sheet liabilities.

These standards do not allow for keeping the general reserves, therefore in the 2005 opening balance sheet the Bank transferred the provisions established as per 31.12.2004 (specific provision and general risk reserve) as well as contingent interest for equity. Simultaneously, the Bank established impairment losses and a write-off for the Incurred But Not Reported losses (IBNR). The value of write-offs in the Bank's 2005 opening balance sheet was by PLN 123 million lower than the provisions established as per 31 December 2004.

The amount of decrease presented in the report for 2005 is different than the amount presented in the annual report for 2004.

At the end of 2004, ING Bank Śląski S.A. held in the off-balance sheet records the fully provisioned loss loans of PLN 1,195.3 million. As of 1 January 2005, the Bank measured the portfolio of credit receivables, transferred to the off-balance sheet records, at PLN 44.1 million. This amount was recognised in the Bank's balance sheet under assets in correspondence with equity (retained result of the previous years) resulting in its increase by PLN 38.4 million, equal to the discounted market value of this portfolio.

# Quality of the Credit Portfolio of ING Bank Śląski Capital Group S.A.

	31.12.2003	31.12.2004	31.12.2004 IFRS	31.12.2005
<b>Total exposure/exposure acc. to IFRS</b>	<b>13,720</b>	<b>11,307</b>	<b>11,349</b>	<b>10,562</b>
<b>Total provisions</b>	<b>1,255</b>	<b>1,072</b>	<b>949</b>	<b>813</b>
<b>Provisioning rate (%)</b>	<b>8.9</b>	<b>9.5</b>	<b>8.4</b>	<b>7.7</b>
<b>Corporate Banking</b>	<b>10,211</b>	<b>8,134</b>	<b>8,150</b>	<b>7,592</b>
Regular portfolio / Non-default portfolio	7,113	7,021	7,331	6,983
Irregular portfolio / Default portfolio	3,097	1,113	818	609
Sub- standard	866	144		
Doubtful	1,489	430		
Loss	742	539		
<b>Total provisions</b>	<b>965</b>	<b>771</b>		
including:				
Specific provisions / Impairment loss	752	601	593	493
Allocation of the general reserve/IBNR	178	153	73	70
Provisions for off-balance sheet liabilities	35	17	33	14
<b>Provisioning rate for the irregular portfolio/ default portfolio (%)</b>	<b>30.0</b>	<b>67.7</b>	<b>72.5</b>	<b>81.1</b>
<b>Retail Banking</b>	<b>3,510</b>	<b>3,172</b>	<b>3,199</b>	<b>2,970</b>
Regular portfolio / Non-default portfolio	3,079	2,865	2,908	2,698
Irregular portfolio / Default portfolio	431	307	291	272
Sub- standard	103	68		
Doubtful	69	20		
Loss	259	219		
<b>Total provisions</b>	<b>290</b>	<b>301</b>		
including:				
Specific provisions / Impairment loss	264	245	201	191
Allocation of the general reserve/IBNR	26	56	31	28
Provisions for off-balance sheet liabilities			19	15
<b>Provisioning rate for the irregular portfolio/ default portfolio (%)</b>	<b>67.4</b>	<b>97.9</b>	<b>69.0</b>	<b>70.1</b>
Share of irregular loans in total portfolio	25.72%	12.56%		
Share of default portfolio in %			9.78%	8.35%

As at the end of December 2005, the credit exposure of the Capital Group of ING Bank Śląski S.A. amounted to PLN 10,562 million. The value of credit exposures at default was less than PLN 881 million. Over the year 2005, the quality of the credit portfolio of the Bank's capital group improved – the share of the exposures at default in the whole credit portfolio declined from 9.8% in December 2004 to 8.4% at the end of December 2005.

In 2005, the balance of asset impairment loss, presented in the Capital Group's profit and loss account, was positive and amounted to PLN 118.0 million. In December 2005, Group held PLN 813 million worth of provisions for the credit portfolio, which is equivalent to the exposure at default provisioning rate of 77.6% (versus 71.6% at the end of 2004).

## Market Risk Management

The basic target of the effective market risk management in ING Bank Śląski is to maximise profit with simultaneous limiting the potential losses that may result from undesirable changes of interest rates, FX rates, and other market parameters as well as customer behaviour.

The process of market risk management in the Bank covers the following elements:

- market risk identification;
- risk measurement (covering back-testing in order to ensure adequacy of the applied models);
- current monitoring of the market risk within the accepted limits;
- limiting or accepting the risk limit based on the risk analyses in relation to the rate of return.

Principles of the market risk management and the methods of measurements applied by ING Bank Śląski are in compliance with the methodology used by ING Group and with the European standards in this area.

For the measurement of the market risk – besides the liquidity risk – ING Bank Śląski applies mainly the Value-at-Risk (VaR) methodology. It makes it possible to calculate the potential loss resulting from accepted proposals and changes in prices, interest rates, market FX rates (and volatility in case of FX options), as well as mutual dependencies among the mentioned parameters. In order to appraise the adequacy of applied models, the risk level set with the use of VaR is subject to back-testing process, i.e. comparing the actual and hypothetical results (set out only based on the positions maintained as of the end of the day) with VaR.

Moreover, the Bank measures Emergency Value at Risk (EVAR) that determines the value of potential loss that may appear on a given market position in case of extreme changes of market parameters. EVAR is determined based on a group of macroeconomic scenarios (selecting the worst of them) assuming that the more extreme changes of market parameters than the ones presented in the scenarios should not happen more often than once every 10 years.

The applied risk measurement methods vary depending on the area of activities and on the degree of complexity of the instruments offered by the Bank. In connection with that, VaR and EVAR are measured and monitored in three areas:

- interest rate
- FX spot,
- FX options.

In the year 2005, in the process of monitoring of potential changes in the Bank's result relating to the interest rate and currency positions and the option portfolio value, the Bank focused in particular on the following issues:

- In connection with a significant growth of value of deposits paid on demand which are invested in accordance with the replicating portfolio rules (reflecting better the characteristic of the interest rate profile of those volumes) – introduction of a full reporting set ensuring an appropriate functioning of those investment mechanisms.
- In order to improve the quality of management of the Bank's capital group – regular monitoring of the interest rate and FX risks in subsidiaries in order to keep those risks at a low level.
- Creation of mechanism ensuring regular measurement and assessment of the interest rate risk level resulting from non-standard price mechanisms used both

for corporate and retail products. However, due to the simplification of the product offer the Bank's risk level in this area went down in the year 2005.

- Regular monitoring of the risk relating to options embedded into corporate and retail term deposits (i.e. the risk connected with the possibility of breakage).

One of the essential elements of the market risk management process at ING Bank Śląski S.A. is the process of liquidity monitoring and management. The liquidity risk is understood in the Bank as a risk of failure to meet the cash liabilities, arising from the balance sheet and off- balance sheet items. The Bank's policy for managing the liquidity risk consists in maintaining the liquidity positions in such a manner so as to meet the Bank's cash liabilities with cash in hand, inflows from transactions of a specific maturity date and/or with sale of the available-for-sale assets. Striving for the proper liquidity management, the Bank:

- prepares and analyses the control reports such as:
  - daily reports on liquidity ratios,
  - monthly reports on liquidity gaps,
  - monthly reports on the structure of finance, concentration and stability of the deposit base,
  - monthly reports on informational indices, calculated on the basis of data from the obligatory reporting.

For each index a permissible limit is determined, subject to continuous monitoring.

- prepares the procedures that ensure the correct cash delivery to branches,
- adjusts the emergency liquidity maintenance plan to changes in the Bank's organisational structure and changes in the warning signal definition.

In 2005, ING Bank Śląski S.A. carried out – where possible – back-testing, comparing the forecast results with the actual ones. It was aimed at verifying the data accuracy in the market risk area. In order to ensure a consistent approach to the market risk measurement and also to mitigate the operational risk, the measurement of market risk for ING Bank Śląski S.A. is transferred from internal systems to integrated applications used by the ING Group members.

## **Capital Adequacy**

In 2005, ING Bank Śląski S.A. complied with the obligatory prudent standards in regard to the capital adequacy. At the end of 2005, the capital adequacy ratio was 18.6%, which means that the Bank Capital Group had sufficient amount of equity to cover specific credit and financial risks.

## **Operational Risk**

Operational risk is understood in ING Bank Śląski as the risk of bearing direct or indirect material loss or as the loss of reputation resulting from not adjusting or faulty functioning of the internal processes, people or technical systems, and also as the result of external events.

The Bank manages operational risk based on the Recommendation of National Bank of Poland that takes into account the directives of the Basel Committee regarding the operational risk management and standards effective at ING Group.

Operational risk management covers the operations in the field of identification, measurement, monitoring of the said risk as well as taking appropriate actions aimed at limiting it. All organisational units of the Bank and Bank subsidiaries are involved in the implementation of tasks connected with the operational risk management. The works regarding the operational risk management are co-ordinated in the Bank by the Operational Risk Management Committee, whereas the Management Board and Supervisory Board of the Bank supervise these activities on a permanent basis.

In the field of the operational risk management the Bank concentrates on the following issues:

- implementation of mechanisms of estimating the level of operational risk and limiting it in the individual areas of the Bank activities;
- determining the ratios of important risk and monitoring them;
- limiting the losses by way of improving the system of controlling the Bank operations;
- improving the audit process as the result of the implementation of the integrated system of recording and monitoring the realisation of recommendations and post-control recommendations;
- allocation of the economic capital adequate to the risk level;
- testing business continuity plans for critical and important business processes;
- improvement of means of physical protection of the Bank, paying special attention to integrated system of monitoring the security of the branches and ensuring immediate help in case of emergency;
- organisation of awareness programmes and training in the field of operational risk management.

## **VII. ORGANISATION AND INFRASTRUCTURE DEVELOPMENT**

### **Changes in Organisation of ING Bank Śląski S.A.**

The organisational changes introduced at ING Bank Śląski S.A. in the year 2005 are in line with the development strategy and they serve the purposes of appropriate realisation of commercial targets and improvement of the operational effectiveness.

In order to adjust the Bank's structure to the current market challenges, in the year 2005 the Bank established two new divisions: Credit Risk Management and Market Risk Management Division (comprising units which previously reported to the Bank Management Board) and Organisation and Strategic Planning Division. At the end of 2005, the Head Office units of ING Bank Śląski S.A. operated within the following 10 organisational Divisions:

- Wholesale Banking Division;
- Treasury and Financial Markets Division;
- Credit Risk Management and Market Risk Management Division;
- Retail Banking Division;
- Banking Marketing and Advisory Division;
- Finance Division;
- Organisation and Strategic Planning Division;
- Operations Division;
- Services Division;
- IT Division.

A separate group of units are the ones that are directly reporting to the Bank Management Board. Those units include: Management Board Bureau, Legal Department, Internal Audit Department, Human Resources Management Department, and Credit Inspection Department.

In 2005, as a result of bigger tasks and the changes introduced in the operations area, new organisational units were established in the Bank's Head Office. Those included: Payment Cards Department, Credit Inspection Department, Treasury and Assets & Liabilities Department and Client Operating Service Centre. The internal organisational structures of numerous departments were also changed.

### **IT and Operations**

In March 2005, the long-prepared migration of the IT environment at the branches into the new state-of-the-art technology-based platform started at the Bank. This process comprised first of all the standardisation of systems and applications as well as replacement of the IT equipment. Implementation works were finalised in October 2005. In total, the Bank implemented the new standard in 331 branches and migrated some 5,900 users. The standardisation of the IT platform will allow for optimisation of the user environment management processes (among others due to the implementation of central user support, remote distribution of programs and patches)

which will lower the costs and improve the quality of the IT network operation. The development of IT tools supporting the sales of bank products will be also easier.

Other important projects initiated in 2005 in the IT infrastructure area included:

- Implementation of the new system for processing embossed cards allowing the Bank to faster react to the changing market requirements.
- Taking initiatives aimed at replacement of the main Bank's server with a new model with expected capacity. According to the assumptions, thanks to the modular structure it will be also used by other units of ING Bank Śląski group, thus allowing to effectively use the financial outlays and ensuring high-level support from the equipment vendor.
- Implementation of new solutions to increase the security of branch computers and system located in the Bank Head Office.

In the year 2005, in the operations area – apart two large projects Retail 2006 and Corporate 2006 – there were continued the following projects determining the efficiency of operation of ING Bank Śląski S.A.:

- The Project of Optimisation of Regional Operating Centres (RCO). In the course of the project works the ultimate structure of the operations area after RCO centralisation was developed, application changes were prepared, the transport model was set up, the pilot implementation was started in 10 main RCO locations.
- The Cash Outsourcing Project, aimed at decreasing costs and operational risk and at creating the standard Bank's offer of cash processing addressed to the clients featuring high cash flows and operating as chain networks. By the end of 2005 the Bank outsourced cash processing services at selected cash centres.
- Implementation in all regional branches of the new application supporting the credit processes which facilitates efficient and fast drafting of credit agreements for corporate clients and mortgage loans for individual clients.
- Adaptation of the front-office application to the new application & decision-making process with regard to issue of credit and charge cards and extension of cash loans.
- Launch of a new system servicing the sales of mutual funds' participation units.
- Implementation of a new application to service seizures and allowing to centralise and fully automate the seizure-related service activities.
- Projects providing for outsourcing of archives, new standards and uniform archiving standards (X-files).

The Bank was also developing reporting applications so that the financial statements and management reports could not only be prepared efficiently and appropriately, but also in the manner reflecting adoption of the International Accounting Standards by the Bank.

### **Development of Electronic Distribution Channels**

Thanks to a fully-fledged multi-channel distribution system, ING Bank Śląski S.A. guarantees its clients an easy access to products and services. Its key elements are up-to-date electronic banking systems such as Internet banking (ING BankOnLine),

phone banking system (HaloŚląski), SMS banking system and electronic banking systems (MultiCash, TransDysk).

In 2005, the Bank continued works aimed at improving the functionality of electronic distribution channels. The Bank implemented the following changes, among others:

- the Bank presented the clients of ING BankOnLine with credit cards (statements, current transactions) and the functionality of card credit debt repayment;
- the Bank made it possible for the corporate clients to place multiple signatures both under single instructions and bundles of instructions (domestic and international ones);
- the Bank expanded the functionality as to master transfer orders in order to satisfy requirements of corporate clients.

The number of clients making use of electronic distribution channels increased considerably over 2005. The number of ING BankOnLine users, for example, went up by 136.8%, whereas the number of HaloŚląski phone service users increased by 26.4%. Dynamic growth of ING BankOnLine users was also a proof that the nationwide advertising campaign of internet banking – held in March and April 2005 – was effective.

Number of clients:	31.12.2004	31.12.2005
HaloŚląski	560,788	708,864
ING BankOnLine	152,832	361,944
SMS	40,650	79,789
Multicash	9,323	9,404

In December 2005, ING Bank Śląski S.A. had a network of 561 ATMs. The Bank was running an ATM optimisation project, aimed at, among others, improving service quality, increasing the degree of ATM network utilisation, and expanding the ATM functionality with additional banking services.

Due to further automation of the operations area, and the increased number of active users of electronic distribution channels, in 2005 electronic payments at the Bank made up for nearly 79% of the total number of payment transactions (excluding transactions made by means of payment cards). In 2004, the ratio was 75%.

### **Branch Network**

In December 2005, ING Bank Śląski S.A. had 331 branches. In the year 2005, the Bank opened one branch and closed two bank outlets.

The consistent image of branches, appealing to clients, is an important element of building the overall image of the Bank. Therefore, in the year 2005 the Bank allocated considerable outlays on completion of the branch re-visualization process. In some branches the re-revisualization was preceded by refurbishment and modernisation which significantly improved the level of customer service.

## HR Management

### *Headcount*

As at 31 December 2005, the Capital Group of ING Bank Śląski S.A. employed 7,446 people. Over the year 2005, the headcount at companies of the Bank's capital group increased by 0.8%.

In December 2005, the number of employees of ING Bank Śląski S.A. reached 7,217 persons, an increase by 2.0% compared with December 2004. Growth of the number of the Bank's employees resulted mainly from the establishment of structures responsible for marketing support and expansion of the sales forces. At the same time, in the second half of 2005 – due to implementation of new IT solutions, centralisation and automation of the operations area and re-organisation of credit risk management units at the regional level – the demand for human resources changed in those areas and the Bank initiated the process of group lay-offs.

On 14 November 2005, the Bank entered into the 'Agreement concerning termination of employment contracts due to reasons independent from the employees of ING Bank Śląski' with the in-house trade union organisations. In the period from December 2005 through the end of second quarter of 2006 the Bank is planning to gradually terminate the employment contracts due to technological and organisational reasons with a group of 400 employees of Regional Operating Centres and Risk Management Sections.

Due to the actions relating to the reorganisation and leading to changes in the headcount structure, in May 2005 the HR Platform was established at ING Bank Śląski S.A. Its main objective is to seek jobs for employees of reorganised units inside the Bank, filling in vacancies in organisational units.

The Platform's tasks also include ensuring fast and transparent communication addressed to all employees, in particular to those of reorganised units. It should make it easier for the employees to find themselves in the new reality, acquaint them with the possibilities they are entitled to and encourage to be active in building their own careers.

In order to reduce the number of people leaving the Bank by redeploying them to units seeking new employees some actions were taken to ensure preferential treatment for people working in reorganised units in the recruitment process.

In addition, the Bank proposes that the redundant employees take part in the Outplacement Programme, i.e. vocational activation programme proposing various forms of support when seeking jobs outside the Bank. The employees may participate in training schemes preparing them for re-entering the job market, they are provided with current information on the job market and the channels used to get access to job offers. Under the supervision of experts they learn how to professionally write CV and the cover letter, and they also acquire hands-on knowledge of the interview techniques and take part in simulated interviews. Moreover, the Bank co-finances the costs of vocational training schemes for the redundant employees which may increase their chances for finding jobs.

As the employer, the Bank under the agreement concluded with trade unions pays to the redundant employees additional severance pays on top of those provided for in the labour law. The amount of the reference pay depends on the period of employment with ING Bank Śląski S.A. and its legal predecessors. The employer covered by additional protection the employees who would become eligible to retire earlier by the end of 2007 and the employees being single parents and being parents of special care children. In case of this group of employees the Bank will make best efforts not to deprive them of their jobs.

### ***Remuneration Policy***

The new incentive system, implemented at the beginning of 2005, became an important tool of the remuneration policy at ING Bank Śląski S.A. Its basis assumption is to set out and integrate the tasks of various organisational units to make those units co-operate at individual levels and in individual areas. The new system also provides for making a bigger part of the bonus depending on the performance of measurable tasks which allows to render objective assessments and makes the bonus predictable (easy to calculate) both for the employee and the employer.

Moreover, growth of the level of remuneration at the Bank in the year 2005 was also caused by including at the beginning of 2005 the holiday and Christmas bonuses to base salaries and spring pay rise, linking the pay rise with the employee appraisal for the past year.

In mid-2005, project works were initiated at the Bank in order to improve the effectiveness of the system of base salaries by the implementation of the job evaluations in accordance with the a new approach which makes it possible to compare the salaries with market conditions. It is based on clearly identified criteria and job position scoring. The application of the new evaluation method should also allow for using more transparent rules for recruitment of employees, planning the headcount level and defining training needs.

At the end of 2005, there were prepared the principles of expanding the non-salary package of additional benefits with private medical care financed by the Bank in order to ensure competitiveness of the jobs offered by the Bank.

### ***Training schemes***

ING Bank Śląski S.A. believes that all the employees should have a wide access to various forms of training and they should be supported in their personal development as it contributes in a great extent to the accomplishment of the business targets of the Bank as well as satisfying the ambitions of the employees.

In 2005, the Bank trained 6,698 employees. Some of them participated in several training schemes, thus the total number of training participants amounted to 21,769. Each of the participating employees spent 1.9 day in training on the average.

In order to adjust the programmes of training schemes to specific needs of ING Bank Śląski S.A., their dominant parts were in-house training sessions, namely:

- More than half of the number of participant took part in training schemes run by the Bank employees, specialising in various topics. They were held in the Bank's training centres and in branches.

- More than 1/3 of participants took part in closed training schemes arranged in the Bank's centres and designed only for the Bank's employees. They were run by lecturers from various training institutions, however the Bank decided upon the topics.

The training sessions held in 2005 at ING Bank Śląski S.A. covered, first of all, the sales network and were devoted to:

- Retail Network – the new product offer for small business, efficient sales with elements of negotiations (for employees selling mortgage loans and Private Banking services) and for managerial staff with regard to upgrading managerial skills and sales coaching;
- Wholesale Network – pro-active sales, a new credit process in the segment of corporate clients and for managerial staff with regard to sales coaching.

Extensive training schemes were also arranged for branch employees in connection with the implementation of the new IT platform. They took the form of e-learning.

The Bank also initiated some organisational actions which would significantly affect the shape of training schemes, namely:

- It decided to run broad-scale e-learning training schemes and prepared the hardware & software platform for that purpose. The platform was implemented in line with the plan in December 2005. It was made available for the employees at the beginning of 2006.
- It established the Internal Coaches Section in the Retail Sales Department structure, responsible for running regular training schemes as part of the Best Service Programme.
- It launched the Corporate Banking Training Project which initiated standardised training schemes for the corporate banking network in the area of financial analysis and assessment of the company financing risk.

## **VI. FINANCIAL STANDING OF CAPITAL GROUP OF ING BANK ŚLĄSKI S.A. IN 2005**

### **Application of IAS and Comparability of Financial Data**

As of 2005, ING Bank Śląski S.A. has been developing its financial statements in accordance with the International Financial Reporting Standards/International Accounting Standards in the version adopted for application within the European Union

The 2004 financial statements of ING Bank Śląski S.A. were made comparable as to:

- impairment of goodwill of the company acquired as a result of takeover of Wielkopolski Bank Rolniczy S.A. (WBR),
- amortisation for 2004 of the goodwill related to the acquisition of the ING Bank NV Branch, WBR and ING Securities Poland,
- measurement of financial instruments related to the long-term incentive scheme,
- real property revaluation to fair value,
- change in presentation of measurement of subsidiaries at the acquisition cost (applicable to the solo financial statement only).

The data related to the application in the financial statements for the year 2005 of IAS 39 (measurement using depreciated cost based on the effective interest rate, impairment losses of financial assets listed according to the depreciated cost based on the effective interest rate) were not made comparable. The said exemption is governed by paragraph 36A IFRS 1.

### **Balance Sheet Structure**

The consolidated balance sheet and consolidated income statement of the Capital Group of ING Bank Śląski S.A. covers ING Bank Śląski S.A. together with: ING Securities S.A., Śląski Bank Hipoteczny S.A., Centrum Banku Śląskiego Sp. z o.o., Solver Sp. z o.o. and ING BSK Development Sp. z o.o. all of which were consolidated with the full method, and also ING Nationale-Nederlanden Polska PTE, which was consolidated with the equity method.

On 31 December 2005, the net balance sheet total of the Capital Group of ING Bank Śląski S.A. amounted to PLN 42,126.9 million, up by PLN 6,653.8 million, or 18.8%, from the end of the previous year. The balance sheet total of the Group and the structure of assets and liabilities have been determined by the operations of ING Bank Śląski S.A. As at 31 December 2005, the balance sheet total of ING Bank Śląski S.A. amounted to PLN 42,084.0 million versus PLN 35,435.4 million at the end of December 2004 (up by 18.8%).

Increase of liabilities towards clients from the non-financial sector was the primary source of growth of the balance sheet total and funding of operations of the Capital Group of ING Bank Śląski S.A.

## Assets

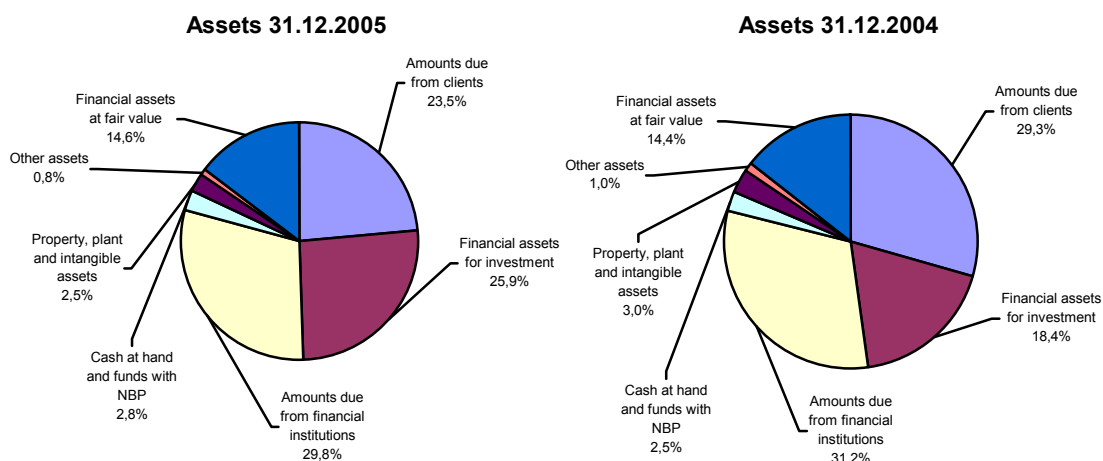
During 2005, important changes occurred in the structure of assets of the Capital Group of ING Bank Śląski S.A. They comprised a substantial drop in the share of credit receivables that were replaced by debt instruments. This change resulted, first of all, from the absence of visible effects in terms of lending growth, with the simultaneous growth of the total assets and liabilities of ING Bank Śląski S.A. following the considerable gains in deposits.

As of 31 December 2005, loans and cash advances extended to clients of the Capital Group amounted to PLN 9,902.9 million compared with PLN 10,407.9 million as at the end of December 2004. Their share in the assets was 23.5% versus 29.3% a year earlier.

As at the end of 2005, receivables of the Capital Group from the financial sector amounted to PLN 12,573.6 million versus PLN 11,077.8 million recorded a year earlier. The share of receivables from financial institutions in assets went down from 31.2% at the end of 2004 to 29.8% as on 31 December 2005.

Financial assets for investment were valued at PLN 10,922.9 million compared with PLN 6,539.4 million at the end of the previous year. Their share in the balance sheet total was 25.9%, up by 7.5 percentage points from 31 December 2004.

Financial assets measured at fair value through profit and loss totalled PLN 6,155.2 million versus PLN 5,122.1 million as at the end of December 2004. Their share in the balance sheet total was 14.6% compared with 14.4% as at the end of December 2004.



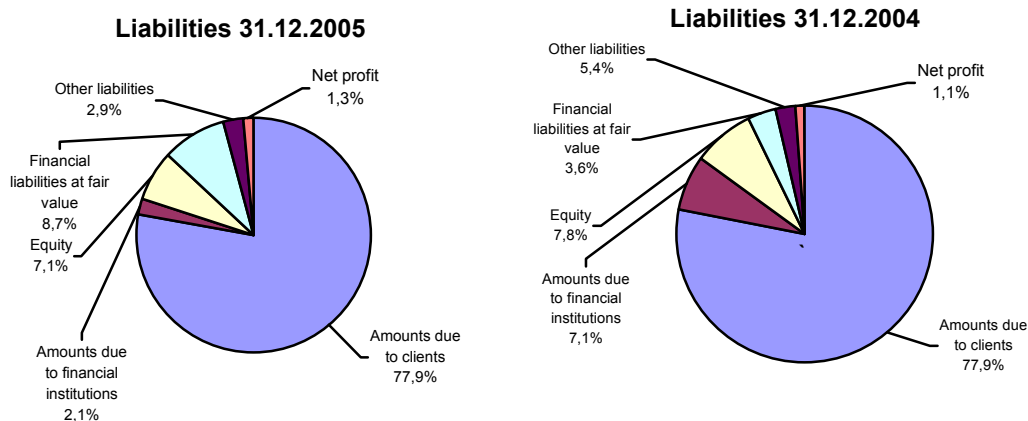
Cash and funds with the Central Bank amounted to PLN 895.3 million in December 2005 and went up to PLN 1,176.4 million at the end of 2005. Their share in the balance sheet total amounted to 2.5% and 2.8%, respectively.

As at the end of December 2005, the net value of property, plant and equipment and of intangible assets of ING Bank Śląski S.A. Capital Group totalled PLN 1,060.3

million compared with PLN 1,090.7 million at the end of 2004.

### Liabilities

The value of liabilities towards the clients went up from PLN 27,638.3 million at the end of December 2004 to PLN 32,823.6 million as at the end of December 2005, up by 18.8%. In December 2005, they represented 77.9% of total liabilities, a level similar to the one recorded a year earlier.



The good results recorded by ING Bank Śląski S.A. in the area of deposit acquisition and a relatively poor lending caused the liabilities of the Group towards financial institutions to amount to PLN 865.3 million at the end of December 2005 versus PLN 2,505.0 million at the end of 2004. The funds obtained from financial institutions constituted 2.1% of total liabilities, whereas in December 2004 their share was 7.1%.

The share of equity in liabilities of the Group of ING Bank Śląski S.A. as at the end of December 2005 totalled 7.1% versus 7.8% in December 2004.

### Income Statement

#### Gross and Net Profit

In 2005, the gross profit of the Capital Group of ING Bank Śląski S.A. amounted to PLN 705.8 million versus PLN 489.0 million in 2004.

Net profit reached PLN 549.5 million compared with PLN 399.0 million a year earlier (up by 37.7%). The core part of the Group's profit was allocated to the dominant entity – in 2005, net profit of ING Bank Śląski S.A. totalled PLN 506.8 million.

The key factors of impact on the financial results of the Capital Group of ING Bank Śląski S.A. in 2005 are the following:

- a slight decrease in the result on core operations (down by 0.7%) on a year-to-year basis, mainly as a result of a relatively low level of lending,
- a moderate increase of operational costs (up by 8.2%), following: the indexation of base salaries and implementation of a pro-sales incentive system,

- growth of the number of the sales network employees, outlays on the Bank's restructuring, and completion of marketing activities on a large scale,
- a positive balance of impairment losses due to improvement of the quality of the lending portfolio, good results of restructuring of the portfolio moved to the off-balance sheet records and introduction of new credit risk management standards.

Basic consolidated values of the income statement (PLN million)

	2005	2004
Interest result	721.2	834.2
Commission-related result	527.7	509.1
Dividend income	1.7	0.8
Result on instruments measured at fair value	212.2	72.7
Result on financial assets for investment	3.7	4.3
Result on sale of a subsidiary	0.3	0.6
Result on fair value adjustments in hedge accounting	-2.0	0.0
Result on FX differences	176.4	251.2
Result on other operating income / expenses	8.2	-11.6
<b>Result on core operations</b>	<b>1,649.4</b>	<b>1,661.3</b>
<b>Operating costs incl. depreciation/amortisation</b>	<b>-1,109.4</b>	<b>-1,025.2</b>
<b>Result on measurement at fair value of investment property</b>	<b>17.4</b>	<b>-19.1</b>
<b>Impairment losses and provisions</b>	<b>118.0</b>	<b>-151.9</b>
Participation in the net profits (losses) of related and associated entities evaluated with the equity method	26.7	23.7
Result on non-current assets and assets held for trading, result on disposal of assets other than the ones held for trading	3.7	0.2
<b>Gross financial result</b>	<b>705.8</b>	<b>489.0</b>
Income tax	-139.4	-79.0
Net result of minority shareholders	-16.9	-11.0
<b>Net financial result</b>	<b>549.5</b>	<b>399.0</b>

### Interest Result

In 2005, the net interest rate income generated by the Capital Group of ING Bank Śląski S.A. totalled PLN 721.2 million, whereas a year earlier it was PLN 834.2 million. It must be noted that in 2004 the item also included income on internal deposit swaps worth PLN 248.9 million. Upon their deduction, interest income in 2004 amounted to PLN 585.3 million.

The interest income recorded by the Capital Group of ING Bank Śląski S.A. in 2005 resulted from:

- considerable gains in deposits that the Bank later invested in safe debt papers;
- recognition of a part of credit commission income into interest income, in line with IAS;
- a drop in interest rates, and subsequent shrinking of interest margins.

As a result of those trends, in 2005, the Capital Group of ING Bank Śląski S.A. earned an interest margin of 2.36% against 2.84% in the same period last year.

### Non-Interest Income

Fees and commissions income constituted the major part of non-interest income. In 2005, it amounted to PLN 527.7 million as compared to PLN 509.1 million in 2004.

The total amount of commission income as presented in the income statement of the Capital Group of ING Bank Śląski S.A. for 2005 was affected by the application of International Accounting Standards (IAS 39), under which certain credit commissions were recognised in commission income, subsequently settled in line with the schedule of the credit receivable repayment.

In the structure of commission income, the largest share was related to commission on current account-related services, granting loans and operations made with payment cards.

In 2005, the result on instruments measured at fair value totalled PLN 212.2 million. In 2004, it was PLN 72.7 million. Upon recognising internal deposit swaps, the result amounted to PLN 321.6 million in 2004.

In 2005, the Capital Group earned PLN 176.4 million in terms of FX-differences income versus PLN 251.2 million a year earlier.

### ***Operating Expenses***

In 2005, the overheads of the Capital Group of ING Bank Śląski S.A. (the operating expenses including depreciation of non-current assets and amortisation of intangible assets) totalled PLN 1,109.4 million versus PLN 1,025.2 million in 2004 (up by 8.2%).

Increase of operating expenses was in major part the consequence of the expanded scale of operations pursued by the Capital Group of the Bank and higher outlays on certain areas of activity affected by reorganisation of ING Bank Śląski S.A.

Following the growth of headcount in the sales network, indexation of salaries and implementation of a new incentive system, which is correlated with the Bank's performance, in 2005 the staff costs were 13.3% higher than in 2004. The staff costs also grew as a result of the PLN 10.3 million worth of provisions established for severance pays to employees laid off as a result of the reorganisation of the Regional Operating Centres and retail debt collection area, which was started in 4Q 2005.

In 2005, tangible costs of the Group went up by 4.0%, mainly due to higher outlays on promotional-marketing activity, a considerable expenditure on finalisation of the branch revaluation and costs incurred in order to reorganise the institution.

### ***Impairment Losses and Provisions***

As of 2005, the Capital Group of ING Bank Śląski S.A. has been establishing provisions in accordance with IFRS/IAS; that is the Bank makes impairment losses when there is objective evidence that assets have been impaired. In 2005, the balance of impairment losses of assets as recognised in the income statement of the Capital Group of ING Bank Śląski S.A. was positive and amounted to PLN 118.0 million. In 2004, the risk costs of the Bank's Capital Group were negative and totalled PLN 151.9 million.

A positive balance of impairment losses and provisions was effected by the improved quality of the lending portfolio and adjustment of risk costs to the binding prudence

standards as well as generation of a considerable income on restructuring of the portfolio of lost loans moved to the off-balance sheet records. In total, a positive balance of write-offs of loans and advances, a positive provisioning balance for off-balance sheet liabilities along with the income from amounts due moved to the off-balance-sheet records was PLN 133,0 million.

#### Impairment losses and provisions

	<b>Total</b>	<b>Balance exposure</b>	<b>sheet</b>	<b>Contingent liabilities</b>		<b>Income on amounts due moved to off-balance sheet records</b>
		<b>Impairment</b>	<b>IBNR</b>	<b>Provision</b>	<b>IBNR provision</b>	
<b>Total</b>	<b>132.97</b>	<b>48.86</b>	<b>6.93</b>	<b>15.89</b>	<b>6.61</b>	<b>54.67</b>
Wholesale	102.74	47.98	3.88	13.88	5.53	31.97
Retail	30.23	0.87	3.06	2.52	1.08	22.70

#### Profitability

The results recorded by the Capital Group of ING Bank Śląski S.A. in 2005 caused the basic efficiency ratios to improve considerably.

An exception was the increase of C/I relation, connected with the continued process of reconstructing the Bank (among others the exchange of IT platform at branches, revisualisation of branches, new solutions in the operations area) as well as actions regarding marketing, which are being conducted to a large extend.

#### Basic efficiency ratios

(%)

	<b>2005</b>	<b>2004</b>
Profitability ratio	29.1	21.8
C/I ratio	66.2	62.6
ROA	1.3	1.1
ROE	18.3	14.4
Interest margin ratio	2.36	2.84
Solvency ratio	18.60	15.68

**Profitability ratio** – gross profit<sup>9</sup> to total costs.

**Cost to Income ratio (C/I)** – total overhead costs to the result on banking activity.

**Return on assets (ROA)** – net profit to total assets.

**Return on equity (ROE)** – net profit to equity.

**Interest margin ratio** – relation between the net interest income and average yield assets of the Bank<sup>10</sup> (including receivables from financial and non-financial entities, fixed and floating yield securities and participation units).

**Solvency ratio** – net equity to off-balance sheet assets and liabilities including risk weights.

<sup>9</sup> Upon adjusting with profits (losses) of minority shareholders.

<sup>10</sup> Net interest income was increased with the income on "internal deposit swaps". Average assets are calculated based on the data from three periods: 31.12.2004, 30.06.2005 and 31.12.2005.

## Share of Individual Business Lines in Creation of Financial Result

The breakdown of results by business lines presented below was prepared based on the data from the management information system.

In 2005, the Retail Banking Division generated income of PLN 826.0 million, thus similar to the result a year earlier. The Division's income was under the positive influence of the following factors: increase of income on deposit and clearing operations (gains in deposits, the number of account holders and bank card holders), expanded scale of operations on the capital market (higher commission from ING Investment Funds Corporation, increased turnovers on the brokering services market), and positive evaluation of the performance of ING NN Poland Pension Fund. Income on lending, on the other hand, was lower than a year earlier. Income of the Retail Banking Division accounted for 48.8% of the result on banking operations of the Bank's Capital Group (49.1% in the previous year).

Income earned by the Wholesale Banking Division was PLN 593.3 million, up by 3.7% from 2004. Increase of the Division's income was, in major part, the consequence of very good results being achieved in terms of the credit portfolio restructuring and an increase of transaction volume in capital markets (custody and brokering services) and expansion of FM operations with corporate clients. By contrast, the Division's income on core operations – deposits and lending – was lower. In 2005, the share of the Wholesale Banking Division in the result on banking operations of the Capital Group of the Bank was 35.1% (versus 34.0% in 2004).

Income on proprietary operations of the Capital Group of ING Bank Śląski S.A. was PLN 271.9 million, or 16.1% of the total result on banking activity. Income on operations generated in the financial markets area represented some 39% of the income on proprietary operations.

In 2005, the total income of the Capital Group of the Bank on FM operations (inclusive of the sales of FM products to the wholesale and retail segments) amounted to PLN 235.7 million, similar as last year's result.

In terms of ALCO<sup>11</sup>, the Capital Group of the Bank earned PLN 165.5 million, down by 1.0% from a year earlier. Their level mainly resulted from a drop in equity gains, following a decline in interest rates.

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<sup>11</sup> Inclusive of other income.

## Profit and Loss Account of ING Bank Śląski Capital Group (analytical layout)

PLN million	IAS / IFRS 12M 2004	IAS / IFRS 12M 2005	12M 2005 / 12M 2004	
Retail banking	826,4	826,0	-0,4	100,0%
<i>Core business</i>	803,6	793,1	-10,4	98,7%
<i>Income on Pension Funds shares</i>	18,9	26,7	7,8	141,4%
<i>FM products sales</i>	4,0	6,2	2,2	156,3%
Corporate banking	572,0	593,3	21,3	103,7%
<i>Core business</i>	436,4	430,4	-6,0	98,6%
<i>FM products sales</i>	114,4	123,1	8,7	107,6%
<i>Equity Markets</i>	21,2	39,8	18,6	187,9%
Own operations	283,6	271,9	-11,8	95,9%
<i>Proprietary trading</i>	117,2	106,4	-10,8	90,8%
<i>ALCO</i>	166,5	165,5	-1,0	99,4%
<b>Income total</b>	<b>1 682,0</b>	<b>1 691,2</b>	<b>9,1</b>	<b>100,5%</b>
<b>Operational expenses, including:</b>	<b>1 052,0</b>	<b>1 120,3</b>	<b>68,2</b>	<b>106,5%</b>
Personnel costs	473,6	516,6	43,0	109,1%
Headcount restructuring cost	0,0	11,3	11,3	x
Marketing costs	37,2	54,9	17,6	147,4%
Depreciation	124,2	128,3	4,1	103,3%
Other expenses	388,8	398,4	9,6	102,5%
Other operational costs	28,2	10,9	-17,3	38,6%
<b>Result before risk costs</b>	<b>630,0</b>	<b>570,9</b>	<b>-59,1</b>	<b>90,6%</b>
Risk costs	-151,9	118,0	269,9	-77,6%
<b>Result before tax</b>	<b>478,1</b>	<b>688,9</b>	<b>210,8</b>	<b>144,1%</b>
CIT	-96,2	-136,1	-39,9	141,4%
<b>Result after tax</b>	<b>381,9</b>	<b>552,8</b>	<b>170,9</b>	<b>144,8%</b>
Tax adjustment (FPU Act)	17,2	-3,3	-20,5	-19,1%
<b>Result after tax adjusted</b>	<b>399,0</b>	<b>549,5</b>	<b>150,4</b>	<b>137,7%</b>

## Proposal in terms of Dividend Payout

In 2005, the Capital Group of ING Bank Śląski S.A. recorded very good financial results. The net profit of the Group was PLN 549.5 million, in which the profit of ING Bank Śląski S.A. amounted to PLN 506.8 million.

The good financial results generated of the Bank in 2005 were impacted – apart from the increase of commercial volumes – also by the positive balance of impairment losses of the credit portfolio and provisions for contingent liabilities in the amount of PLN 128.7 million. The above resulted from an improved condition of credit portfolio and good results in the area of debt collection.

The Management Board of ING Bank Śląski S.A. is of the opinion – which is also shared by the Supervisory Board of the Bank – that a positive balance of impairment losses of loans cannot be considered a normal phenomenon in regular banking operations. Therefore, the Management Board of the Bank recommends its payment in the form of a dividend. Upon netting, the balance amount due to impairment of Bank's loans and advances was PLN 104.2 million in 2005.

A visible improvement of profitability of ING Bank Śląski in 2005 and a high solvency ratio (at 18.6%) confirmed the fact that the Bank had a sufficient level of equity for future market expansion. This is why, the Management Board of the Bank will appeal to the General Shareholders Meeting for payment in the form of the

dividend of also 50% of the 2005 net profit, upon eliminating the impact on the result of adaptation of risk costs to the portfolio condition (i.e. the amount of PLN 222.6 million).

At the end of 2004, ING Bank Śląski S.A. kept in the off-balance sheet records PLN 1,195.3 million worth of fully “provisioned” lost loans. As per 1 January 2005, the Bank valued the portfolio of credit receivables moved to the off-balance sheet records in market terms at PLN 44.1 million. This amount was recognised in the balance sheet of the Bank as a component of assets in correspondence with capital (retained result of previous years), causing it to increase by PLN 38.4 million; i.e. the amount equal to the discounted market value of that portfolio. The Management Board of the Bank recommends allocating an amount of PLN 31.1 million for the dividend. The said amount results from the adaptation of balance sheet positions to IAS (PLN 38.4 million less the tax burden of PLN 7.3 million).

	2004	2005
<b>Net profit of ING Bank Śląski Capital Group PLN million</b>	<b>366.3</b>	<b>549.5</b>
Elimination of impact of a positive balance of impairment losses of assets on net result in 2005		-104.2
<b>Net profit (after elimination of negative risk cost impact) in PLN million</b>	<b>366.3</b>	<b>445.3</b>
Dividend ratio	40%	50%
Dividend from net profit PLN million	147.0	222.6
<i>Dividend per share in PLN</i>	<i>11.3</i>	<i>17.1</i>
Dividend from non-recurring items PLN million:	+119.7	+135.3
<i>Due to adjustment of risk cost</i>	-	+104.2
<i>Due to adjustment of opening balance sheet to IAS</i>	+119.7	+31.1
<b>Estimated dividend total PLN million</b>	<b>X</b>	<b>357.9</b>
<b>Proposed dividend total PLN thousand</b>	<b>266,705</b>	<b>357,775</b>
Dividend share in net profit of ING Bank Śląski Capital Group	72.8%	65.1%
Dividend share in net profit of ING Bank Śląski	72.8%	70.6%
<i>Total dividend per share in PLN</i>	<i>20.5</i>	<i>27.5</i>

In conclusion, the Management Board of the Bank will recommend to the General Shareholders Meeting the payment of the dividend of PLN 357,775 thousand from the 2005 profit; i.e. PLN 27.5 per share. The dividend level proposed by the Bank Management Board in calculation onto 1 share, would translate into the dividend yield at the level of 4.9%<sup>12</sup>.

<sup>12</sup> Comparing to the share price of 30<sup>th</sup> December 2005.

## VIII. LINES OF ING BANK ŚLĄSKI S.A. DEVELOPMENT

In the months to come, ING Bank Śląski S.A. will further pursue the current strategy of development. Its main objectives comprise market expansion by organic growth and increase of the company goodwill by a considerable improvement of efficacy of its operations.

ING Bank Śląski S.A. accomplishes the said objectives in that it implements the concept of the “Customer-Friendly Bank”. This means that the Bank performs activities making it an institution able to establish long-lasting and valuable relationships with clients. First of all, the Bank:

- enhances its offer to ensure that it is attractive and competitive. The Bank pays special attention to efficient offering of a simple and transparent product offer. The following products are of key significance in fostering relationships with clients:
  - on the retail banking market – the Lion Account, the OKO Open Savings Accounts, mutual funds, mortgage facilities and credit cards,
  - on the wholesale banking market – cash management services (including state-of-the-art clearing solutions), loans, especially the ones related to transfers of EU funds, and also assorted forms of asset-based lending (leasing, factoring and commercial real estate financing);
- aims at the efficiency improvement. The Bank simplifies the procedures and implements the proper technological tools, contributing to the efficiency growth and costs reduction. Implementation of the Managing for Value methodology is another key element of those activities.
- develops infrastructure, including the sales network and IT systems. The Bank makes its offer more and more available, by continuous development of functionalities of electronic distribution channels and creation of new access paths, e.g. establishment of a partner outlets network, growth of co-operation with agents.
- reinforces its brand presence and recognition. The market expansion of the Bank is supported by campaigns – visible on the market – promoting the sales of key products and services of the Bank.
- stimulates the sales motivation of employees. The Bank works on establishing a new system of base salaries and continually improves the incentive system based on key performance indicators.

Striving for the market expansion, ING Bank Śląski S.A. simultaneously maintains the high level of operational security and observes stringent risk management standards.

The projects that were launched in 2005 – Retail 2006 and Corporate 2006 – are an important element of the Bank’s strategy. Their main objective is to develop and implement new processes at the Bank that will guarantee not only an effective service of clients, but also increase efficiency of the institution’s performance. The works aimed at optimisation of the operational area at the Bank will continue as well.

ING Bank Śląski S.A. will proceed with laying great emphasis on improving the accessibility of the products and services offered. In the nearest period, the Bank will specially focus on the creation of an outlets network based on the franchising model, and further expansion of electronic distribution channels (mainly internet banking).

The activities undertaken in regard to enhancement of service efficacy and implementation of new products and distribution channels should cause the favourable trends – both market expansion and improvement of performance efficacy – that were observed since 2004 in the business of ING Bank Śląski S.A. to be sustained in the nearest future. However, the scale of the Bank's market expansion and the growth of the financial result will be conditioned by economic situation and financial strength of clients.

## **IX. STATEMENTS OF MANAGEMENT BOARD OF ING BANK ŚLĄSKI S.A.**

### **Truthfulness and Accuracy of Statements**

To the best knowledge of the Management Board of the Bank, the annual financial data for 2005 and the comparable data presented in the annual consolidated financial statements of the Capital Group of ING Bank Śląski S.A. were prepared, in all material aspects, in accordance with the effective accounting principles and present fairly, accurately and transparently all the information on the property and financial standing of the Bank's Capital Group and its financial result. The annual statements of the Management Board enclosed herewith contain a true presentation of the development, achievements and standing (including a description of key risks) of the Bank's Capital Group in 2005.

### **Truthfulness and Accuracy of Statements**

The entity authorised to audit the financial statements who audited the annual financial statements of the Bank's Capital Group was selected according to the effective laws and Bank's regulations. The entity and the certified auditors fulfilled the conditions required to make an impartial and independent report on their audit, as required by the applicable Polish laws.