Management's Report
of PZU
for the year 2016

01

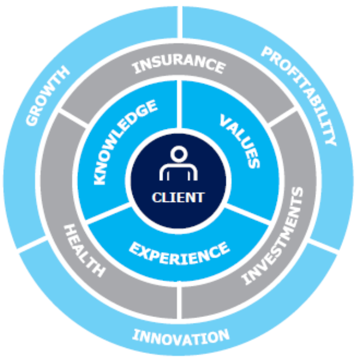
1 Brief overview of PZU

Powszechny Zakład Ubezpieczeń Spółka Akcyjna ("PZU", "Issuer", "Company") is one of the largest insurance institutions of non-life insurance in Poland with market share of 33.3%[1] and one of the largest insurance institutions in Central and Eastern Europe. The history of the PZU brand goes back to 1803 when the first Polish insurance company was established.

On 24 August 2016 PZU Group's Strategy 2020 was released and it assumed increased investment in the banking sector. The process was already initiated in 2015 by purchasing 25.19% of shares in the share capital of Alior Bank SA (Alior Bank). The next step saw Alior Bank acquire a part of Bank BPH, including its core operations (without its mortgage loans portfolio and Investment Trust Company).

While monitoring potential objectives fitting PZU Group's strategy of building a large-scale and profitable bank group, in December 2016 PZU announced that it had signed an agreement with UniCredit for purchase of 20% of the shares of Bank Pekao S.A. (together with the PFR Polish Development Fund – 32.8%).When the transaction is finalized, PZU will become the largest financial group in Central and Eastern Europe as the leader in insurance, banking, and asset management.

As a mature and reliable organization, PZU makes all efforts to ensure that its operations are performed in line with rational and responsible management – financial, human, social, environmental, and intellectual (SECTION 9 CORPORATE SOCIAL RESPONSIBILITY in PZU Group Management Report for 2016). The Management Board intends to offer products and services that are most suitable to meet the needs, ambitions, and aspirations of the clients. All processes – from insurance product concepts, through customer communication channels, to the activity in the scope of Corporate Social Responsibility, are designed to adapt PZU's offer to satisfy the demands and preferences of the stakeholders. At the same time, the Group initiates actions to increase consistency of the offer. Thus, the goals in the area of health and investment management were clearly defined in PZU Group Strategy 2020 (**SECTION 4.5 DEVELOPMENT DIRECTIONS OF PZU GROUP**).



Human capital plays an important role in the long-term development of PZU. This is why the Management Board continues to strive to ensure the best possible conditions for the development of the employees and carry their involvement over onto good relations with clients and high quality of provided services.

[1] PZU share calculated including active reinsurance for LINK4

In accordance with the adopted guidelines, the strategic objectives specified in PZU Group Strategy 2020 will be realized in a client-centric environment. The implementations will be accelerated by the development of a digital operating model, which will make it easier to build customer relations and manage customer experience (**SECTION 4.4 MAIN STRATEGIC OBJECTIVES**). It is also planned to implement innovative self-service and sale processes, as well as CRM (Customer Relations Management) tools in order to ensure that the ambitious plans defined in Strategy 2020 translate into solid results and PZU Group becomes that most innovative company in Central and Eastern Europe.

NON-LIFE INSURANCES

Dynamic increase in gross written premium

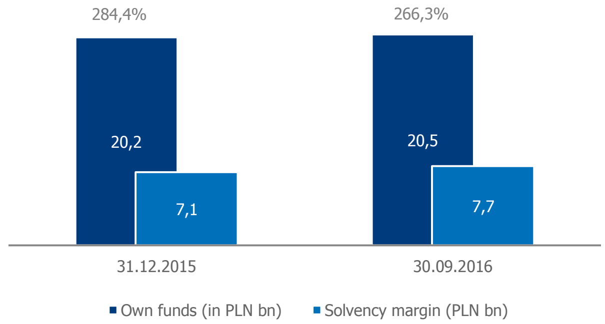
Changes in the motor insurance market (mainly price growth) result in increasing PZU gross written premium at the end of 2016 to:

PLN 10.7 billion (+20.6% y/y)

8.9 billion PLN in 2015; 8.3 billion PLN in 2014

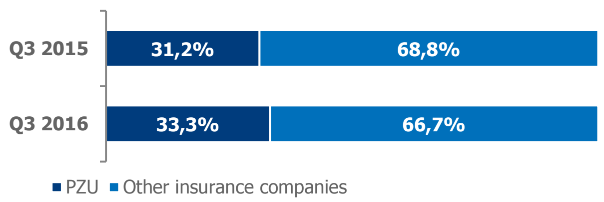
SOLVENCY II

Solvency II *



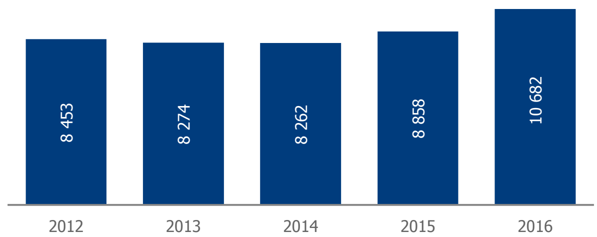
** unaudited data*

Market share (+2.1 p.p. y/y)

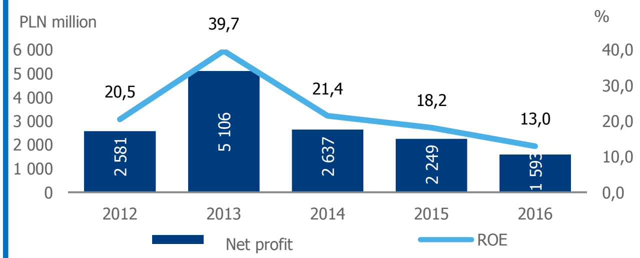


GROSS WRITTEN PREMIUM / PROFIT / ROE

Gross written premium (PLN million)

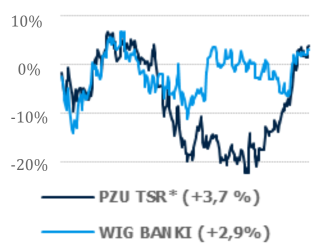


Net profit (PLN million) and ROE (%)



PZU shares

Rate of return of PZU shares in 2016



*	2016	2015
TSR	3,7%	(23,8)%
DY	6,3%	8,8%
DPS	2,1	3,0
EPS	2,3	2,7

Mission

We are here to provide our clients with **peace of mind** and **safety**. Our clients can always rely on us.

What we do

PZU Group is one of the largest financial institutions in Poland and in Central and Eastern Europe. The Group is led by the Polish insurance company Powszechny Zakład Ubezpieczeń SA – a company quoted on the Warsaw Stock Exchange. The history of the PZU brand goes back to 1803 when the first Polish insurance company was established.

~ 16 million clients in Poland

Protection of property

Motor insurance

Non-life insurances

Insurances for enterprises

Agricultural insurances

Financial insurances

Tourism insurances

Protection of the future

Group and individually continued protection products

Individual life insurance

Health care

Health insurance

Medicine insurance

Health care services: general health care and additional services packages

Increasing savings

Participation units TFI

Pillar II of the pension system (OFE)

Pilar III of the pension system (employment pension products - EPP, individual pension accounts – IKE, and individual pension security accounts – IKZE)

Bank products

Savings and checking accounts

Terms deposits

Credits and loans

Our values

Common operating philosophy

We are fair

Our offer is clear and satisfies real expectations of our clients; we follow transparent rules in operating the organization

We are effective

We offer friendly customer service and competitive prices to our clients; we control the costs, ensure that processes are smooth

We are innovative

We continually adapt to the changing needs of the clients; we proactively search for ways to improve our business.

Solvency of the insurance company

Pursuant to Art. 284. 1 and Art. 488 3 p. 1 of the Act on Insurance Activity, PZU is obliged to draw up and publish annual statements on solvency and financial condition, in line with “Solvency II”. For statement for year 2016 the publication due date is no later than 20 weeks after the end of the year, that is, by 20 May 2017. Pursuant to Art. 290. 1 of the Act on Insurance Activity, statement on solvency and financial condition of the insurance company is subject to analysis by entity authorized to audit financial statements.

PZU rating

Characteristic feature of the PZU Group’s business is its utmost security. This is evidenced by both high coefficients of capital adequacy ratios and the A- rating granted assigned by S&P Global Ratings. The above rating is one notch above foreign currency sovereign rating on Poland.

A-

S&P
insurer financial strength
and counterparty credit
rating

“The affirmation and removal from CreditWatch reflect our view of the group's revised business strategy announced in August 2016 after a change in the management board, as well as our view of the group's future banking strategy in Poland. […] We believe that PZU will continue to pass our hypothetical sovereign foreign currency default stress test. We therefore rate PZU one notch higher than our foreign currency sovereign rating on Poland." – explained S&P analysts in the report dated 31.10.2016.

On 22 December 2016, after the announcement of the contract for purchase of Bank Pekao shares, the S&P analysts affirmed the high credit rating for PZU.

Data from the profit and loss account (PLN million)	2016	2015	2014	2013	2012
Gross written premiums	10,682	8,858	8,262	8,274	8,453
Net earned premiums	9,213	7,898	7,903	8,108	8,277
Net claims and benefits	6,149	5,037	5,231	5,047	5,473
Acquisition costs, including reinsurance commission	1,849	1,571	1,523	1,367	1,495
Administrative expenses	724	754	729	663	676
Technical result	537	636	564	1,062	640
Net investment income	1,898	2,024	2,568	4,633	2,473
Gross profit (loss)	1,876	2,476	2,855	5,391	2,924
Net profit (loss)	1,593	2,249	2,637	5,106	2,581
Total assets	37,419	36,358	34,630	30,137	29,913
Financial assets	31,477	32,356	31,031	27,609	27,591
Equity	12,219	12,379	12,329	12,260	13,453
Technical provisions	18,715	17,540	16,861	15,913	14,933

SCHEDULE

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MARCH

acquisition of Bank BPH's assets by Alior Bank

Increaed engagement of PZU Group in the banking sector as a result of the acquiring by Alior Bank (PZU subsidiary) a separated part of Bank BPH. Due to the merger, Alior Bank was promoted to the 9th place among the largest banks in Poland in terms of asset value.

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SEPTEMBER

foundation of Witelo fund

Foundation of the Witelo fund in cooperation with bussines partners, its objective is to invest in the leading global VC funds.

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NOVEMBER

acquisition of Polmedic in Radom

Polmedic offers both basic and specialist health care, advanced diagnostics, and one-day- surgery. The center provides services to NFZ patients, commercial patients, and holders of company health care packages.

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DECEMBER

acquisition of Artimed in Kielce

Artimed offers a comprehensive scope of services, including standby surgeons and orthopedists. The center provides services to commercial patients, holders of health care insurance, and NFZ patients.

01

FEBRUARY

acquisition of Centrum Medyczne Cordis in Poznań

CM Cordis offers innovative diagnostic equipment and extensive range of specializations (including cardiology and cardiac surgery). The center provides services to commercial patients and holders of insurance and health care packages.

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AUGUST

publication of PZU Strategy 2020

Approval of PZU Group Strategy 2016-2020 by the Management Board and Supervisory Board. The Management Board specified three key strategic directions: profitability, growth, and innovation. They are planned to be realized both in the insurance sector, and the complementary areas that exhibit high potential for growth, that is asset management and health care.

04

OCTOBER

publication of PZU Dividend Policy 2016-2020

Approval of PZU Dividend Policy 2016-2020 by the Management Board and Supervisory Board. In accordance with the new guidelines, it was approved that at least 50% profit will be paid out as dividend, 20% will be allocated to organic growth, and not more than 30% will go towards financing strategic mergers and acquisitions.

08

DECEMBER

execution of a contract for purchase of 20% Alior Bank shares

Execution, in cooperation with PFR, of a contract for the acquisition of 32.8% of Pekao Bank shares at the total price of PLN 10.6 billion (price per share – PLN 123.00). It was one of the largest transactions performed in the bank sector in Europe in the recent years.

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2 The external environment

Contents:

2.1 Macroeconomic factors which can affect the operations of the Polish insurance sector and the operations of PZU in 2017

We expect that 2017 will be better than 2016 for the growth of the Polish economy, and thus also for the insurance industry. The GDP growth can amount to approximately 3.5%. Entering the implementation phase of investments co-financed with EU funds will be of key importance. It will allow to revive investments in a significant way and, with a steady, solid growth in consumption, to boost the GDP growth. Improvement of external conditions – foremost, a bigger growth of global trade turnover and a better situation in the global industry - should help Polish exports and industrial production. Our forecast assumes that the labor market situation will continue to improve. However, the increase in employment and a decline in the unemployment rate will be slower than in 2016 – due to the fact that Poland is getting close to the state of "unemployment equilibrium" and limits of labor supply. The increase in inflation may be the signal for the increase in remuneration pressure.

It seems that the biggest risks for this scenario are related to the external situation. The most dangerous risk seems to be related to a rise of protectionism in the global economy, which would lead to a slowdown in world trade and GDP. There will be a series of elections in the major EU countries in 2017, which means a potential threat to preservation of the coherence of the European Union, and furthermore, for sure - a temporary increase in uncertainty associated with said elections. It is difficult to fully predict the economic and market consequences of the probable strategy of "hard Brexit". Risks associated with the problems of European banks and Greece also remain relevant. Higher US interest rates and a strong dollar increase the risk of financial turmoil in emerging markets. The risk of a financial crisis in China, as well as geopolitical risks, still remain. Internal factors which could limit the growth of GDP include such issues as an increasingly noticeable problems with recruiting suitable employees, a possible prolonging of stagnation in private investments, or a sharper than expected rise in inflation, eroding real revenues of households.

Inflation will increase rapidly at the beginning of 2017 in response to a gradual disappearing of the effects of a sharp fall in fuel prices (and partially food) in the previous year and its annual average may amount to approximately 2% year-on-year. We expect stabilization of the NBP interest rates in 2017. The prospect of the NBP real negative reference rate, with accelerating GDP growth, especially at the end of 2017, will force the Council to consider increasing the interest rates.

We estimate that the state budget deficit and the general government deficit (2.9% of GDP) planned for 2017 can be implemented – especially with a probable buffer in the form of another, much higher than expected payment from the profit of NBP. In the context of the deficit of the entire sector, the risk is associated with an increase in the deficit of local governments due to the beginning of their investments. At the same time, implementation of the announced transfer of 25% of the funds from the Open Pension Funds to the Demographic Reserve Fund would temporarily help to reduce the general government deficit below 3% of GDP.

The prospect of higher inflation and economic growth should promote the growth of government bond yields, which in the long term is beneficial for PZU Group, although in the short term, it may adversely affect the investment income. However, there are many risk factors which will increase the volatility of financial markets in 2017. Political decisions or election results in key EU countries, which are difficult to predict, may turn out to have particularly painful effects. They may significantly change the outlook for the various asset classes in the financial markets.

Data for the Polish economy	2017*	2016	2015	2014	2013
Real GDP growth in % (yoy)	3,5	2,8	3,9	3,3	1,4
Increase in individual consumption in % (yoy)	3,5	3,6	3,2	2,6	0,3
Gross fixed capital formation in % (yoy)	4,9	(5,5)	6,1	10,0	(1,1)
Increase in prices of consumer goods and services in % (yoy, end of period)	1,9	0,8	(0,5)	(1,0)	0,7
Nominal wage growth in national economy in % (yoy)	5,0	3,6	3,5	3,2	3,7
Unemployment rate in% (end of period)	7,6	8,3	9,7	11,4	13,4
NBP base rate in % (end of period)	1,50	1,50	1,50	2,00	2,50

Source: PZU Macronomic Analysis Office
* Forecast as at 15 February 2017

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3 PZU's activities

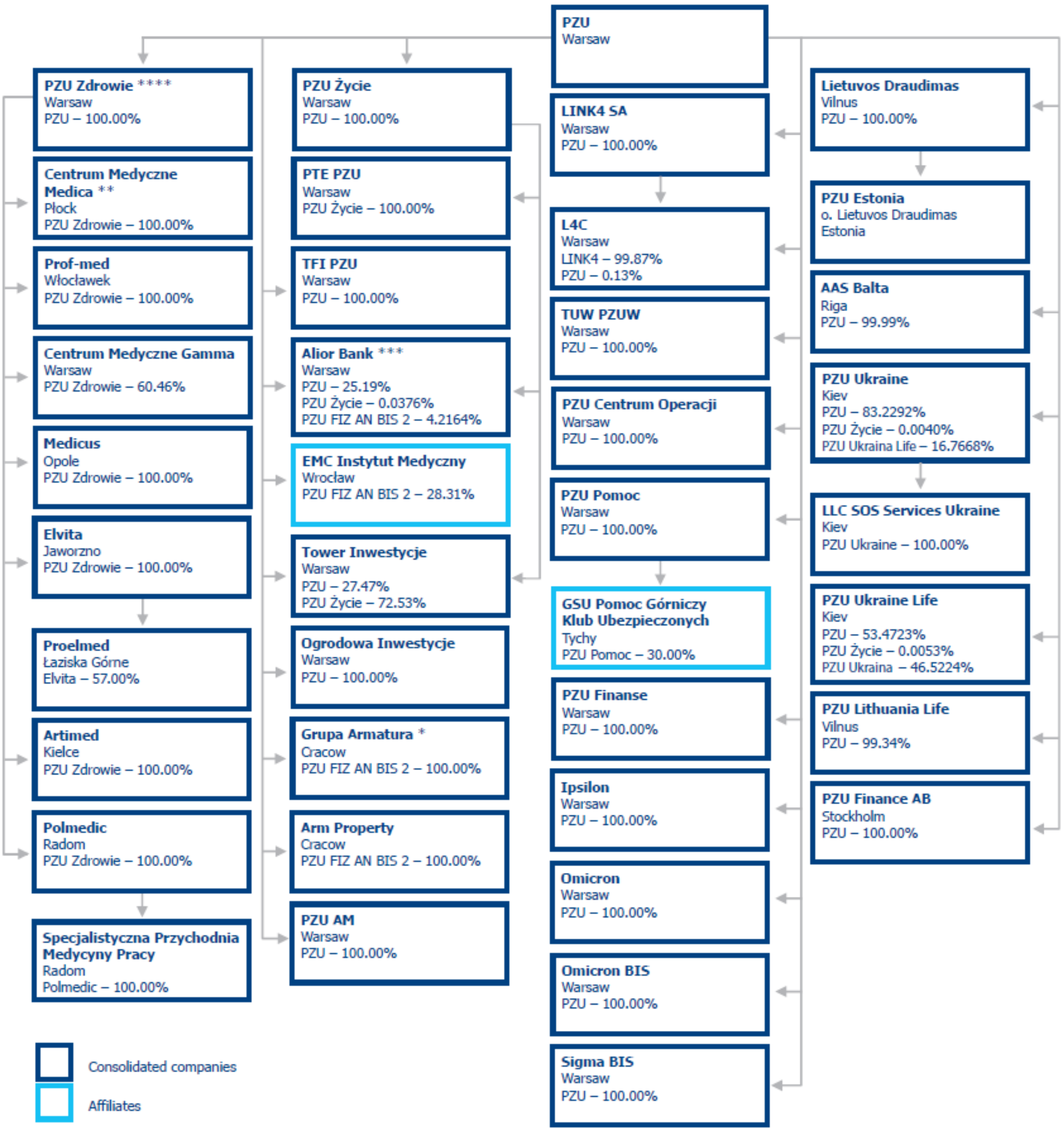
Contents:

3.1 Structure of PZU Capital Group

PZU stands on the forefront of PZU Group (PZU Group, the Group).

PZU Group conducts various activities in the area of insurance and finance. In particular, PZU Group's entities provide services in life insurance, non-life insurance, health insurance and asset management for clients within OPFs and investment funds, as well as banking services, thanks to the investment in Alior Bank.

Structure of PZU Capital Group (as at 31 December 2016)



* the Armatura Group includes: Armatura Kraków SA, Armatoora SA, Aquaform SA, Aquaform Badprodukte GmbH, Aquaform Ukraine TOW, Aquaform Romania SRL, Morehome.pl sp. z o.o.

** the Centrum Medyczne Medica Group includes the following entities: Centrum Medyczne Medica Sp. z o.o., Sanatorium Uzdrowiskowe „Krystynka" Sp. z o.o. and Rezo-Medica sp. z o.o.

*** the Alior Bank Group includes the following entities: Alior Bank SA, Alior Services sp. z o.o., Centrum Obrotu Wierzytelnościami sp. z o.o., Alior Leasing sp. z o.o., Meritum Services ICB SA , Money Makers SA , New Commerce Services sp. z o.o., Absource Sp. z o.o.

****within PZU Zdrowie 2 branches are operating: CM Nasze Zdrowie in Warsaw and CM Cordis in Poznań

The structure does not include investment funds and entities in liquidation.

Through its representatives in the supervisory bodies of the companies and voting during General Shareholders' Meetings, PZU – as the parent company – influences defining strategic directions regarding both the scope of activities and the finances of the entities making up PZU Group. Due to the expertise of selected companies Group members provide mutual services both under market conditions and based on the internal cost allocation model (within Tax Capital Group).

Detailed information on changes in the PZU organizational structure have been presented in Management Report of PZU Group www.pzu.pl/relacje-inwestorskie/raporty-okresowe-biezace/okresowe

3.2 Non-life insurance market - PZU

Situation on the market

The non-life insurance market in Poland (measured by the gross written premium) in the first three quarters of 2016 increased by PLN 2,840.5 million (+14.2%) compared with the corresponding period of the previous year. The biggest impact on premiums had increased sales of MTPL insurance (by PLN 2,140.6 million, +34.7%) and motor own damage insurance (by PLN 694.4 million, +16.9%), mainly as a result of substantial growth in premium average (which is a consequence of cyclical increases that are being introduced since 2015 as an answer to persistently negative results of the motor insurance market) and higher premiums from indirect business (increase of PLN 192.2 million in MTPL year-to-year).

Furthermore, there was growth recorded in sales of property insurance (by PLN 256.3 million, +5.9%, PLN 134.6 million of which concerns indirect business) and insurance of assistance (by PLN 146.0 million, +31.1%, including a PLN 142.0 million growth in direct business) which was a follow-up consequence of rise in premium from motor insurance.

The drop in premiums was most visible in TPL insurance (decrease of PLN 195.7 million, -11.8%, PLN 160.8 million of which concerns direct business), legal protection insurance (drop by PLN 113.1 million, -73.2%, PLN 113.1 million of which concerns direct business), as well as accident and illness insurance (drop by PLN 77.4 million, -4.5%, PLN 107.0 million of which concerns direct business).

The non-life insurance market generated a net profit of PLN 1,233.2 million in the first three quarters of 2016 (drop by 37.3% compared with the same period of the previous year). Excluding the dividend from PZU Życie, the net profit of the non-life insurance market grew by PLN 131.1 million (47.3%). After the first three quarters of 2016, the technical result of the non-life insurance market dropped by PLN 212.4 million, i.e. by 51.9% to the level of PLN 196.5 million. This change was affected to the greatest extent by the drop of the technical result in MTPL insurance (PLN -251.3 million) and in the group of property insurance (PLN -200.9 million). Some positive changes were recorded in the group of accident and illness (increase by PLN 87.4 million), motor own damage (increase by PLN 82.7 million) and TPL insurance (increase by PLN 80.4 million).

Non-life insurance market – gross written premium (PLN million)

Gross written premium	1 January-30 September 2016			1 January-30 September 2015		
	PZU*	Market	Market without PZU	PZU	Market	Market without PZU
Motor own damage insurance	2,054	4,793	2,739	1,642	4,098	2,457
MTPL	3,364	8,310	4,945	2,320	6,169	3,849
Other products	2,812	9,788	6,976	2,663	9,782	7,119
TOTAL	**8,230**	**22,890**	**14,660**	**6,625**	**20,050**	**13,425**

Source: PFSA (www.knf.gov.pl). Quarterly Bulletin. Insurance market 3/2016, Insurance market 3/2015, data of PZU

** including LINK4 and TUW PZUW*

The decrease of the technical result in MTPL insurance derived mainly from higher dynamics of claims and benefits (increase of PLN 564.2 million, +12.3%) as compared to dynamics of net earned premium (growth by PLN 493.4 million, +9.5%) - it resulted mainly from the implementation of the PFSA recommendations causing increase in average payments and as well as from strong price competition in recent years.

A profitability decline was also recorded in the group of insurance for damage caused by forces of nature (PLN -246.3 million on direct business) as a result of numerous claims in agricultural insurance which were caused by frost and hail.

Non-life insurance market – technical result (PLN million)

Technical results	1 January-30 September 2016			1 January-30 September 2015		
	PZU*	Market	Market without PZU	PZU	Market	Market without PZU
Motor own damage insurance	62	27	(36)	18	(56)	(74)
MTPL	(232)	(848)	(616)	(157)	(596)	(439)
Other products	477	1,017	540	553	1,061	508
TOTAL	**308**	**196**	**(111)**	**414**	**409**	**(5)**

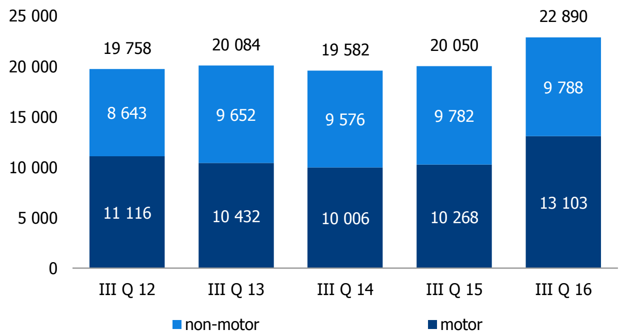
Source: PFSA (www.knf.gov.pl). Quarterly Bulletin. Insurance market 3/2016, Insurance market 3/2015, data of PZU

** including LINK4 and TUW PZUW*

The value of investments of non-life insurance companies at the end of third qurter of 2016 (excluding subsidiary investments) was PLN 53,063.9 million and it incresed by 1.9% vs the end of 2015.

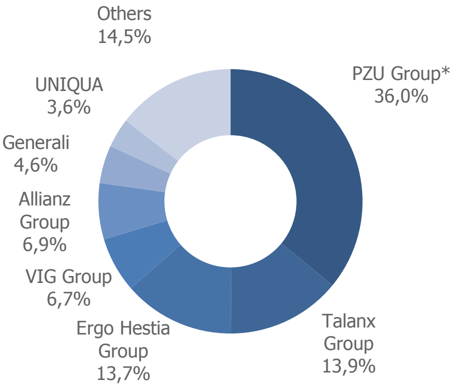
Non-life insurance companies, on aggregate, estimated the value of net technical provisions at PLN 43,342.9 million, which represented an increase of 3,9% compared with the end of 2015.

Gross written premium of non-life insurances companies in Poland (PLN million)



Source: PFSA (www.knf.gov.pl). Quarterly Bulletin. Insurance Market 3/2016, Insurance market 3/2015, Insurance market 3/2014, Insurance market 3/2013, Insurance market 3/2012

Non-life insurance companies - share in gross written premium for 3 quarters in 2016 (%)



Capital groups: Allianz – Allianz, Euler Hermes; Ergo Hestia – Ergo Hestia, MTU; Talanx – Warta, Europa, HDI; VIG – Compensa, Benefia, Inter-Risk
Source: PFSA Quarterly Bulletin. Insurance market 3/2016
** PZU Group - PZU, LINK4, TUW PZUW*

PZU's activities

PZU, being the parent entity of PZU Group, offers a wide range of non-life insurance products, including motor, property, personal and agricultural insurance, as well as third party liability insurance. PZU has been controlling over 1/3 of the non-life insurance market. PZU offers over 200 insurance products, of which the most important is motor insurance, with its share in the market amounting to 37.3% after the first three quarters of 2016, compared to 35.6% after the first three quarters of 2015.

PZU's share in market's technical result was 169.7% after the first three quarters of 2016 which, toghether with the market share of 33.3% in gross written premium, confirms high profitability of its operations.

In the changing conditions and in the face of new needs and interests of the clients, PZU introduced new solutions to its insurance offer in 2016. In mass client insurance:

- PZU DOM [PZU HOME] product was introduced to online sales of household insurance, including a variant "protection from all risk", which covers also the damage caused by uncommon and unpredictable events. The offer was accompanied by "Od Wszystkich Ryzyk" [From all risks] marketing campaign conducted through i.a. TV, radio, and social media;
- existing offer of personal insurance was made more attractive by broadening the catalogue of additional benefits and introducing to the market a new, comprehensive PZU Edukacja [PZU Education] product for educational establishments as well as individual client;
- general TPL insurance offer was extended in terms of the scope of responsibility by the addition of clauses covering environmental damage, damage due to package and label defects, and damage resulting from providing IT services;
- in order to approach the clients' needs, online sales of the PZU Wojażer insurance were launched, which was accompanied by *Spokojny Wypoczynek* [Peaceful leisure], campaign Basing on activities using the Internet.

In corporate insurance segment, the majority of changes concerned introduction of service and sales of corporate client products to the Everest system **GLOSSARY**, including:

- change in the approach towards pricing by implementing the model basing on the size of the fleet, which replaced the previous one that depended on the client's segment;
- modification of the existing distribution model, which allows the agents and multiagents to offer and sale basic non-motor products on their own by using the Everest platform **GLOSSARY** ;
- starting the works on extending the existing offer with new risks, including cybernetic risk incurred by enterprises.

In terms of financial insurance, PZU consequently supported Polish economy by granting insurance guarantees in its key areas, such as energy, infrastructure, and road construction. Among the main initiatives of 2016 were:

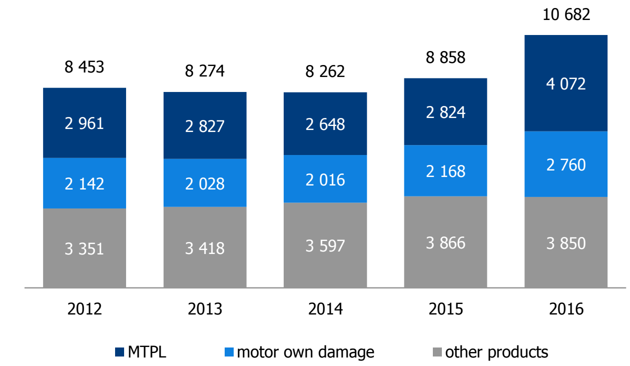
- increasing efficiency of the cooperation with SME sector by simplifying and accelerating the decision process – new rules for guarantee sales to the clients with guarantee exposure of up to PLN 1.5 million were introduced;
- conducting activities aiming at increasing the market share concerning financial liability insurance – in the first half of 2016 an agreement was concluded with a significant client from the fuel sector.

In 2016, PZU cooperated with 8 banks and 8 strategic partners. The partners of PZU Group are the leaders in their fields and have customer bases with great potential offering possibilities to expand with successive products. The cooperation in the scope of strategic partnerships concerned mainly the companies operating in telecommunications and energy sectors, which were used to offer insurance of electronic equipment and assistance services. The bancassurance sales covered mainly the insurance of buildings, structures and residences, as well as insurance dedicated for payment cards.

In 2016, PZU collected gross written premium of PLN 10,682.0 million, which was 20.6% more than in the previous year. At the same time, the sales structure slightly changed :

- value of MTPL insurance was PLN 4,072.4 million, which was 44.2% higher than in the previous year. It composed 38.1% of the entire portfolio, and its share grew by 6.2 p.p. from 2015. The increase in sales resulted mainly from substantial growth of average premium (a consequence of cyclical increases that are being introduced since 2015) and higher number of insurances;
- PZU collected premiums amounting to PLN 2,759.9 million from motor own damage insurance, which is 27.3% more than in the previous year. Share of motor own damage insurance in the overall portfolio grew by 1.4 p.p. to 25.8% in comparison with 2015;
- share of gross premiums from non-motor insurance in total premium increased to 36.0% (as compared with 43.6% in 2015). The value of gross written premium dropped by 0.4% year-on-year to PLN 3,849.7 million.

Gross written premium in PZU (PLN million)



In 2016, PZU generated a net profit of PLN 1,593.0 million, of which PLN 825.0 million was from the dividend from PZU Życie.

Factors, including risks and dangers, which will impact the activities in the non-life insurance sector in 2017

Apart from events of a catastrophic nature (such as floods, drought and spring frost), the main factors which can affect the situation of the non-life insurance sector in 2017 include:

- the potential slowdown of the economic growth in Poland resulting from the deteriorating external conditions which may result in lack of investments growth and declined perspectives of economic growth. In consequence, the limitation of household spending, including purchase of motor policies (as a result of lower new car sales), lower sales of mortgages and the mortgage related insurance, as well as lower demand for other non-life insurance. The poorer financial standing of businesses can result in a growth in credit risk and an increase in the level of claims in the financial insurance portfolio;
- stronger than expected inflation growth not compensated with growth of nominal salaries entailing decline in dynamics of real remuneration and limited household expenses – including those for non-life insurance;

- prospect of higher inflation and economic favoring growth of government bond yields, which in the long term is beneficial for PZU Group, although in the short term, it may adversely affect the investment income. Numerous risk factors escalating volatility on financial markets in 2017 and potentially serious effects of unpredictable political decisions or election results in key European Union countries, which may considerably alter perspectives of individual asset classes on financial markets;
- decisions of supreme courts on compensations from the MTPL insurance to relatives of car accident vicitims for pain and suffering claims resulting from the violation of their personal welfare even if the the damage took place before 3 August 2008;
- potential raise of claims handling costs resulting from the implementation of further recommendations of PFSA concerning claims handling, especially personal claims;
- raise of spare parts prices with effect on claims handling costs resulting from the successive drop of PLN against the EUR;
- further regulations or financial burdens imposed on insurers – e.g. a possible reinstatement of so-called "Religa tax" (i.e. compulsory fee payable to NFZ from every MTPL policy).

04

4 Business strategy

Contents:

4.1 Summary of PZU Group Strategy 2020

2016 saw a number of changes in the composition of the corporate bodies of the PZU Group companies SECTION 8. CORPORATE GOVERNANCE). The new Management Board of PZU led by Michał Krupiński reviewed and updated the existing strategy. The Management Board identified areas where it saw a potential for continuation of activities performed to date, space for improvement, as well as new ambitious initiatives that, in the long haul, would result in creating competitive advantages of PZU and goodwill for its shareholders. The results of the strategy overview confirmed that insurance should continue to be the Group's core business. Moreover, a greater potential for development of PZU Group's business was identified in health care and investments. In addition, as far as the realization of long-term development perspectives is concerned, a decision was made to invest in the banking sector in Poland.

"PZU Group Strategy 2020 – Profitability, Growth, Innovation"

Development directions of PZU Group 2016-2020

"We are planning to concentrate on the area which has been a cornerstone of PZU identity for over 200 years – that is insurance business. We should put all our effects in offering to our clients the best and most innovative insurance products which protect their future, health, and property. That is why in everything we do, we will concentrate on ensuring that our core business is highly profitable, stable, and future-oriented." - Michał Krupiński, 15 March 2016.

The PZU Group strategy 2016-2020 published on 24 August 2016 was developed on the basis of the following core values: profitability, growth, and innovation. The Management Board's intention was to increase profitability of insurance activity and develop innovative tools for business management and customer service. The strategic goals took a form of ambitious growth initiatives, also related to such areas as PZU Zdrowie, PZU Inwestycje, and banking sector. The process of achieving these goals was planned in a way that allows PZU to secure means for further sustainable development and providing attractive dividend in the long term. Maintaining a high return on equity ratio (ROE) is the key to the strategy's success.

"Today, PZU is one of the most profitable companies in the insurance sector. However, we realize that, in order to ensure high profitability for our investors in the future and considering rapid technological changes, we also need to invest in our own development. We need to constantly develop and stay focused on the clients and their changing needs." - Michał Krupiński, 24 August 2016.

All goals included in the Strategy were quantified and are seasonally monitored by means of precisely specified measures that allow for on-going monitoring and correction of assumptions made. SECTION 4.7 SELECTED MEASURES OF THE GROUP STRATEGY AND INITIATIVES IN 2016

Key changes made to PZU Strategy 3.0 adopted in January 2015 concerned the following:

- increased focus on profitability of the Group's core business (insurance), e.g. by reducing fixed cost by PLN 400 million by 2018;
- accelerating PZU Group growth rate, including development of the following areas: Zdrowie and Inwestycje;
- including in PZU Group Strategy a plan for investment in the banking sector;
- increased role of innovation in PZU Group as a tool for achieving goals regarding profitability and growth.

Key strategic directions 2020

Focus of high profitability of insurance activity coupled with simultaneous growth in selected market segments

Reduce fixed costs by PLN 400 millions till the end of 2018

Effectively pursue growth initiatives in health and investments

Build a large and profitable banking group

Create one of the most innovative insurance group in Europe

Capital and dividend policy as an integral part of PZU Group Strategy

On 4 October 2016, Group Strategy was supplemented with Capital and dividend policy of PZU Group for 2016-2020. In line with the presented assumptions, maximum 20% of profit could be set aside for organic development, and no more than 30% on financing strategic mergers and acquisitions. That means that every year the Management Board recommends that the General Shareholders' Meeting (after obtaining an opinion from the Supervisory Board) allocates at least 50% of net profit for dividend for shareholders. Should the budget allocated for acquisition be not used in a given financial year, it can be used for payment of dividend for shareholders (**SECTION 7.8 PZU GROUP'S CAPITAL AND DIVIDEND FOR 2016**)

"Dividend policy is an important element of PZU Strategy 2020. The Management Board's goal is for PZU to be a company that pays attractive dividends in the future. We will achieve that by investing in organic development and innovations, and by realizing our strategic goals in the area of mergers and acquisitions. Every year, we want to allocate at least 50% of profit for dividends. (..)*We will develop Group is a way that ensures increasing dividends to all PZU SA shareholders."* - Michał Krupiński, 4 October 2016.

The goal of capital and dividend policy is to focus on the shareholder return. It is based on efficient capital management, maximizing return on equity for parent company shareholders (especially by maintaining security level and capital resources for strategic development realized by mergers and acquisitions), maintaining target Solvency II ratio at 200% and leverage ratio at 35% or less, and assuming that PZU will not issue shares as long as the policy is in place.

4.2 Basic assumptions of the strategy

The PZU Group Strategy 2020 was created with the following assumptions concerning the condition of the Polish economy and insurance sector, including especially:

- moderate pace of economic growth in Poland (approximately 3.0-3.5% annually);
- increased inflation as of 2017;
- higher interest rates as of 2017;
- changes in shopping preferences – growing importance in the direct channel (mobile devices) and price comparison engine market that are based on ad-hoc shopping decision-making;
- introduction of regulative changes, including the following:
    - improving structure of the unit-linked life insurance market,
    - implementing the recommendation regarding a standard payment of compensation resulting from non-property claim under a MTPL insurance policy,
    - introducing by early 2018 the MiFID II directive that recommends transparency in commissions paid in the sales of *inter alia* investment products;
- stable perspectives in the development of property and motor insurance - decreased intensity of the price war in motor insurance and improved profitability in MTPL segment;
- stable growth in investment fund market – increased importance of low-cost (from the client's perspective) and long-term investment products;
- growing (double-digit) potential in health insurance and prepaid health packages.

4.3 Core values of the strategy

Common operating philosophy:

- We are Fair – our offer is clear and satisfies real expectations of our clients; we follow transparent rules in operating the organization.
- We are Effective – we offer friendly customer service and competitive prices; we control the costs and ensure that the processes are smooth.
- We are Innovative - we continually adapt to the changing needs of the client; we proactively search for ways to improve our business.

The strategy of PZU Group is customer-focused. Our commitment to stay client-centric is clearly visible in the adopted strategic mission – „We are here to provide our clients with peace of mind and safety. Our clients can always rely on us." We want to accompany our clients everywhere they go to stay ahead of their needs just the way they expect us to. In practice, it translates into transforming PZU from a product-centered organization into a company that focuses on the clients' needs.

Clients

- We are here to provide our clients with peace of mind and safety. Our clients can always rely on us.
- We know our client very well and that is why we are able to meet their needs and rational expectations. The scale and efficiency of our operations help us provide premium services at competitive prices.
- Due to its market position, PZU acts as a "market watchdog" – our activities are beneficial for the entire market and the clients, we actively influence the market growth and establish standards in customer service.

Shareholders

- Thanks to the scale of business ensured by our leading position in the Central European Market, we continue to provide exceptional profits to our shareholders.

Employees

- PZU creates a working environment that inspires our staff to do their best while maintaining an optimal work-life balance.

Sustainable development

Realization of our strategic assumptions depend on proper capital management – financial, human, social, environmental, and intellectual. The Management Board follow one basic rule: increasing goodwill of PZU should stay in line with the interests of its environment and be based upon sustainable and responsible use of resources.

4.4 Main strategic objectives

In August 2016, the new Management Board and Supervisory Board of PZU approved the updated PZU Group Strategy 2016-2020. The Management Board specified three key strategic directions: profitability, growth, and innovation. They are planned to be realized both in the core insurance sector, and the complementary areas that exhibit high potential for growth, that is asset management and health care. At the same time, the Management Board declared that the realization of the assumption should result in boosting investment attractiveness of PZU not only for dividend investors, but also investors who search for growing companies, with a high potential to generate capital gains on market valuation of the share.

Profitability

The most important goal of PZU Group when it comes to profitability is to achieve ROE (of a parent company) at least 18%. Reaching such a target is to a large extent correlated with the growth initiatives (below). The initiative to reduce fixed costs in insurance business in Poland (PZU and PZU Życie) by PLN 400 million by the end of 2018 also contributes to realization of this goal.

Growth

In the insurance sector, PZU Group plans the largest growth in such market areas where PZU's share was lower than the natural level of approximately 30%. In complementary business sectors covered by PZU Strategy 2020, the growth will be realized by organic development and acquisitions, which will help achieve gains and profits dynamics higher than the market average.

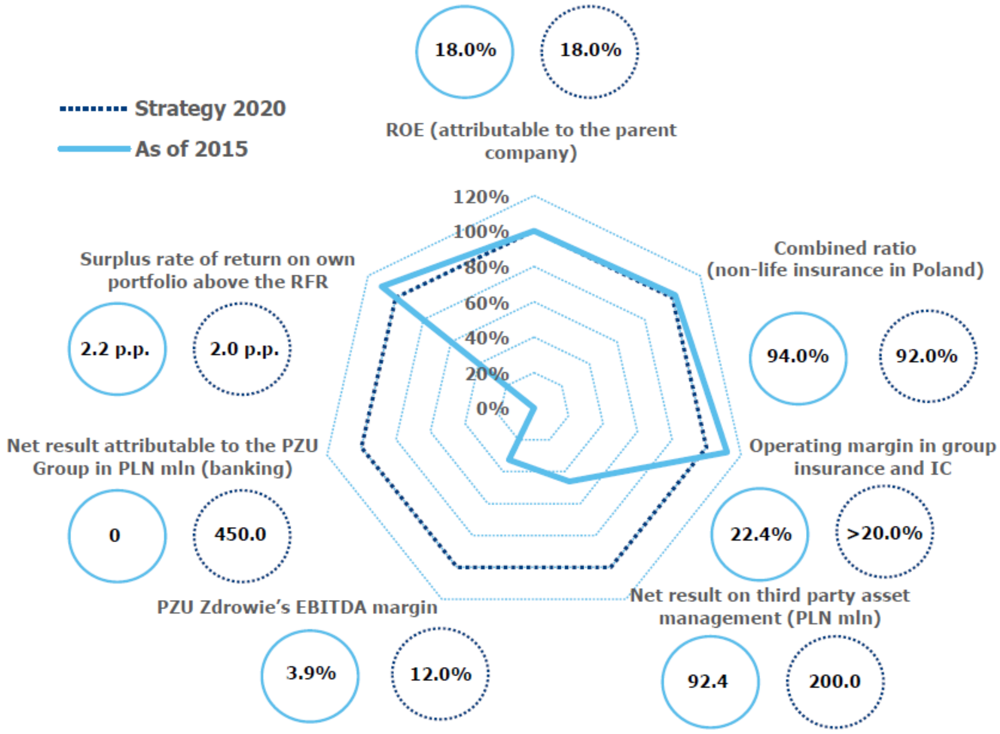
Innovations

Innovation is an important part of the Strategy. On the one hand, innovation is our ambition as we aim to transform PZU into one of the most innovative insurance groups in Europe. On the other hand, it accelerates the realization of the other key strategic targets: growth and profitability.

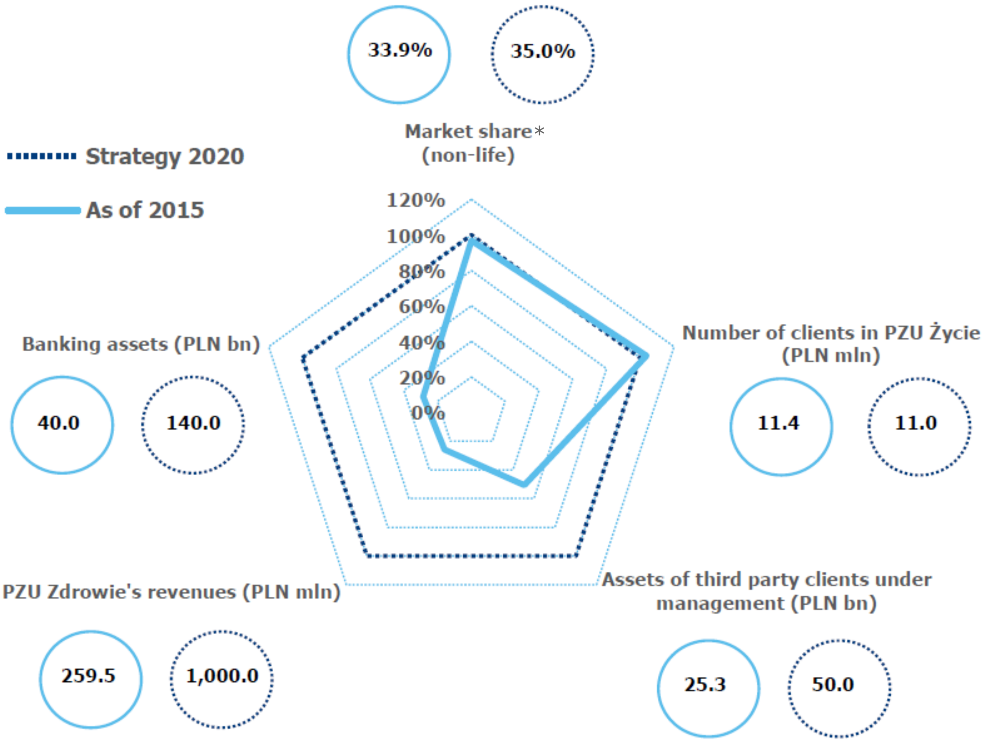
Creating innovation-driven culture in PZU Group will be realized especially by means of the following activities:

- use of Big Data in quotation, sales, and service;
- development of electronic distribution and service channels;
- implementation of effective know-how and technologies inside PZU Group by regional innovation centers: LINK4, Alior Bank and selected foreign companies;
- providing innovative risk management solutions in large-scale businesses (PZU Lab)
- development of innovation-driven culture that will support the process of generating new solutions by the employees.

PZU Group Strategy 2016-2020 (business profitability)



PZU Group Strategy 2016-2020 (business size)



** direct business*

Implementation of the above projects will allow for building a comprehensive digital operational model in PZU Group that will boost flexibility in the entire organization to meet the changing needs of the clients and improve the company's position in the Young Clients and Premium Clients segment. Comprehensive and multi-channel distribution and Customer service, including further development of CRM (Customer Relationship Management) tools and using available client data, will result in customizing the Group's offer to individual client needs. Using efficient analytical tools and Big Data will make it possible to manage the portfolio on the basis of actual risk profile of a given client and use advanced price management methods in property insurance. As the expectations continue to grow, PZU plans to implement self-service processes and new forms of sale wherever required.

The Group sees a high potential for growth in health care, old age pension, and property products. The 360° overview of the client and using additional interactions will allow for sales of products and services that better fit the clients' needs, as well as cross-selling **GLOSSARY** development. In the long term, such activities should translate into an increased number of products held by the client. A so-called productization of a retail client in PZU Group should increase to 1.64 by 2020.

PZU Group will proactively support the creation an ecosystem that boosts Polish entrepreneurship and innovations, by providing the following:

- support Polish entrepreneurs and scholars by own initiatives of PZU Group and cooperation with other projects that promote innovativeness (e.g. Witelo fund);
- identifying and supporting external initiatives that are synergic and complementary with PZU Group's activities;
- financial support for initiatives of entrepreneurs provided on commercial basis, including via Venture Capital **GLOSSARY**.

4.5 Development directions of PZU Group

The PZU Strategy was diversified in a manner allowing for both generating stable and predictable cash flows (property and life insurance) and obtaining exceptional profits from complementary operations (asset management and health care). Investment activity, including in the banking sector, is also a part of the strategy of determining the scale of PZU Group. In the long-term, this approach should allow the shareholders to obtain the expected rate of return from the PZU shares, while maintaining at the same time a moderate level of risk.

Non-life insurance

The aim of the strategy of PZU Group is to strengthen its leadership position on the non-life insurance market in Poland, as well as the improvement of profitability (combined ratio) in this segment.

Retail Client

Almost 16 million Clients in Poland have put their trust in PZU Group, which is why the retail client segment is an extremely important area for the Group from the point of view of maintaining high level of customer satisfaction, especially by means of appropriate and dynamic adaptation of services and products to rapidly changing needs.

2020

Rentability of non-life insurances (combined ratio)

The aim of PZU is to maintain its leading position on the market by improving price and profitability management by channels and strategies of two brands in Poland (PZU and LINK4). The Management Board of PZU intends to implement these goals by means of, for example:

- permanent restoration of profitability of motor insurance and an increase of the activity on the market of profitable non-motor insurance by means of better recognition of the needs of the client and a flexible price policy;
- focusing on maintaining the scale and the growth in internal sales channels (exclusive agents, branches) and improving profitability of external channels by means of better adoption of costs of service to the potential of the distributor and management of profitability in the channels;
- use of the cross-selling potential of PZU Group by means of comprehensive management of PZU Group's offer (property insurance, life insurance, investments, health, and pension) – development of CRM tools supporting all retail sales channels, including direct ones;
- implementation of product innovations on the basis of new technological developments.

Alternative channels for reaching new clients

In order to reach the biggest possible number of retail clients, PZU Group makes use of its two brands – PZU and LINK4 – which have different positions and offers. The complementary offer of LINK4 supports the position of PZU Group in the multiagency channel and on comparison websites. The strategy in this area provides for a systematic exchange of market and organization know-how, including the creation of a joint competence center focusing on price management and an internal innovation center, where LINK4 will function as a low-cost environment for testing new solutions in PZU Group.

Corporate client

The strategy provides for a dynamic growth of PZU Group in individual business lines within the corporate client segment and Mid-Corpo segment (medium-sized corporations operating on the Polish market). PZU Group will be a business partner with strong expertise that provides its clients not only with insurance products, but also advice, at every stage of risk management process.

It is planned to increase the scale of cooperation with hospitals, local authorities and state-owned companies through development of Towarzystwo Ubezpieczeń Wzajemnych Polskiego Zakładu Ubezpieczeń (TUW PZUW).

Improvement of PZU Group's position in the Corporate Client segment (non-life insurance) will be carried out by means of:

- implementation of system solutions which enable optimal management of the portfolio of Corporate Clients, including profitability management in the segment and dynamic development of sales of non-motor products;
- dynamic business growth in the Mid-Corpo segment, both in motor insurance and in non-motor insurance (medium-sized corporations operating on the Polish market);
- development of cooperation with hospitals, local authorities and state-owned companies by means of creation of a dedicated insurance coverage offer (almost PLN 500 million in premiums of PZUW TUW in 2020);
- implementation of advanced risk management consulting services (PZU Lab).

Development directions of other areas further described in SECTION 4.6 REALIZATION OF KEY PROJECTS AND INITIATIVES IN 2016 in PZU Group Management Report for 2016.

4.6 Realization of key projects and initiatives in 2016

In 2016, the Group achieved the following objectives in specific Business Fields:

Activities realized in 2016

Key areas	Summary of activities and achievements in 2016
Insurance	• PZU strengthened its leading position on the non-life insurance market. According to PFSA data for the third quarter of 2016, PZU's market share (direct business) was 33.0% (an increase by 1.6 p.p. year-on-year). • The share of LINK4 in non-life insurance market amounted to 2.2% at the end of the third quarter of 2016 (an increase by 0.3 p.p. year-on-year). • PZU retained its top position in life insurance with periodical premium after the third quarter of 2016 with 45.0% market share (up from last year's 43.9%). Following the third quarter of 2016, PZU Życie had a 33.7% share in the entire life insurance market (an increase by 4.5 p.p. year-on-year). • Strengthen the market position in the Lithuania and Latvia. Market share in Lithuanian non-life insurance market was 29.5% (decrease of 1.6 p.p.comparing to previous year), while the share in the Latvian market grew by 2.0 p.p. at the end of third quarter of 2016 and amounted to 27.2%. The market share in life Lithuanian market amounted to 4.8% (increase by 0.4 p.p.). The share of PZU Group in the Estonian non-life market amounted to 14.5% in 2016 and recorded growth by 0.6 p.p. The Ukrainian non-life company recorded after the third quarter of 2016 an increase in the market share (3.7%) by 1.0 p.p. compared to the same period of previous year, while the life company registered a decline in the market share (8.5% vs 8.6% y/y). • Continuation of implementation associated with the introduction of a new policy system (project Everest GLOSSARY) which should improve PZU's flexibility and competitiveness. In April 2016, another version of the system was implemented, which included making further products available (inter alia: general agreements, Cargo, D&O) and introducing changes to existing functionalities and products. Moreover, other external distribution channels were implemented, including the multiagents and bancassurance channel, the implementation of own corporate sales channel was completed, and the portal "moje.pzu.pl" with the online sales functionality was launched. Sales carried out via off-line channels was transferred in the last quarter of 2016 to the Everest GLOSSARY platform (among others: motor and non-life leasing, central dealers, and financial insurance). • Active presence on the insurance market since 29 February 2016, i.e. when it started its insurance business by concluding its first insurance contract, and the further dynamic development, confirmed a market share of 0.5% in the first year of operation. • The analytic tool for pricing was implemented, which will be used for increasing the effectiveness of communication tariffs. • The agreements on research and development cooperation were signed with the Warsaw University of Technology as part of the "Scientific Council". • Implementation of IT solutions improving life customer service efficiency. • Completion of the process of implementation of innovative PZU Branches – well-visible and common for the entire Group. There are altogether 190 Branches functioning within this new model. • Completion of work aiming to consolidate and improve the visualization standard of Exclusive Agent offices. From the start of the project, 1,143 offices in the new standard were opened. • The development of a product providing continuous technological protection has begun, accompanied by insurance protection from the effects of cyber-attacks.
Investments	• TFI PZU ranked the second on the market in terms of the value of managed net assets. At the end of 2016, the value of AuM TFI PZU amounted to over PLN 22 billion, which constituted 8.6 % of the assets obtained by domestic investment funds.

	• Growth of the volume of the managed assets of external clients from PLN 6.8 billion at the end of 2015 to PLN 7.0 billion at the end of 2016. At the end of 2016, the share of assets of external TFI PZU clients in TFI market assets (with exception of non-public assets) was 4.8% (4.6% at the end of 2015). • TFI PZU was the leader in the segment of employee pension programs among domestic investment funds. At the end of 2016, TFI PZU managed assets with value of almost PLN 4.0 billion (EPP – Employee Pension Plan, PPO – Employee Saving Program, ZPI – Corporate Investment Program) – AuM growth by 17.2% compared with the end of 2015. • The value of net assets of OFE PZU Złota Jesień at the end of 2016 amounted to PLN 20.0 billion. • The net profit of PTE PZU at the end of 2016 amounted to PLN 60.3 million. • The Witelo fund was also established in cooperation with business partners. The fund will invest assets in the top venture capital **GLOSSARY** funds in order to promote Poland as a place for investments and implementation of innovative projects. • Preparation of a new investment strategy including strategic allocation of assets, organization and processes linked to the management of the investment portfolio of PZU Group. • Works related to the implementation of business initiatives aimed at developing cooperation between Alior Bank and PZU.
Health	• At the end of 2016, the revenues of PZU Zdrowie amounted to PLN 363.8 million, which means a 40.2 % increase year-on-year. • The gross written premium from group health insurance rose by 38.4% from 2015. • Three medical entities (CM Cordis, Polmedic and Artimed NZOZ) were acquired by PZU Zdrowie. • The works on the implementation of the tool for the cooperation with medical establishments. • Implementation of tools for management of the network of medical establishments, both PZU Zdrowie's own establishments and ones which cooperate with it, as well as tools for management of client traffic on the medical hotline. • Works have begun on providing medical hotline consultants with a way of communicating on-line in the scope of arranging medical benefits with a distributed network of medical establishments.
Banking	• The acquisition of the third tranche of Alior Bank shares was settled. As a result of this transaction, PZU Group has the controlling package, i.e. 29.45%. • The declaration of backing from PZU in relation to the conclusion and implementation of the Sale of Shares and Division Agreement by Alior Bank, a subsidiary of PZU. The agreement concerned the acquisition of independent area of activity of Bank BPH. The assets of the merged banks (Alior Bank and Bank BPH) will reach the value of PLN 61 billion. • The agreement concerning the purchase of 32.8% of shares of Bank Pekao S.A by PZU Group and the Polish Development Fund (PFR) was signed. Under the agreement, PZU Group will purchase approx. 20% of the shares, while PFR (Polski Fundusz Rozwoju S.A.) will acquire 12.8% shares of the bank. • The contribution of the banking segment to the operating result of PZU Group amounted to PLN 691 million at the end of 2016.

Support factors	Summary of activities and achievements in 2016
Effective handling and operations, flexible IT	• 82% of PZU Group's clients are satisfied with claims and benefits handling (satisfaction survey on a sample of 4.3 thousand clients conducted in the fourth quarter of 2016). • Work was conducted on the implementation of the Fraud Detection System for motor insurance. • Implementation of a new human resources and salaries system, including self-service portal for the employees, was completed – the first step towards standardization and improvement of HR processes in the whole company. • Implementation of an application for self-handling of claims by clients. • Commencement of works on modernization of the infrastructure of data warehouses. • Implementation of works related to transforming PZU from a product-centered organization into a company organized in accordance with client segmentation. • Commencement of works on a self-service portal including all products of PZU Group. • Continuation of process related to the sale of real estate which is unnecessary from the point of view of the statutory activities of PZU and PZU Życie.
Socially responsible organization	• PZU continued to follow the action lines adopted for social activities – safety, health and active lifestyle, the national heritage. • PZU Group's involvement in running initiatives is the key way to promote active lifestyles and health prevention among Poles. PZU served as the strategic partner of, among others, the PZU Warsaw Marathon, PZU Warsaw Half-Marathon, PZU Gdynia Half-Marathon and the PZU Cracovia Royal Half-Marathon. All running events sponsored by PZU were accompanied by a "Share Your Kilometers" charity action, which encourages Poles to help others through their own physical activity. • PZU is a patron of culture – it is involved in the preservation of Polish cultural heritage, supporting the Royal Castle in Warsaw, Royal Łazienki Museum, Warsaw Uprising Museum, National Museum in Kraków, National Museum in Warsaw, National Theatre and Grand Theatre—National Opera. • A new prevention agreement was signed with rescue service, GOPR. The agreement will remain in force until 2019. The funds transferred by PZU will be used to purchase new quads and expedition backpacks for all rescue teams in southern Poland.
Culture of cost effectiveness	• The decrease in administrative costs of insurance segments in Poland amounted at the end of PLN 26 million, that is, - 1.8% year-on-year. • Improvement of the administrative cost index for insurance segments in Poland by 0.7 p.p., at the end of 2016, the index amounted to 8.1%. • Improvement of the administrative cost index in foreign companies by 2.9 p.p., at the end of 2016. The index amouted to 11.0%.
Capital and investment policy, and integrated risk management system	• The payment of the dividend in the amount of PLN 1.80 billion, i.e. PLN 2.08 per share. • Confirmation of the Capital Structure and Dividend Policy of PZU Group for the years 2016–2020, in accordance with which the dividend payment ratio will amount to not less than 50% of net profit. • The S&P rating of PZU and PZU Życie remains at the level of A-, which is one step higher than the rating of the country. • Effective and adequate adaptation of risk management system and compliance to the changing organizational structure of PZU Group and legislative environment.

4.7 Key metrics of the Strategy for 2016-2020

ROE[1]

2015	2016	2020 S
18%	15.0%	18%

BUSINESS SIZE

NON-LIFE INSURANCE – PZU Group's market share[2]

2015	2016	2020 S
33.9%	35.9%[12]	35%

LIFE INSURANCE – Number of clients in PZU Życie (million)

2015	2016	2020 S
11.4	11.2	11

INVESTMENTS – Assets of third party clients under management (PLN bn)

2015	2016	2020 S
25.3	27	50

HEALTH – Revenues (PLN mln)

2015	2016	2020 S
259.5	363.8[7]	1,000

BANKING – Assets (PLN bn)

2015	2016	2020 S
40	61	140

BUSINESS PROFITABILITY

NON-LIFE INSURANCE – Combined ratio[3]

2015	2016	2020 S
94%	95%	92%

LIFE INSURANCE – Insurance margin in group and individual continuation

2015	2016	2020 S
22.4%	25.8%	>20%

INVESTMENTS – Net result on third party asset management (PLN mln)

2015	2016	2020 S
92.4	83.8	200

HEALTH – EBITDA Margin[6]

2015	2016	2020 S
3.9%	7.2%	12%

BANKING – Net financial result attributed to the PZU Group (PLN mln)

2015	2016	2020 S
0	193	450

Cutting fixed expenses (PLN mln)

2015	2016	2018 S
-	78	400

Surplus rate of return on its own portfolio above the RFR

2015	2016	2020 S[4]
2.2 p.p.	0.6 p.p.	2.0 p.p.

GROUP OBJECTIVES

Solvency II solvency ratio[5]

2015	2016	2020 S
276%	253%[11]	>200%

NPS for Retail Client vs. competition

2015	2016	2020 S
+8.6 p.p.	+9.1 p.p.[8]	> competition

Number of products per Retail Client

2015	2016	2020 S
1.49	1.51	1.64

Employee commitment index

2015	2016	2020 S
49%[9]	n/a[10]	55%

[1] ROE attributable to the parent company
[2] Direct business
[3] PZU jointly with PZUW TUW and LINK4
[4] Average during the Strategy implementation
[5] Own funds after subtracting anticipated dividends and asset taxes
[6] Net of transaction costs
[7] Data on the annual basis regardless of the acquisition date; establishment's revenue are presented as managed, in the same way as the other branches, i.e. including PZU Zdrowie
[8] Average surplus of period: Q1, Q2, Q3, Q4 of 2016
[9] Value of the meter after 2014 – the last measurement
[10] Lack of the research in 2016
[11] Data after three quarters of 2016, unaudited
[12] Data after three quarters of 2016

05

5 Organization, infrastructure and human resource

Contents:

5.1 PZU business model

The main business model of PZU includes the following:

- Insurance – still the main and primary pillar of PZU Group's activity. Each day, PZU ensures that the offered products match the needs of the clients and the quality of customer services concerning events covered by insurance is at the top possible level;
- Investment activity – the collected premium is invested according to the "prudent investor" GLOSSARY rule. This means that funds are invested in a way ensuring security, quality and liquidity with preservation of profitability.

5.2 Business model – insurance

Clients' segments

For management purposes, PZU has been divided into the following business segments:

- corporate insurance (non-life). This segment encompasses a wide range of non-life insurance, general liability and motor insurance, which are adapted to customer needs and, with individually valued risks, offered by PZU to large business entities;
- mass-market insurance (non-life). This segment comprises property, accident, general liability and motor insurance. PZU provides the insurance to individuals and entities from the SME sector.

Sales channels

The organization of the PZU sales network guarantees sales effectiveness, while simultaneously assuring high quality of the provided services. PZU has the largest network of sales and service branches on the Polish market.

At the end of 2016, PZU distribution network included:

- exclusive agents – PZU's own agency network consisted of 6,562 exclusive agents, including individuals performing agency activities. The agency channel conducts sales mainly in the mass client insurance segment, especially motor and non-life insurance.
- multiagencies – PZU cooperates with 3,232 multiagencies to make sales mainly to the mass client (this channel is used to sell all types of insurance, especially motor insurance and non-life insurance).
- insurance brokers – PZU, in particular the Corporate Customer Division, cooperated with more than 900 insurance brokers.
- bancassurance and strategic partnership programs – PZU cooperated with 8 banks and 8 strategic partners in scope of protective insurance in 2016. The partners of PZU are the leaders in their fields and have customer bases with great potential. The cooperation in the scope of strategic partnerships concerned mainly the companies operating in telecommunications and energy, which were used to offer insurance of electronic equipment and assistance services.

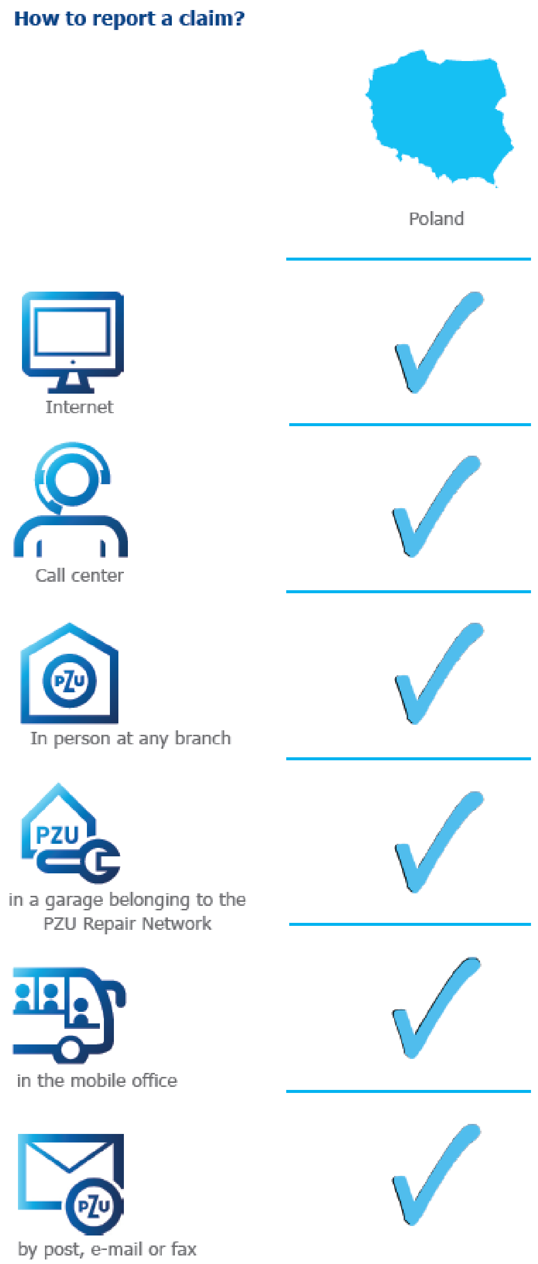
	non-life insurance
Employees	✕✕
Exclusive agents	✕✕✕
Multiagencies / Brokers	✕✕✕
Direct	✕✕
Banks	✕
Startegic partners	✕

Claims handling

For the customer, claims handling process is the moment in contacts with the insurer and an opportunity to test the quality of the purchased product. Satisfying his or her expectations in the claims/issue handling process is the key to building client ties with PZU. Because of this, PZU Group took numerous activitiesin 2016 to improve and shorten the process.

In Poland, claims and benefits are handled in 6 competence centers, which operate nationwide. This is based mainly on electronic information and is not connected with the place of residence of the insured or the place of the event. Competence centers handle certain types of claims; this results in higher specialization level and boosts customer satisfaction. Such units specialize, among others:

- in non-life claims handling process;
- motor and personal claims
- corporate clients claims;
- benefits;
- claims consisting in a complete theft of vehicles belonging to natural persons;
- claims under the BLS service (direct claims handling) **GLOSSARY**.

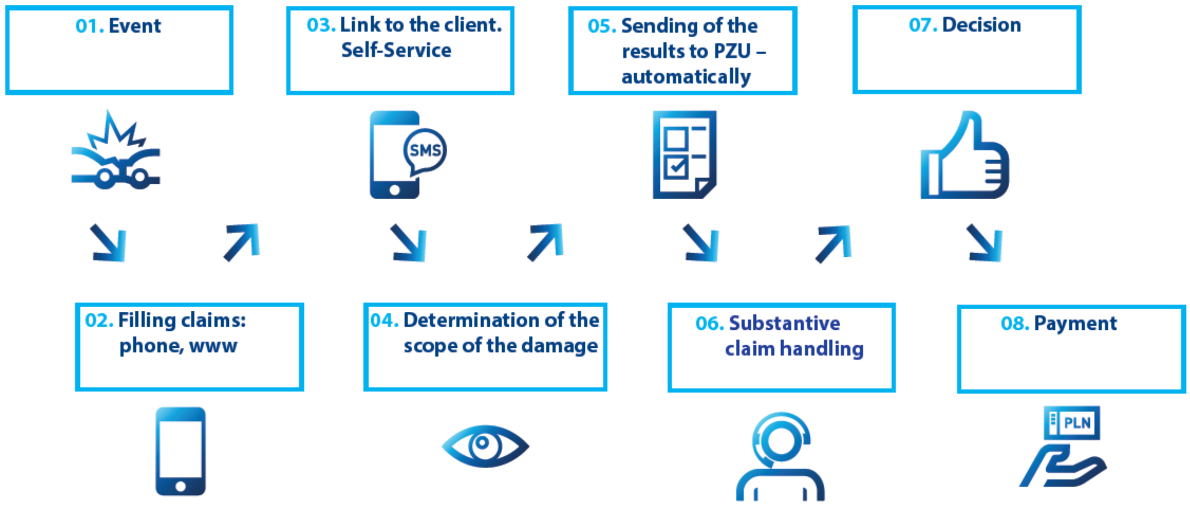


A separate entity provides technical support for motor and property claims.

In 2014, PZU became a BLS pioneer on the Polish insurance market. At present, the Company realizes it in the two forms: individually and under an agreement. By the end of 2016, the BLS agreement drafted by PIU encompassed eight insurance companies, including PZU. Together, they represent nearly 70% of the MTPL insurance market measured at gross written premium level. The agreement, which is based on lump-sum schemes, introduced in April 2015 considerably simplified the settlement of paid claims between the insurers. PZU also maintained its earlier BLS solution for its clients who suffered damage at the hands of the people insured at insurance companies that are not parties to agreement.

PZU created the largest network of companies on the Polish market that provide car rental, towing, and parking services. PZU was the first to introduce its own fleet of replacement cars to the Polish insurance market. The offer covers 300 hybrid Toyota Auris cars, which guarantee comfort and safe and ecological use. This provides a high replacement car availability standard according to market rates to all PZU clients.

Process of self-service damage



In 2016, PZU continued cooperation with garages in the field of post-accident vehicle repairs in countries where PZU Group operates. Every client that commissions a vehicle repair at a PZU Pomoc garage in Poland receives a Quality Certificate confirming that the repairs met top standards. PZU continues to develop its offer when it comes to the management of objects that are left after a damage and that can be sold on the Pomoc Online platform. The clients receive an offer to sell the remains for the highest obtained purchase offer from credible entities, who are permamently working with the platform administrator.

In addition, PZU is implementing claim self-service, which is activated personally by the client with the link received via text message or email. In case of accident claims or benefits, the client accepts or rejects the proposed amount of the benefit **GLOSSARY**. In motor and property claims and in cooperaing workshops repairing equipment damaged in electrical overloads, the client may estimate the amount of compensation prior to deciding. The information is sent online to the Issue Consultant, who realizes the payment. The service allows easy and convenient participation in the decision-making process concerning the payment, and speeds up the entire process, thus shortening the period of waiting for money. Client satisfaction surveys conducted among the PZU Życie clients show that the insured perceive the service in a very positive way. In 2016, over 30% of the clients whose issues qualified for this form of service decided to use it.

In 2016, PZU introduced a number of simplified solutions to contact the clients, e.g. it resigned from traditional letters, popularized contact over the telephone and electronic means of communication, but first and foremost it made its correspondence simpler and more user-friendly.

Visual representation of claims handling stages in the Online Claim/Issue Status – available for the Group's clients in Poland is also very helpful tool for the clients. After logging to his or her claim/issue at www.pzu.pl , the Client can learn how many stages the PZU customer service process involves, become familiar with every stage, and checks his or her claim/issue status, as well as sees which activities have already been realized. Moreover, the www.pzu.pl website features also a video with tips related to online claims handling. Short videos depict PZU employees showing the clients how to quickly file a claim, change its status, or how to use the accident insurance in case of an accident. PZU – Video tips – Online claims handling

Another innovative move that supports the process of personal claims handling from TPL insurance was to appoint the Assistance Providers under the name of Organizatorzy Pomocy Poszkodowanym w Wypadkach [Providers of Assistance to Accident Victims]. These are mobile employees who meet with the victims in their houses in Poland and determine the actual life situation and the needs related to the accident they suffered from and for which PZU is liable. Assistance Providers shall explain to accident victims their laws and tell them which documents they have to present. For people who have suffered serious damage, they shall organize broadly defined medical, social and vocational rehabilitation. They advise on how to adjust place of residence to meet the needs of a disabled person, as well as how to choose proper systems compensating for dysfunctions and disabilities. They assist in obtaining the benefits from governmental institutions (from PFRON [National Disabled Persons Rehabilitation Fund], ZUS [Social Insurance Institution], KRUS [Farmer's Social Security Fund], MOPS [Municipal Social Services Centre], and MOPR [Municipal Family Support Centre]).

Another innovation which is being developed by PZU is the creation of a system for handling cultivation damage by using aerial and satellite photographs. It is significantly important in a situation in which a larger number of crop damages occur in a short period of time. With this solution PZU will shorten the process during which the clients are waiting for decision concerning the claim.

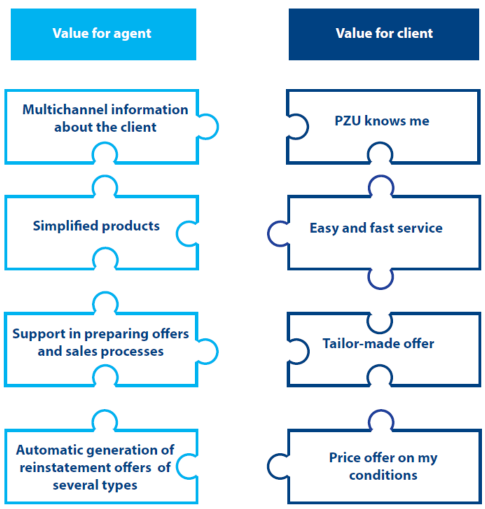
An important area of activity within the processes of claims and benefits handling is prevention of insurance frauds. PZU continues to improve solutions limiting payments of unduly benefits and impeding practices of clients providing both false documentation during reporting the claim and untrue declarations concerning their health, as well as simplifying many processes.

Innovations

In recent years, PZU has been intensively working on implementing innovative solutions to improve the customer experience as much as possible. This objective is supported by the Laboratory of Innovation, which was established at the end of 2013. The Laboratory of Innovation is currently working on implementing an innovation strategy for all of PZU Group, which covers building a culture of innovation and cooperation with other Group's companies, including LINK4, Alior Bank and foreign entities.

One of the Group's biggest innovative operations is the PZU Everest Platform. This is the biggest IT project in the Central and Eastern Europe and PZU largest business transformation at the same time. The Platform is a state-of-the-art tool that facilitates sales of non-life insurance, assessment of insurance risk, and management of policies and settlement, which PZU has been implementing since 2014. The implementation of the Everest platform in all channels will end in Q1 2017. The platform lets PZU distribute information faster and, consequentially, allows the agents to better recognize and understand the needs of clients from different sectors. As it improves and modernizes the working environment of PZU agents and employees (reduction of paper consumption by 70%), the Everest platform helps raise operating efficiency, which additionally expands the potential for presenting a competitive offer to the clients.

Benefits of the Everest Platform launching



Following tests over 13 thousand intermediaries were trained last year in external distribution channels (multiagents, dealers). The Everest platform was implemented also in bancassurance channel and corporate client segment.

Development of Everest **GLOSSARY** platform allowed to expand product offer available to intermediaries – in 2016 new and enhanced products were introduced, addressing the needs of corporate segment clients and small and medium-sized enterprises. The final quarter of 2016 also saw the transfer of sales realized through offline channels to the platform (including motor and non-life leasing, bancassurance, and financial insurance).

PZU continues to work on more innovations and started the development of the PZU GO *Self Service* platform for the individual client at the end of 2016. The platform will provide online access to the products and services (purchase of insurance, medical services, and investment or savings products) offered by all of the Group's companies and to their features in the future (filing claims, making doctor's appointments, checking measurements of units of funds or other entities, or paying premiums). Meanwhile, the Group will have aggregated information about its clients and will be able to distribute information and identify their individual needs quicker.

5.3 Human resources management

Level of employment

In 2016, the average annual PZU employment of approximately 7.7 thousand employees calculated as FTEs.

As at the end of 2016, most of PZU employees were women, who represented nearly 58.5% of the total number of employees. Over 78.9% of the employees had college education. The employee age structure also remains stable. As at the end of the year about 68.5% of the employees were under 44 years old.

On 9 March 2017, the Management Boards of PZU and PZU Życie decided to continue restructuring of employment in PZU and PZU Życie. The Management Boards od PZU and PZU Życie addressed the trade unions operating at PZU and PZU Życie to start working on agreements concerning group releases.

The restructuring of employment in PZU and PZU Życie is planned for the period between 24 March and 18 December 2017. The restructuring process will cover up to 1,944 people with estimations seeing 956 employees of PZU and PZU Życie from various professional groups subject to employment reduction.

The cost assiociated with payment of benefits to employees released due to employment restructuring are assessed in the budgets of PZU and PZU Życie for 2017 and will be included in the annual consolidated financial statements of PZU Group for 2017.

The ultimate number of people covered by the restructuring process and its assiociated costs and savings will be known when PZU and PZU Życie's consultations with trade unions are completed.

Salary policy

PZU's salary policy aims to provide employees with remuneration appropriate to the performed job, competences, and skills and encourage the implementation of PZU's long-term objectives. It also aims to prevent conflicts of interest and eliminate potentially negative influence of remuneration systems on risk management.

Remunerations in PZU are shaped with respect to employee's scope of tasks and level of responsibility, and their market competitiveness is evaluated annually. An important element of the remuneration scheme is the variable, which is subject to restrictions in terms of the maximum amount possible to be granted – it is covered by the determined percentage relation to fixed base remuneration. The basis for determining the total amount of the remuneration subject to variations is the evaluation of performance of a given employee (taking into account financial and non-financial criteria) and given organizational unit, combined with the Group's results. A part of remuneration subject to variations is developed on the basis of the above-mentioned factors and depends on the group of employees it concerns.

Moreover, as part of the remuneration system, PZU offers its employees very rich additional benefits package, as well as it supports non-professional activities of PZU's employees (i.a. through the PZU Sport Team or employee volunteering program).

Recruitment, training and building the image of an employer of choice

The following have been organized in PZU in 2016 to support employees in improving their skills, which are required at the given work post:

- e-learning – employees and managerial staff have an access to a broad catalogue of e-learning training, which they can use without any limitations; the trainings were held in different, engaging forms: e-learning, educational animation, e-books, simulations, and educational games. In total, the employees have access to over 100 different activities;
- Menedżer 2.0 [Manager 2.0] program which focused on the development of mid-level management (over 1,500 managers) in building managerial thinking, team engagement, business effectiveness of a team, as well as coaching skills indispensable at a managerial position. An interactive and gamified Inspiratorium Menedżer 2.0 [Inspiration Space Manager 2.0] platform was a continuation and extension of stationary trainings. The platform uses state-of-the-art trends to combine elements and mechanisms known from games to support development of a habit to pursue self-education and knowledge acquisition, as well as social network mechanisms to create an interactive space for sharing knowledge, experience, ideas, and inspirations; In 2016, the main focus of the program was to build team effectiveness and using coaching skills in pursuing managerial tasks.
  - Lider 2.0 [Leader 2.0] program, the aim of which was to strengthen the competence of senior managers in the role of all-round leaders. In 2016, the main focus of the program was to boost innovation. It consisted of two parts: individual sessions and classroom trainings organized as group workshops;
  - "Challenges in management" program – a program dedicated for new managers. The objective of the trainings was to provide a basic set of managerial skills indispensable for successful fulfillment of managerial tasks;
- PLUS training program (Professionalism – People – Skills – Trainings) – trainings are selected for the employee on the basis of his/her DNA appraisal (PZU competence model), which have the objective of developing the key competences. Every program contained several training modules which develop competences in such fields as: client, result, responsibility, development, cooperation. The training cafeteria included 12 thematic fields. The program included a range of 2-day classroom training, supplemented with interactive forms of development. In 2016, 2,600 employees in total participated in trainings organized within the program;
- there were also numerous workshops to provide an opportunity for sharing experiences and raising competences among the Groups in Poland (PZU, Link4) and companies abroad, which covered finances, mass sales, claims and benefits handling, and marketing.

In its highly-awarded campaign "PZU. Przyciągamy Najlepszych (2014-2017)" [PZU. We attract the Best (2014–2017)] the Company continues also comprehensive activities promoting its brand as an employer, which are addressed to students and professionals. Last year, the campaign was held under the name of "Praca w PZU dobrze wróży" [Work at PZU is a Good Omen] whose main element was a recruitment and image-building video.

Popular social competitions, i.e. Studencki Projekt Roku [Student Project of the Year] and Inwestycja w Przyszłość [Investment in the Future], were continued in 2016 to support the most active students and most popular academic projects. PZU experts shared their knowledge and experience at a number of business presentations and trainings for students (i.a. Dni Otwartego Biznesu w PZU (Open Business Days at PZU), and all image activities were supported by active and creative Ambasadorzy i Doradcy Grupy PZU (PZU Group Ambassadors and Advisors).

In 2016, the image-building activities of the Company as an employer gained recognition at the EB Kreator, EB Excellence Award and EB Stars competitions, and two independent surveys by HRM Group and Goldman Recruitment declared PZU Group as the undisputed leader in employer brand management in Poland. Current projects can be followed on the Facebook, LinkedIn and Instagram career website.

06

6 Financial results

Contents:

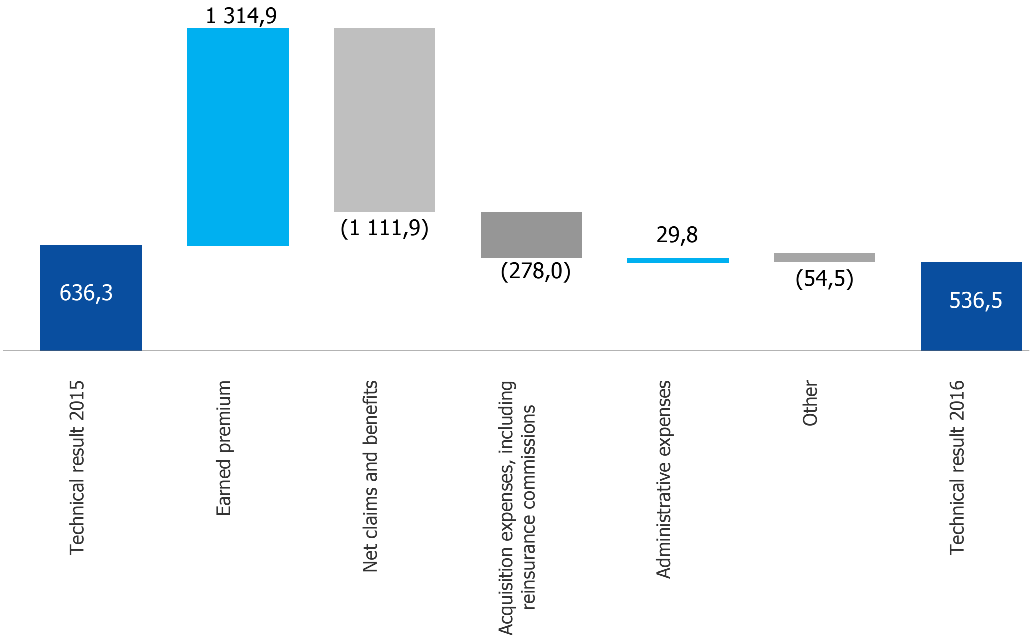
6.1 Key factors affecting the achieved financial results

PZU achieved technical profit in 2016 at the level of PLN 536.5 million compared with PLN 636.3 million in the prior year (decrease of 15.7%). The net profit amounted to PLN 1,593.0 million, compared with PLN 2,248.5 million in 2015 (a drop of 29.2%). Without the dividend obtained from PZU Życie, the net profit of PZU was PLN 768.0 million and was PLN 209.6 million higher than in 2015.

Within particular items of the net result, PZU recorded:

- increase in the gross written premium to PLN 10,682.0 million, i.e. by 20.6% year-on-year, mainly in motor insurance, as the effect of increased average premium, which results from the changes which have been implemented gradually from 2015 to the average prices and insurance of assistance offered mainly as a part of motor insurance package. After accounting for the share of reinsurers and the change in provision for unearned premium, the net premium earned amounted to PLN 9,212.8 million, which was 16.6% higher than in 2015;
- higher claims and benefits at PLN 6,148.5 million, a rise of 22.1% from 2015. The change was recorded mainly in motor insurance as a result of an increase in a insurance portfolio and in agricultural insurance as a result of a number of losses caused by natural forces in the first half of 2016;
- lower net investment result by PLN 126.4 million, mainly due to lower dividend from PZU Życie;
- higher acquisition costs (an increase by PLN 278,0 million), resulting mainly from an increase in direct acquisition costs as a result of expanding insurance portfolio. Simultaneously, bankassurance recorded a drop of direct acquisition costs, which resulted from the changes in bancassurance agreements – from 1 April, in accordance with the requirements of the Act on Insurance Activity, the rules of remuneration for group agreements were changed;
- drop in administrative costs to PLN 723.9 million compared to PLN 753.7 million in 2015, mainly due to applied cost discipline.

PZU's technical result in 2016 (PLN million)



Basic amounts of the profit and loss account: in PLN million	2016	2015	2016/2015 in PLN million	2016/2015 in %
Gross written premiums	10,682.0	8,858.0	1,824.0	20.6%
Net premiums earned	9,212.8	7,898.0	1,314.9	16.6%
Net claims and benefits	(6,148.5)	(5,036.6)	(1,111.9)	22.1%
including paid gross claims and benefits	(6,393.0)	(5,135.2)	(1,257.8)	24.5%
Acquisition expenses, including reinsurance commission	(1,849.5)	(1,571.5)	(278.0)	17.7%
Administrative expenses	(723.9)	(753.7)	29.8	(4.0)%
Technical result	536.5	636.3	(99.8)	(15.7)%
Net investment result	1,897.6	2,024.0	(126.4)	(6.2)%
Gross profit (loss)	1,876.3	2,475.9	(599.6)	(24.2)%
Net profit (loss)	1,593.0	2,248.5	(655.6)	(29.2)%

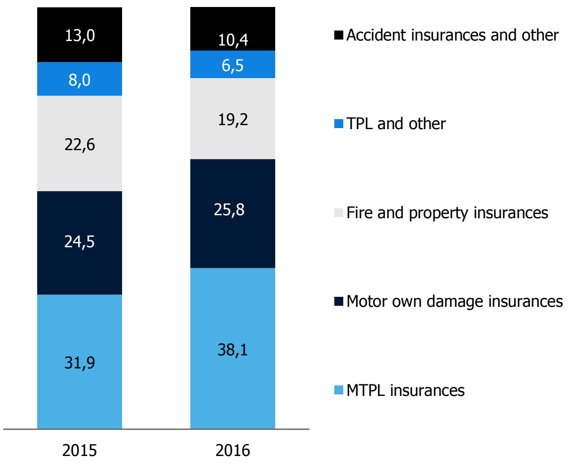
6.2 Gross written premium

Premiums

Gross written premiums **GLOSSARY** in 2016 amounted to PLN 10,682.0 million, which means an increase by 20.6% compared to 2015. They comprised mainly:

- MTPL insurance premiums comprised 38.1% of the PZU's insurance portfolio (31.9% in the prior year). In 2016, their value was 44.2% higher than in the previous year, mainly due to an increase in average premium which resulted from changes in average price, which have been implemented from late 2015, and a growing number of insurances;
- motor own damage insurance premiums with 25.8% share in PZU's total gross written premium (i.e. 1.4 p.p. higher than in corresponding period of the previous year) – growth resulting from higher number of insurance and gradually implemented price increases;
- fire and property insurance premiums comprising 19.2% PZU's premium portfolio. In 2016, their share dropped by 3.4 p.p. but their value was up by 2.4% from the previous year – resulting from the acquisition of several big contracts of inward reinsurance and of higher sales volume of household insurance;
- accident and other insurance premiums, which had a 10.4% share, (a drop of 2.6 p.p. from 2015). This insurance category recorded decrease in the premium written in other financial losses due to decrease in obligatory amount inward reinsurance agreement with a big client.

Structure of PZU Group's gross written premium (in %)



6.3 Investment activity

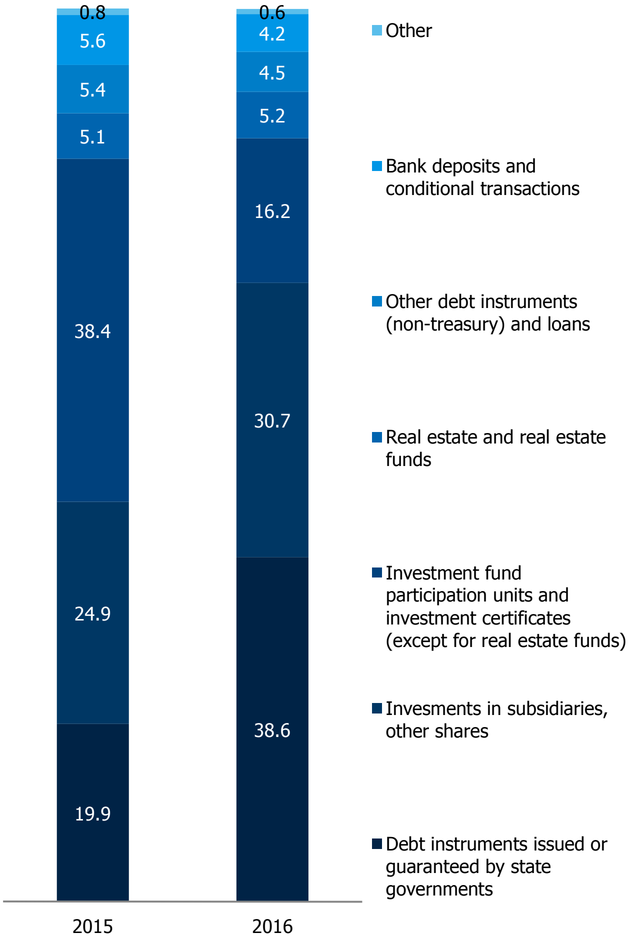
The investment activity of PZU was aimed mainly to properly match the structure of assets with the structure of liabilities, maintaining the appropriate security, profitability and liquidity at the same time.

In 2016, PZU's net investment result amounted to PLN 1,897.6 million compared with PLN 2,024.0 million in 2015 (drop of 6.2%). Without the dividend obtained from PZU Życie, PZU's net investment result amounted to PLN 1,072.6 million, compared with PLN 333.8 million in the previous year.
The following factors had the greatest impact on the increase in the result:

- redemption of participation units in PZU Specjalistyczny Fundusz Inwestycyjny Otwarty Universum and the resulting realization of revaluation reserve in the amount of PLN 764.4 million,
- better performance of currency instruments caused by positive currency rate differences, which were higher than instruments denominated in foreign currencies in 2015 compensated by slightly lower results on interest bearing financial instruments.

In December 2016, the value of PZU's investments portfolio amounted to PLN 31,476.6 million compared with PLN 32,356.0 million as at the end of 2015.

Financial asset structure (in %)[2]



The largest part of PZU investment portfolio are debt securities issued by governments (38.6%). The increase in comparison to 2015 resulted mainly from the redemption of participation units in PZU Specjalistyczny Fundusz Inwestycyjny Otwarty Universum. The redemption of the fund units was to a large extent performed in a non-cash form, i.e in the form of Polish treasury bonds. As a result of this transaction, as well as redemption of investment certificates of the PZU Fundusz Inwestycyjny Zamknięty Dynamiczny fund, the share of Investment fund participation units and investment certificates (excluding real property funds) dropped. Portfolios of funds included in this investment category encompassed mainly corporate loans and non-treasury bonds, as well as listed shares; whereas as the result of the above-mentioned transactions of redeeming participation units and investment certificates, the share of treasury bonds significantly decreased.

A considerable part of PZU's portfolio, apart from investment funds, was composed by investments in subsidiaries, other shares and stocks. Their share amounted to 30.7% compared to 24.9% at the end of 2015. PZU Życie shares were the largest share in the investments of this category, while the main reason for the increase in this category of investments was the acquisition offor the new issue of Alior Bank shares in 2016.

PZU did not apply hedge accounting in 2016.

6.4 Claims and technical provisions

In 2016, the total net amount of claims and benefits and increase in provisions of PZU amounted to PLN 6,148.5 million. In relation to 2015, the value of claims together with the change of provisions was higher by 22.1%. The following factors also contributed to the change in the net value of claims and benefits:

- considerable increase in losses in crop insurance as a result of a number of claims caused by forces of nature occurring in the first half of 2016 (claims from adverse effects of wintering were over PLN 230 million higher than the average during the last 3 years),
- increased value of claims and benefits in motor insurance resulting from a growth of insurance portfolio (higher number of reported claims) and a higher frequency of TPL claims' occurrence was partially offset by a decrease in an average payment;
- higher claims ratio in additional insurance, including insurance of assistance, offered mainly in the package with motor insurance.

[2] Specific investment categories with exception of investment funds presented in a seperate line.

6.5 Acquisition expenses and administrative expenses

In 2016, acquisition expenses without reinsurance commissions amounted to PLN 1,855.1 million and increased by 18.0% from 2015. The increase was caused mainly by a growth in direct acquisition costs (commission) which to a large extent resulted from a higher sales volume. At the same time, share of commissions in the written premium from bancassurance significantly dropped due to the change in settlement rules under bancassurance group contracts, which made them consistent with the regulations resulting from Article 18 and 19 of the amendment to the Act on Insurance Activity.

In 2016, the Group's administrative expenses were at the level of PLN 723.9 million, which was 4.0% lower than in the previous year due to stricter cost discipline, e.g. in the scope of real property costs (renovation services) and marketing.

6.6 Other operating income and technical and operating expenses result

The 2016 balance of technical revenue and expenses was negative and amounted to PLN 169.3 million. In comparison to 2015, the result was by PLN 55.9 million lower, e.g. due to significantly lower revenues from interests on delayed payments, a drop in technical revenues from retrocession, as well as a change in the value of impairment of receivables.

In 2016 the balance of other operating income and other operating expenses was negative and amounted to PLN 361.7 million compared with the positive balance in 2015 of PLN 19.3 million. As of mid- 2014, the balance of other operating costs was encumbered with the costs of interest and change in valuation of currency differences from the loan taken from PZU Finance AB for the total amount of EUR 850 million (EUR 500 million in July 2014 and EUR 350 million in October 2015). In 2016, the costs of interest and currency differences from the loan taken from PZU Finance AB (publ.) amounted to PLN 202.1 million, i.e. nearly 307,0% higher than in 2015, which resulted from higher currency differences.

Additionaly, tax on certain financial institutions has a relevant influence on the other operating costs – financial burden of this tax amounted PLN 147.7 million in 2016.

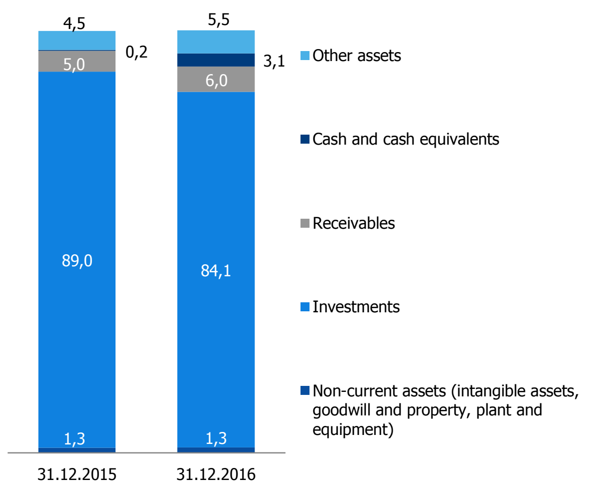
6.7 Structure of assets and liabilities

As at 31 December 2016, the balance total of PZU amounted to PLN 37,418.6 million and was 2.9% higher than at the end of 2015.

Assets

Investments composed the main element of PZU's assets and reached the total value of PLN 31,476.6 million (a 2.7% drop from the end of 2015), which amounted to 84.1% of PZU's balance total compared to 89.0% at the end of the previous year. With exception of investments in subsidiaries, this level was 10.3% lower. The growth of investment value in subsidiaries resulted mainly from the 2016 acquisition of new issue of Alior Bank shares.

PZU's assets structure (in %)



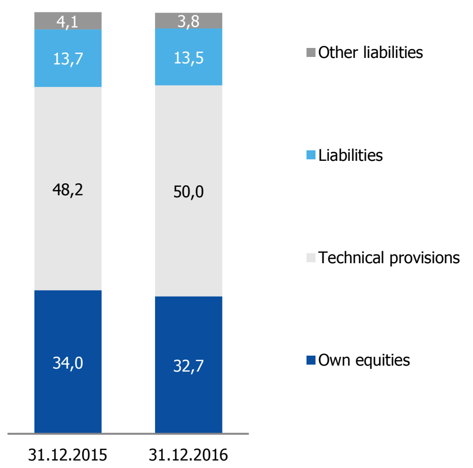
PZU's receivables amounted to PLN 2,252.4 million and composed 6.0% of assets. In comparison, their value at the end of 2015 was 1,801.9 million (5.0% of PZU's assets). The most significant increase was recorded in the value of receivables from direct insurance, resulting from a dynamic growth in insurance portfolio (mainly motor insurance). Non-current assets – in the form of intangible assets, goodwill and property, plant and equipment – were disclosed in the statement of financial position at PLN 502.2 million. They comprised 1.3% of total assets.

As at 31 December 2016, PZU held cash of PLN 1,148.0 million (3.1% of the assets). A year earlier, they amounted to PLN 65.1 million.

Liabilities

At the end of 2016, the main component of PZU's liabilities was technical provisions. They amounted to PLN 18,714.8 million, which represented 50.0% of liabilities. Their share in the balance sheet increased by 1.8 p.p. compared to 2015, while their value increased by PLN 1,174.3 million, mainly due to the higher premium provisions in motor and various financial loss.

PZU's liabilities structure (in %)



At the end of 2016, equity amounted to PLN 12,219.0 million and composed 32.7% of the liabilities (drop by 1.3 p.p.).

The balance of other liabilities and special funds at the end of 2016 amounted to PLN 5,156.2 million, composing 13.8% of PZU's liabilities. The balance value rose by 0.9% from the previous year.

Cash Flow Statement

The net cash flows from operating activity at the end of 2016 amounted to PLN 722.5 million and increased by PLN 342.7 million compared to the previous year.

Off-balance sheet items

In 2016 the method of drafting the financial statements was changed, including the presentation method for granted insurance guarantees and bills of exchange used as collaterals. The change was introduced in order to more closely reflect the economic content of such collaterals. At the moment, the collaterals are presented up to the amount of granted guarantees.

Conditional receivables amounted to PLN 4,357.1 million and declined by PLN 5,261.2 million from the previous year. They included the following:

- received guarantees and sureties (a drop of PLN 10.5 million compared to the balance as at the end of the previous year);
- bills of exchange from granted insurance guarantees in amount of PLN 2,957.4 million (drop of PLN 4,725.5 million from the balance at the end of 2015) and
- other contingent receivables of PLN 953.1 million (down by PLN 786.4 million from the end of 2015) covering mainly mortgage collateral on debtor's property and other conditional receivables.

The balance of conditional obligations rose by PLN 47.6 million from the previous year. Growth was recorded mainly in granted guarantees and sureties, which included the guarantee granted to subsidiary PZU Finance AB. Guarantee with provided to all bondholders, which covers all liabilities of the issuer arising from the bonds (including the obligation for payment of the nominal value of bonds and interest on the bonds). The nominal value of bonds is EUR 850,000 thousand with maturity date as at 3 July 2019.

Loans taken and granted

At the end of 2016, PZU debt ratio increased to 23.6%[4].

On 23 March 2015 PZU granted a limit to the PZU Zdrowie loan at maximum PLN 200 million. The first two tranches of the loan has been paid in 2015 and the third in the amount of PLN 70 million has been paid on 4 July 2016. The loan is interest-free. It will be paid off in 120 equal installments with deadline of 31 December 2030.

On 9 November 2016, PZU granted a loan of PLN 80 million to TUW PZUW with the maturity deadline set for 4 January 2027.The loan was granted on market conditions (WIBOR plus 300 bps).

On 7 August 2013 a framework agreement in the field of cash loan transactions between PZU and PZU Życie was signed. Cash loans will be granted in PLN, for a specified period not longer than 12 months. The value of loans granted by either party can not exceed PLN 1 billion. In 2016, PZU Życie granted loans for a total amount of PLN 1,350,000.00 thousand, and in 2015 – PLN 1,300,000.00 thousand. As at 31 December 2016, all loans have been repaid.

Increase of Alior Bank's share capital

On 24 June 2016, the capital of Alior Bank was increased in the National Court Register by 56 550 249 ordinary series I bearer shares with a nominal value of PLN 10 and issue price of PLN 38.90 each. PZU acquired 14 247 701 shares composing 25.19% of the newly issued shares (proportionally to the share held previously) for the amount PLN 554,236 thousand. In effect, the share of PZU Group in share capital and votes at the Alior Bank General Shareholders' Meeting remained unchanged. Additionally, PZU Życie and investment funds controlled by PZU acquired the shares of the new issue proportionally to the shares held previously.

[4] Debt ratio calculated as Liabilities from received loans/(Equity + Liabilities from received loans).

6.8 Share of the business segments in the PZU's results

For management purposes, PZU has been divided into the following business segments:

- corporate insurance (non-life). This segment encompasses a wide range of non-life insurance, general liability and motor insurance, which are adapted to customer needs and, with individually valued risks, offered by PZU to large business entities.
- Mass-market insurance (non-life). This segment comprises property, accident, general liability, and motor insurance. PZU provides the insurance to individuals and entities from the SME sector.

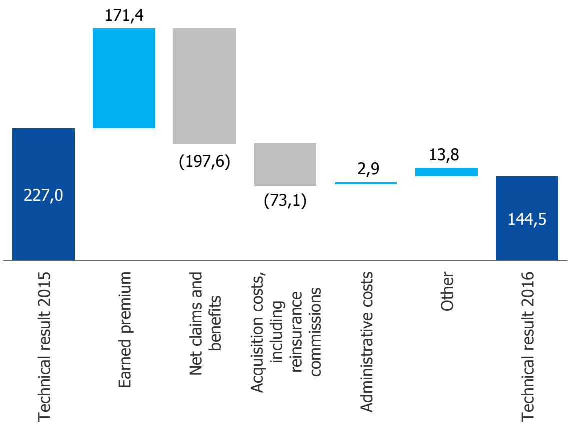
Corporate insurance

In 2016, the corporate insurance segment earned a technical result of PLN 144.5 million, which is 36.4% less than in the previous year.

The 2016 level of this segment was determined by the following factors:

- 11.8% growth of net earned premium and simultaneous increase in the gross written premium by 18.7% compared with 2015. In 2016, sales increased mainly in the motor insurance (including motor own damage that grew by PLN 204.6 million), due to the increased average premium and growing number of insurance policies and in other property insurance and casco insurance for maritime and inland navigation, as a result of acquisition of several contracts of a high single value. The growth of the gross written premium was partially offset by the declining sales in the group of general TPL insurance (down by PLN 46.2 million) and other tangible damage produced by TUW PZUW being joined by several major entities in the coal and energy sectors, who were previously clients of PZU SA;
- 23.4% increase in net claims and benefits from the previous year, which, considering a 11.8% growth in the net premium earned, means that the claims ratio increased by 6.0 p.p.

The technical result of the corporate segment (in PLN million)



Growth of claims ratio was recorded in general liability insurance (submission of several major claims), as well as in insurance of various financial risks. The effect was partially offset by the improved claims ratio in MTPL portfolio (claims ration lower by 12.3 p.p.), despite of a higher value of claims that results from expansion of the insurance portfolio;

- higher acquisition costs by PLN 78.8 million, i.e. 28.0% compared to 2015, resulting mainly from higher direct acquisition costs (a consequence of increased sales dynamics) and a lower level of deferral of costs;
- slight drop in administrative costs to PLN 121.4 million, i.e. 2.4% year-on-year. Lower costs in 2016 result mainly from application of cost discipline, both in the current operations, as well and in projects.

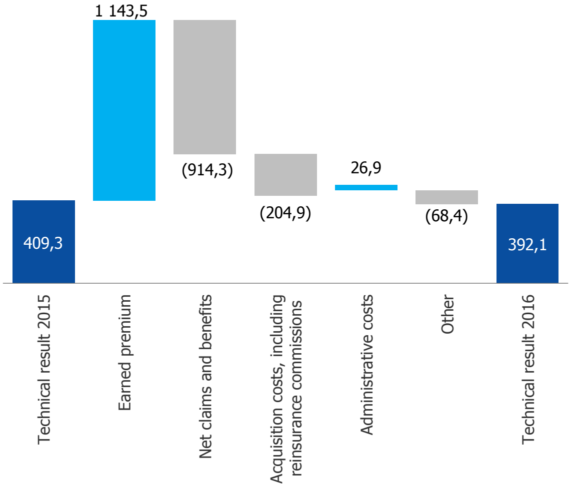
Mass client insurance

In 2016, the technical result in the mass client insurance segment amounted to PLN 392.1 million (a 4.2% decrease compared with the prior year).

This result was determined by the following factors:

- 17.7% growth in the net earned premium to PLN 7,586.4 million. At the same time, gross written premium grew by 21.1% year-on-year, mainly in the motor insurance group (+35.8%) due to an increase in average premium which resulted from changes in average price, which have been implemented from late 2015. Increase in premiums was recoreded in assistance insurance (resulting from sales of additional risks mainly together with motor insurance), in other tangible damage insurance (+5.5%) and in TPL insurance (mainly in PZU DOM household insurance). At the same time, a decrease in premium from insurance of other financial losses was recorded, which resulted from changes in obligatory inward reinsurance agreement with a big client.
- net claims and benefits were at the level of PLN 5,105.8 million, i.e. they increased by 21.8% in relation to 2015, mainly due to:
  - higher compensations in crop insurance as a result of a number of claims caused by forces of nature occurring in the first half of 2016 (claims from adverse effects of wintering were over PLN 230 million higher than the average during the last 3 years),
  - higher value of claims and benefits in MTPL insurance resulting from the increased insurance portfolio;
- acquisition expenses amounted to PLN 1,494.2 million, 15.8% higher than those of the previous year. The change in acquisition costs was determined by the higher level of direct acquisition costs (including the effect of the rising insurance portfolio). Simultaneously, bankassurance recorded a drop of direct acquisition costs, which resulted from the changes in agreement with banks – from 1 April, in accordance with the requirements of the Act on Insurance Activity, the rules of remuneration for distribution of group agreements were changed;
- administrative expenses which amounted to PLN 602.6 million, decreased by 4.3% compared with 2015. Lower costs result mainly from applied cost discipline (e.g. in real property costs and marketing costs), partially offset with the change in bancassurance group contracts and as a result recognition of remuneration for administrative activities amounting to approximately PLN 50 million.

The technical result in the mass client insurance segment (in PLN million)



6.9 Operating efficiency ratios

In 2016, PZU's return on equity was 13.0%. ROE was 5.2 p.p. lower than in the previous year.

On average, the 2014-2016 return on equity (ROE) was almost 17.5%.

One of the basic efficiency and operating measures of an insurance company is the combined ratio (COR), which PZU has maintained at a level proving high profitability in recent years. The operating efficiency ratios are presented below.

Key profitability ratios of PZU Group	2016	2015	2014	2013	2012
Rentability of equity (ROE) *(annualized net profit / average equity) x 100%*	13.0%	18.2%	21.4%	39.7%	20.5%
Rentability of assets (ROA) *(annualized net profit / average assets) x 100%*	4.3%	6.3%	8.1%	17.0%	9.0%
Administrative expense ratio *(administrative expenses / premium earned net of reinsurance)*	7.9%	9.5%	9.2%	8.2%	8.2%
Return on Sale *(net income / gross written premium) x 100%*	14.9%	25.4%	31.9%	61.7%	30.5%

	Operating efficiency ratios	2016	2015	2014	2013	2012
1	Claims ratio gross *(Gross claims /gross written premium) x 100%*	58.8%	61.2%	65.5%	61.2%	66.4%
2	Claims ratio net of reinsurance *(claims and benefits net of reinsurance/net premium earned) × 100%*	66.7%	63.8%	66.2%	62.2%	66.1%
3	Insurance activity costs ratio *(Costs of insurance activity/premium earned net of reinsurance) x 100%*	27.9%	29.4%	28.5%	25.0%	26.2%
4	Acquisition expenses ratio* *(Acquisition costs/premium earned net of reinsurance)* *x 100%*	20.1%	19.9%	19.3%	16.9%	18.1%
5	Administrative costs ratio *(Administrative costs/premium earned net of reinsurance) x 100%*	7.9%	9.5%	9.2%	8.2%	8.2%
6	Combined ratio (COR) *(claims + costs of insurance activity/premium earned net of reinsurance)* *x 100%*	94.7%	93.2%	94.7%	87.3%	92.3%

** following recognition of obtained reinsurance commission*

07

7 Risk management

Contents:

7.1 Risk management objective

Risk management in PZU aims to:

- increase the value of PZU through active and conscious management in the amount of exposure to risk;
- prevent acceptance of risk at a level which could threaten the financial stability of PZU.

Risk management at PZU is shared by the whole PZU Group.

Risk management in PZU Group is based on risk analysis of all processes and entities, and it is an integral part of the management process.

The main elements of an integrated risk management system are consistent for all insurance companies of PZU Group and implemented in a way which ensures the realization of strategic plans of individual companies and secures business objectives of the whole PZU Group. They include, among others:

- systems of limits and restrictions of the acceptable risk level, including the level of risk appetite;
- processes of identification, measurement, and assessment, monitoring and control, reporting and management actions with respect to individual risks;
- risk management organizational structure, in which Management Boards and Supervisory Boards of companies, as well as dedicated Committees, play the key roles.

Companies from other financial market sectors are obliged to follow the standards applicable to a given sector. In internal regulations adopted, they specify among others the following:

- processes, methods, and procedures that enable risk measurement and management;
- segregation of duties in the risk management process;
- scope, terms and conditions, and frequency of reporting on risk management.

PZU supervises the PZU Group risk management system under cooperation agreements with PZU Group entities and on the basis of information provided as per such agreements. It also manages PZU Group aggregated risk, especially as far as the capital requirements are concerned.

Moreover, there exist the processes in PZU Group that help ensure effectiveness of risk management on the Group level. Risk management rules in the PZU Group subsidiaries include recommendation of PZU SA (parent company) concerning the organization of risk management system in subsidiaries in both insurance and banking sector.

The management boards of the PZU Group entities are responsible for performing their duties in line with generally applicable regulations of domestic and international law, especially for implementing adequate and effective risk management system.

Supervisory Boards exercise supervisions over risk management systems in particular regulated entities. In its subsidiaries, including Alior Bank, PZU designates its representatives to join the supervisory boards.

7.2 Risk management system

The risk management system of PZU Group is based on:

- organizational structure – including division of responsibilities and tasks performed by management bodies, committees as well as organizational units in the risk management process;
- risk management process, including the methods of identification, measurement and assessment, monitoring and control, reporting risk and taking management action.

The organizational structure of the risk management system is consistent within PZU Group and in individual insurance companies within PZU Group and includes four competence levels.

The first three are as follows:

- Supervisory Board, which oversees the risk management process and assesses its adequacy and effectiveness as part of its decision-making powers defined in the company's By-laws and the Supervisory Board rules and regulations, as well as through the appointed Audit Committee;
- Management Board, which organizes the risk management system and ensures its functionality through approving the strategy and policies and defining the risk appetite, the risk profile and tolerance for individual categories of risk;
- Committees which make decisions to reduce individual risks to a levels determined by the risk appetite. Committees implement the procedures and methodologies for mitigating individual risks and accept their limits.

Fourth level of competence relates to operational actions and is divided between the three lines of defense:

- first line of defense – ongoing risk management at the business unit and organizational unit level and decision-making as part of the risk management process;
- second line of defense – risk management by specialized units responsible for risk identification, monitoring and reporting, as well as controlling limits;
- third line of defense – comprises internal audit, which conducts independent audits of the elements of the risk management system, as well as control activities embedded in the activity.

Established in 2016, the PZU Group Risk Committee supports (both Supervisory Boards and Management Boards of subsidiaries) in implementing effective risk management system which is consistent within the entire PZU Group. The objective of the PZU Group Risk Committee is to coordinate the actions and exercise supervision over risk management systems and processes present in PZU Group.

7.3 Risk appetite

The risk appetite is defined in PZU Group as the amount of risk taken in order to achieve business objectives and it is measured by the level of potential financial losses, decrease in the value of assets or an increase in the value of liabilities in a one-year period.

The risk appetite determines the maximum level of acceptable risk when setting individual partial risk limits and restrictions which, when exceeded, result in taking actions necessary to limit further risk growth.

In all insurance PZU Group companies, the process of determining the risk appetite and limits for individual categories of risk that is in line with the group process was implemented. The Management Board in each company determines the risk appetite, risk profile, and tolerance limits which reflect its strategic plans and objectives of the entire PZU Group. Such an attitude ensures appropriateness and efficiency of the risk management system in PZU Group and prevents risk acceptance at a level which could pose a threat to the financial stability of individual companies or the entire PZU Group. The Management Board is responsible for determining the appropriate risk level for every company, whereas the risk unit reviews the level of risk appetite once a year. All the activities are coordinated at the level of the Group.

Identification

Begins with the proposal to commence the creation of an insurance product, acquire a financial instrument, change the operating process, as well upon the occurrence of any other event which potentially results in a risk. The identification process takes place until the expiry of the liabilities, receivables or activities related to the given risk. The identification of market risk involves recognising the actual and potential sources of such risk which are then identified as to their relevance.

Risk measurement and assessment

Risk measurement and assessment are performed depending on the characteristics of the given risk type and the level o its relevance. The risk assessment is performed by specialised units. In every company, the risk unit is responsible for development of risk assessment tools and risk assessment process to the extent which specifies risk appetite, risk profile and risk tolerance levels.

Risk monitoring and control

This involves ongoing reviews of any variances from the assumed parameters, namely limits, thresholds, plans, values from the previous period, recommendations and guidelines issued.

Reporting

Allows efficient risk communication and supports risk management at various decision-making levels.

Management actions

These activities encompass among others risk mitigation, risk transfer, risk avoidance, specifying risk appetite, acceptance of risk tolerance levels, as well as tools which facilitate such activities, i.e. thresholds, reinsurance plans and reviews of underwriting policy.

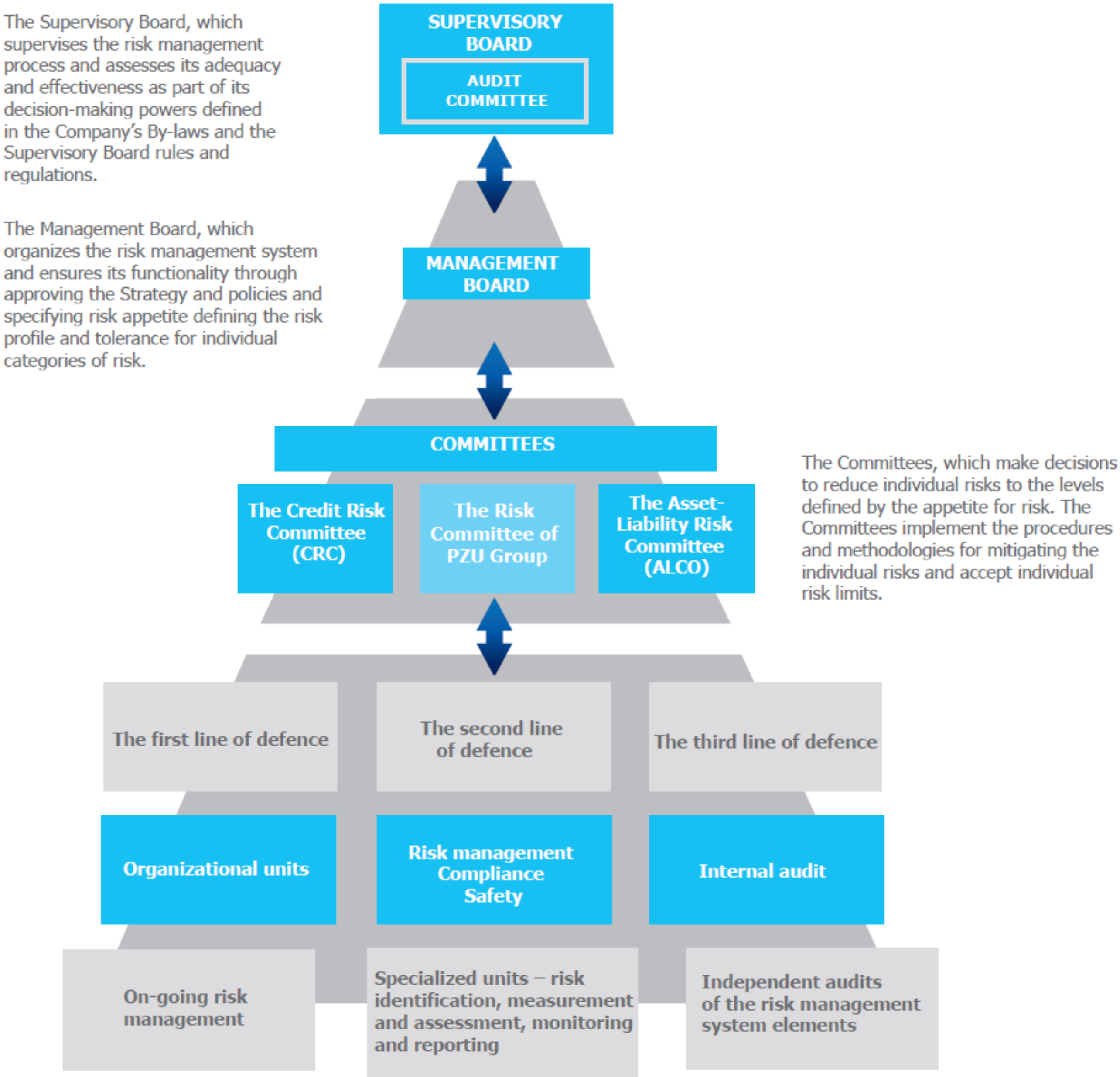
7.4 Risk management process

Two levels are distinguished in the risk management process:

- PZU Group level – ensures that PZU Group implements its business objectives in a safe way which is adequate to the degree of risk involved. This level engages the monitoring of limits and risks specific to PZU Group, such as: catastrophe risk, financial risk, counterparty risk, or concentration risk. PZU Group provides support in implementation of the integrated risk management system which encompasses introducing coherent mechanisms, standards, and operational organization of an effective internal control system (with special focus on compliance function), risk management system (especially in the reinsurance field), and security management system at PZU Group, as well as monitors their regular application. Dedicated employees from PZU Group cooperate with Management Boards of the companies and with management of such areas as finance, risk, actuary, reinsurance **GLOSSARY**, investment, and compliance, under relevant cooperation agreements;
- entity level – ensures that a PZU Group entity implements its business objectives in a safe way which is adequate to the degree of risk involved by this entity. This level engages the monitoring of limits and specific risk categories present in a given entity and introducing coherent mechanisms, standards, and operational organization of an effective internal control system (with special focus on compliance

function), risk management system (especially in the reinsurance field), and security management system to the structure of the integrated risk management system.

Organizational structure of risk management system



7.5 Risk profile of PZU Group

The main types of risks incurred by PZU Group include actuarial risk, market risk, credit risk, concentration risk, operational risk, and compliance risk. The main risks associated with the activity of Alior Bank include the following: credit risk, operational risk, and market risk (covering interest rate, liquidity, foreign currency, and commodity price risk). The overall risk of Alior Bank constitutes approximately 9% of the total risk of PZU Group, whereas the credit risk makes up the largest contribution.

Underwriting risk

It is a risk of loss or an adverse change in the value of liabilities which may arise from insurance contracts and insurance guarantee agreements in relation to improper assumptions regarding premium valuation and establishment of technical and insurance provisions **GLOSSARY**.

The process of risk identification starts with the idea of creating an insurance product and it lasts until the related liabilities expire. Underwriting risk identification is carried out, inter alia by means of:

- analysis of general insurance terms in respect of the accepted risk and compliance with generally applicable provisions of law;
- analysis of general/specific insurance terms or other agreement templates in respect of the underwriting risk accepted under such agreements;
- recognition of potential risks related to a given product, performed in order to measure and monitor them in the future;
- analysis of the influence of introducing new insurance products on capital requirements and the Company's risk margin calculated according to the standard formula;
- verification and validation of changes to products;
- assessment of underwriting risk viewed in the framework of similar existing products;
- monitoring of the existing products;
- analysis of the policy relating to underwriting, tariffs, provisions, and reinsurance, as well as the claims and benefits handling process.

Underwriting risk assessment involves recognizing the degree of exposure or a group of exposures related to the possibility of incurring a loss and analyzing the risk elements in order to make a decision on whether PZU should accept a risk for insurance and assume liability. The aim of the risk assessment (underwriting **GLOSSARY**) is the assessment of future claims and the reduction of anti-selection. Underwriting risk assessment covers also actions related to reinsurance **GLOSSARY** of the largest and the highest risks.

Underwriting risk measurement is based in particular on:

- analysis of selected ratios;
- scenario method – analysis of impairment arising from an assumed change in risk factors;
- factor method – a simplified version of the scenario method, reduced to one scenario per risk factor;
- statistical data;
- exposure and sensitivity measures;
- expertise of company's staff.

Monitoring and controlling the underwriting risk involve regular analyses of the risk level and determination of the utilization level of the agreed risk tolerance thresholds and limits specified in the Risk management strategy in PZU Group.

Reporting aims to ensure efficient underwriting risk communication and supports underwriting risk management at various position from the employee level to the Supervisory Board. The frequency of individual reports and the scope of information is tailored to meet the information needs at different decision-making levels.

Administration activities in the underwriting risk management process are carried out in particular by:

- specifying the level of tolerance of underwriting risk and monitoring thereof;
- business decisions and sales plans;
- calculating and monitoring the adequacy of technical provisions **GLOSSARY**;
- tariff strategy, as well as monitoring existing estimates and assessing the adequacy of the premium;
- process of assessment, measurement, and acceptance of underwriting risk;
- use of actuarial risk mitigation tools, including, in particular, reinsurance **GLOSSARY** and prevention.

Furthermore, in order to reduce the underwriting risk associated with the ongoing activities the following actions, in particular, are undertaken:

- definition of the scopes of liability in the general/specific terms of insurance or other agreement templates in the financial insurance sector;
- definition of the exclusions of liability in the general/specific terms of insurance or other agreement templates in the financial insurance sector;
- definition of the scopes of liability and exclusions in the general terms of insurance;
- reinsurance activities;
- adequate tariff policy;
- application of appropriate methodology of provisions calculation;
- appropriate underwriting **GLOSSARY** procedure;
- appropriate claims handling procedure;
- sales decisions and plans;
- prevention.

Market risk

Risk of a loss or an adverse change in the financial standing, which directly or indirectly arises from fluctuations and changes in market prices of assets, credit spread, value of liabilities, and financial instruments.

The nature of the process of credit spread risk management and concentration risk varies from management process of other subcategories of market risk and has been defined in the next section (**CREDIT AND CONCENTRATION RISK**) along with the process of managing counterparty insolvency risk.

The investment activity in PZU Group entities is regulated in a number of documents approved by the Supervisory Boards, the Management Boards and dedicated Committees.

The identification of market risk involves recognizing the actual and potential sources of such a risk. In the case of assets, the market risk identification process begins when a decision is made to commence transactions on a given type of financial instrument. The units which decide to start transactions on a given type of a financial instrument prepare the description of the instrument, including, in particular, the description of the risk factors. The description is then submitted to the risk management unit which uses it to identify and assess the market risk.

The process of identifying market risk related to insurance liabilities starts simultaneously with the process of creating an insurance product and involves identifying the relationship between the amount of cash flows associated with this product and the market risk factors. Identified market risks are assessed in terms of materiality, i.e. based on whether the materialization of a risk would be related to a loss that could affect the financial standing.

The market risk is measured using the following measures of risk:

- VaR, i.e. Value at Risk – a risk measure quantifying the potential economic loss, which will not be exceeded over a period of one year with a 99.5% probability under normal market circumstances;
- standard formula;
- exposure and sensitivity measures;
- accumulated monthly loss.

The following stages of the market risk measurement process can be distinguished:

- collection of information on assets and liabilities that generate market risk;
- calculation of the value of the risk.

The risk measurement is performed:

- for the measures of exposure and sensitivity of instruments;
- when using a partial internal model.

Monitoring and control of the market risk involves analyzing the risk levels and utilization of limits.

Reporting consists of communicating the level of market risk and the effects of monitoring and control to the different decision-making levels. The frequency of individual reports and the scope of information is tailored to meet the information needs at different decision-making levels.

Management actions regarding market risk include, in particular:

- concluding transactions to mitigate market risk, such as selling a financial instrument, closing out a transaction on a derivative, and purchasing a hedging derivative;
- diversifying the portfolio of assets, in particular with respect to market risk categories, maturities of instruments, concentration of exposure in one entity, geographical concentration;
- setting market risk restrictions and limits.

The setting of limits is the main management tool for maintaining risk positions within acceptable risk levels. The structure of limits for the individual market risk categories and the organizational units is defined by dedicated Committees in line with the risk tolerance determined by the Management Board.

Credit risk and concentration risk

Credit risk is the risk of loss or adverse change of the financial standing resulting from fluctuations of reliability and creditworthiness of issuers of instruments, counterparties and debtors, which materializes in the default of counterparty or an increase in credit spread.

Concentration risk is a risk arising from a lack of diversification in the portfolio of assets or from high exposure to the risk of default by a single issuer of instruments or a group of related issuers.

Identification of the credit and concentration risk takes place at the stage of making a decision to invest in a new type of financial instrument or the credit exposure to a new entity. Identification is based on an analysis of whether a given investment is related to credit or concentration risk, on which its level and volatility depends. The actual and potential sources of credit and concentration risk are identified.

Risk assessment is based on estimating how probable it is that the risk occurs and a potential impact of such an occurrence on the financial standing.

Credit risk is measured with the use of the following tools:

- exposure measures (the amount of the gross and net credit exposure and maturity-weighted net credit exposure);
- standard formula.

Concentration risk for a single entity is calculated in accordance with the standard formula.

The total concentration risk is measured as the sum of concentration risks of individual entities. In the case of related entities, concentration risk is specified for all related entities cumulatively.

Monitoring and controlling of the credit and concentration risk involve analyzing the current risk level, assessing creditworthiness, and determining the level of utilization of the limits set.

Monitoring is conducted for:

- financial insurance exposures;
- reinsurance exposures;
- exposure limits and VaR limits.

Reporting consists of communicating the level of credit and concentration risk and the effects of monitoring and control to different decision-making levels. The frequency of individual reports and the scope of information is tailored to meet the information needs at different decision-making levels.

Management actions with respect to credit risk and concentration risk include, in particular:

- setting limits of exposure to a single entity, group of entities, sectors or states;
- diversifying a portfolio of financial assets and insurance, mainly with respect to the state, sector;
- accepting security;
- concluding transactions aimed at mitigating credit risk, such as selling a financial instrument, closing out a derivative transaction or purchasing a hedging derivative, restructuring of the granted debt;
- reinsuring **GLOSSARY** a financial insurance portfolio.

The structure of credit and concentration risk limits for the individual issuers is determined by dedicated committee in line with the risk tolerance.

Operational risk

Is a risk of loss resulting from incorrect or erroneous internal processes, human actions, operation of systems or external factors.

Identification of operational risk is carried out, in particular, by means of:

- collecting and analyzing information on operational risk incidents;
- operational risk self-assessment;
- scenario analyses.

Assessment and measurement of operational risk is carried out by means of:

- identifying the results of operational risk incidents;
- estimating the results of potential operational risk incidents which may occur in the course of business activity.

Monitoring and controlling operational risk is carried out mainly by established operational risk indicators which make it possible to assess the change of operational risk level and the factors that influence the risk level in business activities.

Reporting consists of communicating the level of operational risk and the effects of monitoring and control to the different decision-making levels. The frequency of individual reports and the scope of information is tailored to meet the information needs at different decision-making levels.

Management actions in response to identified and assessed operational risk involve in particular:

- reducing risk by taking actions aimed at minimizing the risk, i.a. by strengthening the internal control system;
- risk transfer – in particular by means of concluding an insurance agreement;
- avoiding risk by not engaging in or withdrawing from particular business activity when excessive operational risk is detected and its restriction would be too costly to make the venture profitable;
- risk acceptance – approval of consequences of a possible materialization of operational risk if its level does not exceed the tolerance level for operational risk.

The business continuity plans in the PZU Group companies are kept up to date and regularly tested.

Compliance risk

It is a risk that the PZU Group entities or persons related to the PZU Group entities violate or fail to comply with the provisions of law, internal regulations, or standards of conduct adopted by the PZU Group entities, including ethical norms, which result or may result in suffering by PZU Group or persons acting on its behalf legal sanctions, financial losses, or loss of reputation or credibility.

Compliance risk management process at the PZU and PZU Życie level concerns both the systemic operations, realized by the Compliance Bureau, and ongoing compliance risk management, for which responsible are the managers of the entities and organizational units of the Companies. Compliance risk is identified and assessed for individual internal processes of PZU and PZU Życie in line with the division of reporting responsibilities. Additionally, the Compliance Bureau identifies risks on the basis of legislative process, entries in the register of conflicts of interest, gifts, benefits and irregularities, as well as the enquiries it receives.

Among systemic operations, the following should be noted:

- development and implementation of systemic assumptions and internal regulations coherent with them;
- recommendation of solutions concerning the method for coherent compliance function realization and systemic compliance risk management to other entities of PZU Group;
- monitoring of the compliance risk management process comprising in particular: performance of compliance risk analyses, review of the implementation of guidelines concerning compliance risk management provided by external entities;
- providing consultation, interpretation, and guidelines in the scope of application of adopted standards of conduct and compliance risk management;
- planning and realization of training, as well as conducting internal communication in scope of compliance assurance;
- preparing reports and information in scope of compliance risk.

In turn, the operations related to the ongoing management mean, among others:

- compliance risk identification and assessment within the supervised area;
- compliance risk measurement;
- defining hedging instruments and instruments limiting the number and scale of occurring irregularities;
- reporting threats and compliance risk events to the Compliance Bureau;
- performing mitigating activities;
- constant compliance risk monitoring.

In addition, at the PZU level, the Compliance Bureau cares for coherent and uniform standards of compliance solutions in all PZU Group entities, as well as it monitors compliance risk at the PZU Group level.

In 2016, the PZU Group companies continued to adapt their compliance systems to standards set by PZU; the insurance companies subject to the Solvency II GLOSSARY regime additionally concentrated on adapting their business operations to the requirements of the directive.

Compliance risk is assessed and measured by determining the effects of materialization of the following risks:

- financial, resulting i.a. from administrative penalties, court verdicts, Office of Competition and Consumer Protection (UOKiK GLOSSARY) decisions, contractual penalties, and damages.
- intangible, such as loss of reputation, including damage to PZU Group's image and brand.

Compliance risk is monitored mainly through:

- analysis of reports received from the managers of the entities and organizational units;
- monitoring of regulatory requirements and compliance of PZU Group companies' operation to a changing legal environment;

- participation in legislative work on amending the generally applicable regulations;
- participation in the activities of professional organizations;
- coordination of external control processes;
- coordination of fulfilling the reporting requirements arising from the stock exchange regulations (PZU) and the statutory law;
- popularizing knowledge on competition and consumer protection law in PZU Group among the employees and adopting it to the fields they operate in;
- monitoring of anti-trust rulings and proceedings conducted by the President of the Office of Competition and Consumer Protection **GLOSSARY**;
- review of the recommendations of PZU Group's compliance unit;
- ensuring coherent realization of compliance function in PZU Group.

Management actions taken in response to the compliance risk comprise in particular:

- acceptance of risk, e.g. in connection with legal or regulatory changes;
- mitigation of risk, including adjustment of procedures and processes to regulatory requirements, issuing opinions and drafting internal regulations from the point of view of compliance, participating in the process of agreeing marketing activities;
- avoiding risk through the prevention of involvement in activities which do not comply with the regulatory requirements or good market practices, or which could have an adverse effect on their image.

Under compliance risk mitigation on a system and current level, among others the following mitigating activities have been implemented:

- current realization of effective compliance function as one of the key functions in the management system at the PZU Group companies;
- participating in consultations with legislative and supervision bodies (PZU Group's supervised companies) upon drafting regulations (public consultation);
- delegating representatives of PZU Group's supervised companies to participate in committee works at supervision bodies;
- conducting implementation projects for new regulations;
- training employees of the Group's companies in the field on new regulations, standards of conduct, and recommended remedial actions;
- issuing opinions on internal regulations of PZU Group companies and recommending potential changes with regards to compliance with legal provisions and accepted standards of conduct;
- verification of procedures and processes with regards to compliance with legal provisions and accepted standards of conduct;
- advance adjustment of documentation to upcoming changes of legal requirements;
- systemic supervision of PZU over realization of compliance function in PZU Group companies.

7.6 Reinsurance activity

Reinsurance cover in PZU secures insurance activity, reducing the consequences of the occurrence of catastrophic events which could adversely affect the financial standing of insurance companies. This objective was realized through mandatory reinsurance contracts supplemented with facultative reinsurance.

Reinsurance contracts of PZU

PZU uses concluded reinsurance contracts to mitigate its exposure to catastrophic losses (e.g. flood, hurricane) through, among others, a catastrophic non-proportional excess of loss contract and to the consequences of large one-off losses by non-proportional excess of loss contracts protecting property, technical, marine, aviation, TPL and MTPL portfolios. PZU's risk is also mitigated through reinsurance of the financial insurance portfolio.

Reinsurance premium from PZU's obligatory agreements accoridng to the S&P/AM Best rating

In 2016, the main partners providing treaty reinsurance cover to PZU were: Munich Re, Hannover Re, Scor and Swiss Re. As per S&P/AM Best, ratings of PZU reinsurance partners are high, which is an evidence of reinsurer's good financial standing and guarantees security to the Company.

PZU's activity in the area of inward reinsurance **GLOSSARY** includes other PZU Group's insurance companies. Further commitment to the protection of Baltic companies and LINK4 resulted in an increase in the related written premium.

In addition, PZU obtains gross written premium from inward reinsurance from activity on the domestic and foreign market, mainly through optional reinsurance.

7.7 Capital management

PZU Group aims to effectively manage the capital and maximize the rate of return for the shareholders of the parent company, especially alongside with ensuring a steady safety level and maintaining capital funds for strategic development through acquisitions.

On 3 October 2016, the Supervisory Board of PZU adopted a resolution regarding the confirmation of the Capital Structure and Dividend Policy of PZU Group for the years 2016–2020. The introduction of the Policy results from the implementation of Directive 2009/138/EC of the European Parliament and the Council dated 25 November 2009 on the taking-up and pursuit of the business of insurance and reinsurance (Solvency II), as amended, the Act on Insurance and Reinsurance dated 11 September 2015, and the expiry of "The Capital Structure and Dividend Policy of PZU Group for the years 2013–2015" updated in May 2014.

The capital management policy bases on the following rules:

- managing the PZU Group's capital (including surplus capital) at the level of PZU as the parent entity;
- maintaining target solvency ratios at the level of 200% for PZU Group, PZU, and PZU Życie (according to Solvency II);
- maintaining PZU Group's leverage ratio at a level no higher than 0.35;
- providing funds for development and acquisitions in the upcoming years;
- no share issues by PZU in the period of the Policy being in effect.

Solvency II ratio	Q3 2016	2015
PZU*	266.3%	284.4%

* *unaudited data*

7.8 PZU Group's capital and dividend policy

On 3 October 2016, the Supervisory Board of PZU adopted a resolution to pass the PZU Group's capital and dividend policy for 2016–2020 ("Policy").

The introduction of the Policy was the effect of the 1 January 2016 implementation of Directive 2009/138/EC of the European Parliament and of the Council of 25 November 2009 on the taking-up and pursuit of the business of Insurance and Reinsurance (Solvency II), as amended, the Act on Insurance and Reinsurance Activity of 11 September 2015, and the end of the "Capital Structure and Dividend Policy of PZU Group for the years 2013–2015", which was updated in May of 2014.

According to the Policy, PZU Group is aiming towards:

- effective capital management through optimization of capital use from the perspective of the Group;
- maximizing the rate of return for the shareholders of the parent company, especially alongside with ensuring a steady safety level and maintaining

capital funds for strategic development through acquisitions;
- ensuring enough funds to cover the Group's liabilities towards its clients.

The capital management policy is based on the following rules:

- PZU Group's capital management (including surplus capital) at the level of PZU as the dominant entity;
- maintaining target solvency ratios at the level of 200% for PZU Group, PZU, and PZU Życie (according to Solvency II);
- maintaining PZU Group's leverage ratio at a level no higher than 35%;
- providing funds for development and acquisitions in the upcoming years;
- no share issues by PZU in the period of the Policy being in effect.

The capital management policy of PZU Group and PZU is based on the following rules:

- PZU Group aims to effectively manage the capital and maximize the rate of return for the shareholders of the parent company, especially alongside with ensuring a steady safety level and maintaining capital funds for strategic development through acquisitions;
- dividend amount proposed by the Management Board of the dominating entity paid out by PZU for the given financial year is established based on the consolidated financial result of PZU Group assigned to the dominating entity, where:
  - no more than 20% will raise the profits detained for purposes of organic development, innovation, and realization of growth initiatives (supplementary capital);
  - no more than 50% is subject to payout in scope of annual dividend;
  - the remaining part will be paid out as annual dividend or raise retained profits. (supplementary capital) if the given year includes realization of important expenditures associated with performance of the premises in PZU Group's Strategy, specifically concerning fusion and acquisition transactions;

with reservation of below points:

- according to the plans of the Management Board and own evaluation of risks and solvency of the dominating entity, the own funds of the dominating entity and PZU Group following declaration or payout of the dividend remain at a level ensuring fulfillment of the conditions specified in the capital policy;
- recommendations of the authority supervising the dividend are taken into consideration for dividend determination.

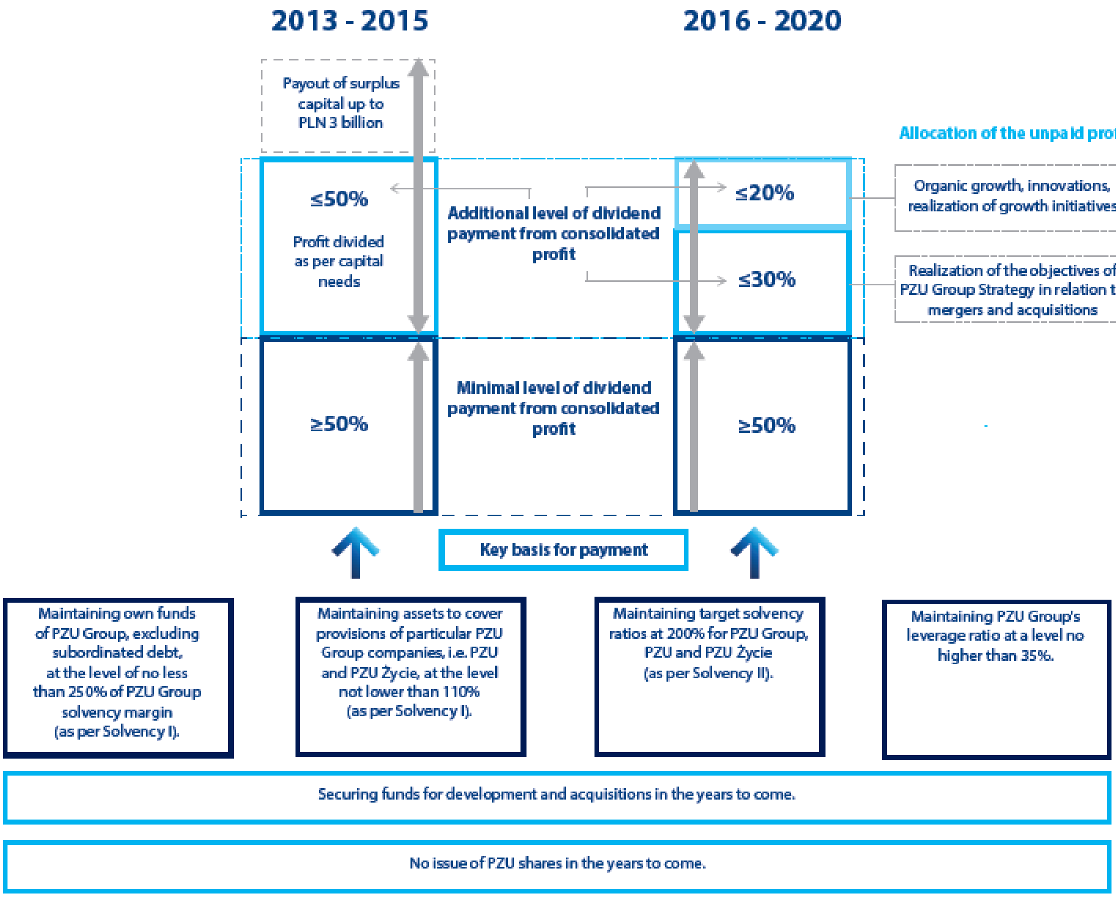
Payout of dividend for 2015

On 30 June 2016, the General Shareholders' Meeting of PZU adopted the resolution on the distribution of the net profit for the year ended 31 December 2015, in which it decided to allocate to the dividend payment the amount of PLN 1,796,127,840.00, i.e. PLN 2.08 per share. 30 September 2016 was chosen as the date according to which the list of shareholders entitled to the payment was established. Dividend was paid on 21 October 2016.

Issue of subordinated debt

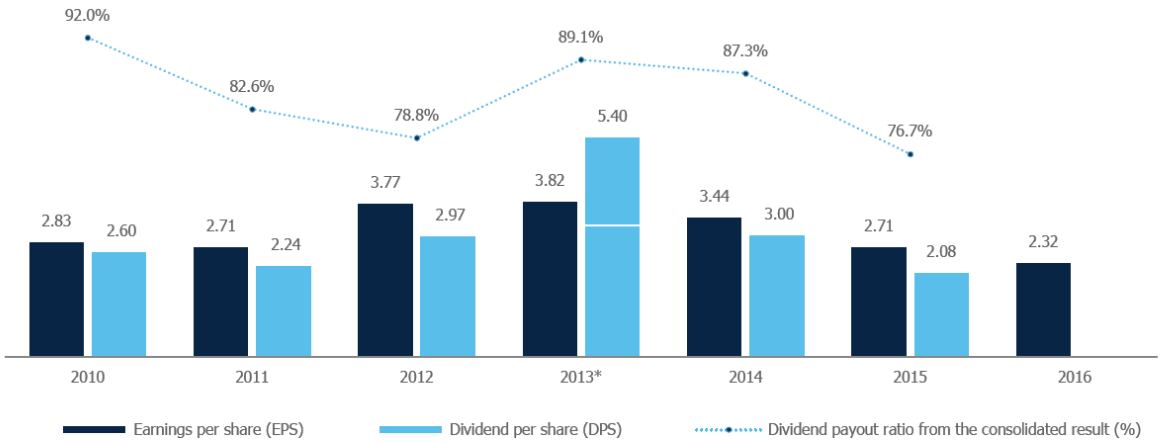
Moreover, as at 14 March 2017 PZU Supervisory Board approved the request of the PZU Management Board to the PZU General Shareholders Meeting regarding the adoption of the resolution on the issue of subordinated debt with a total par value not higher than PLN 3 bn.

Dividend and capital policy of PZU Group



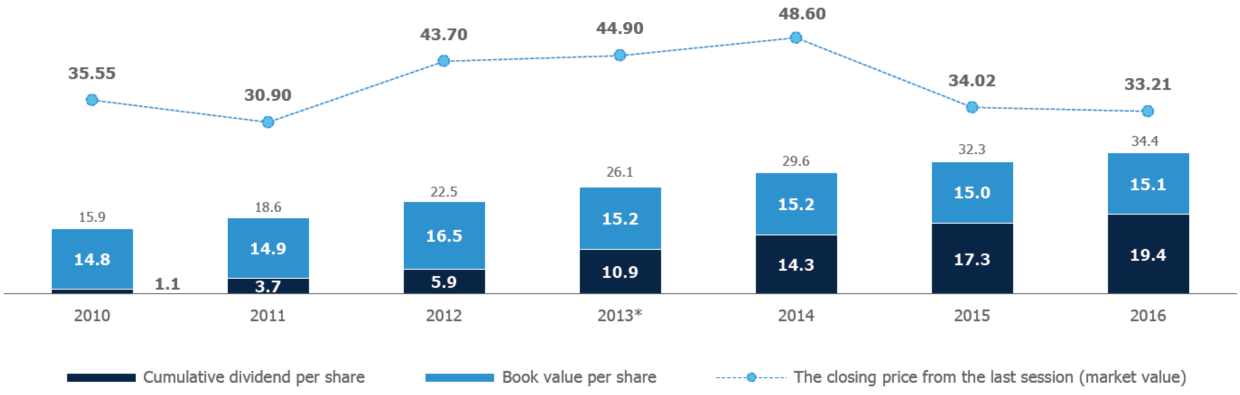
Source: PZU

2010–2016 profit and dividend per PZU share



* dividend from surplus capitalspaid in 2013 (PLN 2.00 per share)
** By the date of preparing this Management Report of PZU Group, the Management Board had not adopted a resolution concerning distribution of profit for 2016.

Book value per share and gross accumulated dividend per PZU share (PLN)



Payouts of PZU's dividends and Total Shareholder Return -TSR (2010–2016)

PSFA recommendation for payout of dividend for 2016

Similarly to previous years, on 6 December, the Polish Financial Supervision Authority presented an opinion concerning the dividend policy of banks, insurance and reinsurance companies, pension funds, brokerage houses, and investment funds in 2017 (download).

As per the supervisory institution's recommendation, the dividends should be paid only by the insurance companies that meet specific financial criteria. At the same time, the dividend payment should be limited to the maximum of 75% of the 2016 profit, maintaining the capital requirement coverage for the quarter concerning the dividend payout at minimum 110%. Simultaneously, PFSA permits dividend payment equal to the total profit of 2016 as long as the coverage of the capital requirement (after subtraction of the projected dividends from equity) at the end of 31 December 2016 and for the quarter concerning the dividend payout is at the level of minimum 175% for companies operating in section I and at least 150% for companies operating in section II.

By the date of preparing this Management Report of PZU Group, the Management Board had not adopted a resolution concerning distribution of profit for 2016.

By the date of preparing this Management Report of PZU, the Management Board had not adopted a resolution concerning distribution of profit for 2016.

7.9 PZU's share prices and capital market ratios

PZU shares were first traded on the Warsaw Stock Exchange on 12 May 2010. Since its IPO, the company has been included in the WIG20, WIG, WIG30, WIG-Poland, and WIGdiv indexes. Since 2012, PZU shares have been also included in the RESPECT sustainable development index (presence confirmed on 14 December 2016).

Stock split

On 30 November 2015, PZU split its shares, the operation consisting in decreasing the nominal value of shares from PLN 1 to PLN 0.1. The operation was purely technical (i.e. without any influence on share capital); following the split, the share price decreased 10 times and the number of shares increased 10 times. The main objective of the split was to make the PZU shares more accessible to individual investors as well as to diversify the shareholder structure.

WSE indexes

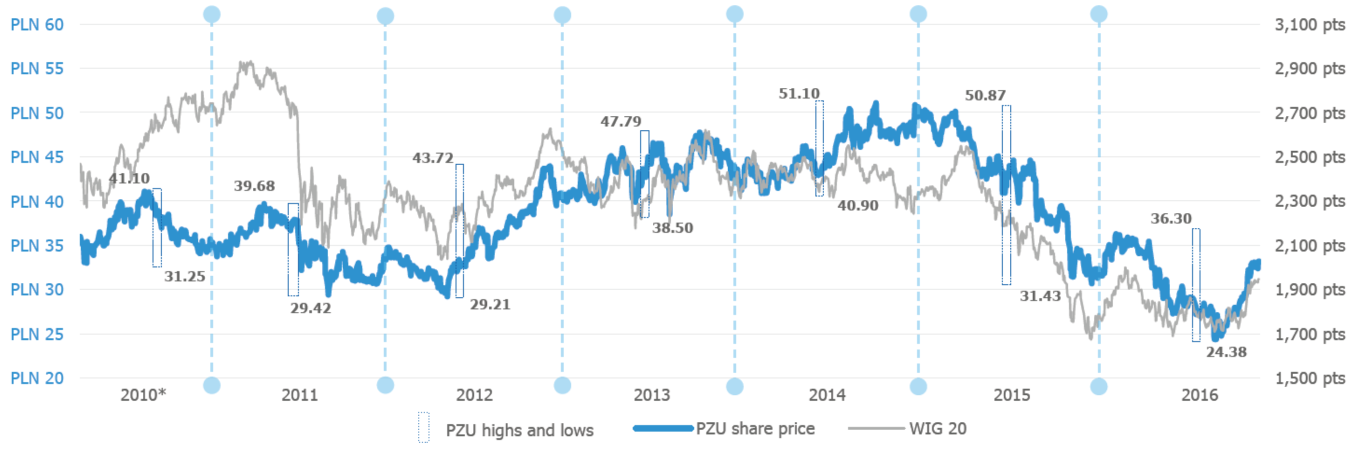
In 2016, the most important Polish index, WIG20, fluctuated in the range of 1,674–1,999 points, closing the final session of the year at a level close to the year's maximum, i.e. 1,947 points (up by 4.8% year-on-year). The broad WIG market index closed 2016 by recording 51,754 points, up by 11.4% year-on-year, thus confirming the greater strength of small and medium enterprises quoted on WSE (mWIG gained 18.2% year-on-year). The RESPECT Index also presented high dynamics and closed at 10.9% higher than in 201.

PZU share prices

In 2016, PZU shares continued to remain among the top most liquid companies on WSE. With capitalization amounting to PLN 28.7 billion, at the end of 2016 PZU was the sixth company with regard to capitalization of domestic companies. PZU's share in the trading of the whole exchange reached 8.9% (4th place).

In 2016, the maximum PZU share price (calculated at session end) amounted to PLN 36.30. The price reached its bottom soon after the dividend (PLN 2.08 per share) from 2015 profit was cut off from the share price on 30 September 2016. The price per share at the end of this session was PLN 24.38, a historical low from PZU's debut on the exchange.

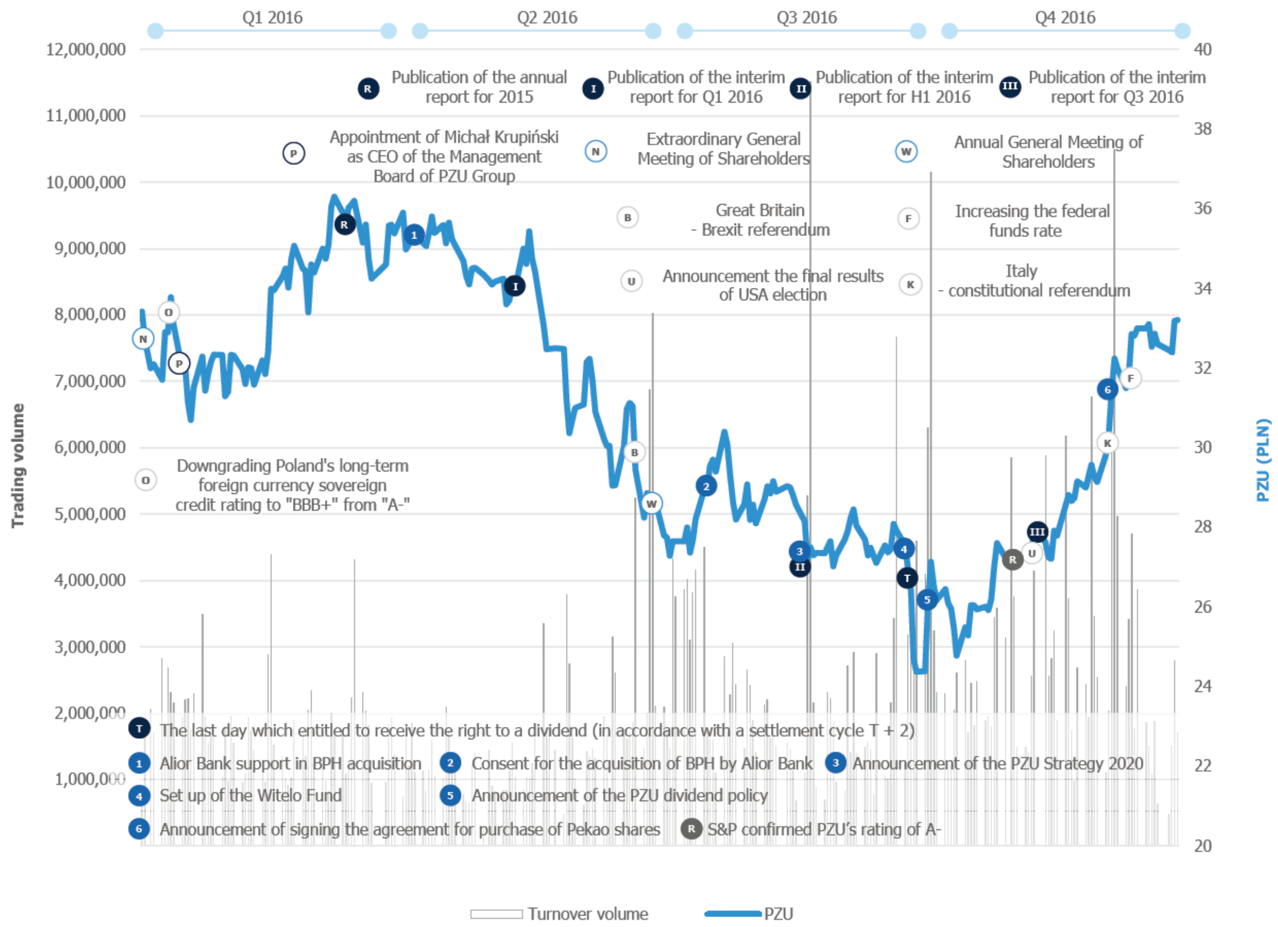
Min/max PZU share prices following the session end in the years 2010–2016



* Share prices from 12 May 2010 (PZU's IPO on WSE).

Source: Reuters

Factors influencing the exchange rate of PZU shares in 2016



Source: PZU

In the first half of 2015, WIG20 experienced a downward trend, which entailed a decline in the price of PZU. There was a strong attempt at reversing this trend, which took place no sooner than in the fourth quarter of 2016, which saw PZU grow by 36.2% quarter-on-quarter, i.e. considerably more than WIG20 and WIG, which rose appropriately by 13.9% and 9.9% quarter-on-quarter. Consequentially, the volatility of PZU share prices in all of 2016 (recognized as the quotient of the standard deviation from the period's average price) was 10.3%, only 68 bps lower than in 2015. In 2016, PZU's systematic risk expressed by the Beta coefficient (PZU price compared with WIG for daily changes) was 1.18 (1.07 in 2015). At the last session of 2016, WIG20 recorded growth of 4.8% year-on-year while PZU's shares were quoted at a similar level to that of the end of 2015, i.e. PLN 33.21 (-2.4% year-on-year).

The total shareholder return (TSR) in 2016 reached 3.7% (for comparison, its value at the end of 2015 was negative: -23.8%). The dividend rate (calculated in relation to the share price at the end of 2016, i.e.5 PLN 33.21) was 6.26% (PLN 2.08 of dividend per share), which is almost twice as high as the average for WIG20 and WIG Banks, which were at appropriately 2.8% and 3.1%[6].

In 2016, PZU's shares retained high liquidity. Average spread was only 9 pbs. (the average for the top 20 companies with the biggest trading value was 18 bps). The average number of transactions involving PZU shares per session was 4,169 (a 25.3% increase year-on-year). The highest trading volume, i.e. 11.5 million units, was recorded on 24 August 2016 (with 1.1% growth of the share price at the end of the session), i.e. on the day of announcement of the PZU Group Strategy for the years 2016–2020. For comparison purposes, the highest trading value in 2015 (at a single session) did not exceed 7.7 million share units. Also the announcement of the dividend policy (4 October 2016) was accompanied by strong emotions. On 4–5 October 2016, the total turnover reached 16.5 million shares and the price rose by 11.3% in total.

In 2016, investors discounted the uncertainty associated with PZU's potential involvement in the consolidation of assets of the banking sector in Poland and the possibility to further receive attractive dividends from PZU. The anxiety went down when PZU announced its dividend policy (4 October) SECTION 8.7 CAPITAL AND DIVIDEND POLICY and its purchase of a share package of Bank Pekao S.A. (8 December). The PZU Management Board declared that it wanted to continue to provide its shareholders with an attractive stream of rising dividends and that it had no plans for changes in Bank Pekao, neither in the Management Board nor in the Bank's dividend policy and strategy. After the exchange session on 8 December, the value of PZU grew by PLN 716.7 million (growth of share prices by 2.6%) at a high trading volume of 10.5 million shares.

Quick Response (QR) codes for video transmission

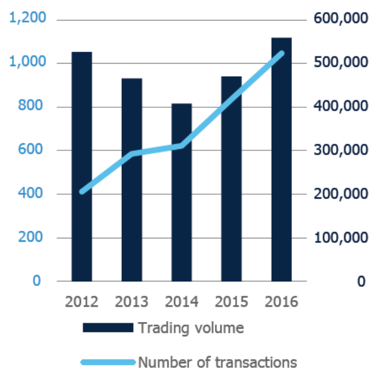
W Zwyczajne Walne Zgromadzenie Akcjonariuszy	3 Ogłoszenie strategii PZU na lata 2016 – 2020	5 Ogłoszenie polityki dywidendowej PZU	6 Ogłoszenie podpisania umowy nabycia pakietu akcji Pekao

Ratios

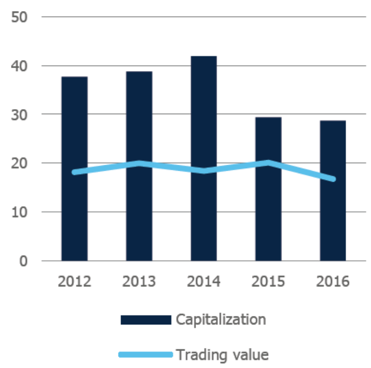
As at the end of 2016, the capitalization of WSE companies rose by 7.8% year-on-year to PLN 557 billion (including 19 new entities that were first traded on WSE in 2016). The P/E GLOSSARY ratio for the banking industry (the most adequate comparison for PZU on WSE) was 11.7 while the P/BV GLOSSARY was 0.76[4]. PZU's P/E GLOSSARY ratio was 12.5 and its P/BV GLOSSARY was 2.27.

[5] Statistic bulletin of GPW 2016
[6] http://www.gpw.pl/analizy_i_statystyki6

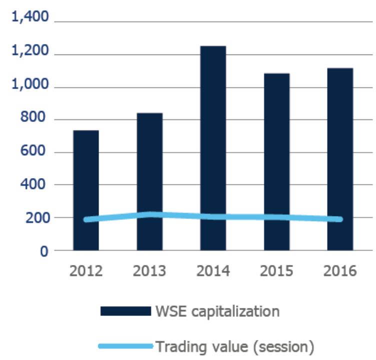
PZU trading volume / number of transactions



PZU capitalization/ trading value



WSE capitalization / trading value



PZU share statistics	2016	2015	2014	2013	2012
Maximum rate of shares (PLN)	36.30	50.87	51.10	47.79	43.72
Minimum rate of shares (PLN)	24.38	31.43	40.90	38.50	29.21
Exchange rate at the last session of the year (PLN)	33.21	34.02	48.60	44.90	43.70
Average rate per session (PLN)	30.76	43.72	45.22	43.22	34.61
Alue of volume (PLN million)	16,754.98	20,144.56	18,400.72	19,970.38	18,152.22
Average value of the volume per session (PLN milion)	66.8	80.3	73.9	80.9	73.2
Number of transactions (item)	1,046,398	835,471	621,224	585,205	411,635
Average numer of transactions per session	4,169	3,329	2,495	2,369	1,660
Trading volume	558,496,883.0	470,048,842.0	407,247,220.0	464,899,980.0	525,648,380.0
Average trading volume per session (item)	2,225,086.9	1,872,704.5	1,635,531.0	1,882,186.2	2,119,549.9
Capitalization at the end of the period (PLNmillion)	28,677.6	29,377.1	41,967.2	38,767.9	37,736.0

Capital market ratios for PZU shares*	2016	2015	2014	2013	2012
P/BV Market price per share / book value per share	2.20	2.27	3.19	2.95	2.64
BVPS Book value per share	15.07	14.97	15.25	15.20	16.52
P/E Price per share / profit per share	14.73	12.54	14.14	11.77	11.60
EPS (PLN) Net profits (losses) of owners / numer of shares	2.25	2.71	3.44	3.82	3.77

* calculation based on PZU Group's data (according to IFRS)

08

8 Corporate governance

Contents:

8.1 Corporate governance principles applied by PZU

Since the IPO of PZU on a regulated market, the Issuer has followed the corporate governance principles laid down in Good Practices of Companies quoted on WSE.

The document was accepted by WSE Council on 4 July 2007 and has undergone several modifications since then. The document accepted by the Resolution of WSE Council regarding amendments to the Good Practices of Companies Quoted on WSE of 21 November 2012 was effective between 1 January 2013 and 31 December 2015.

On 13 October 2015, a new set of corporate governance rules under the name of "Good Practices of Companies quoted on WSE 2016" was accepted by the resolution of WSE Council. The new rules are in force as at 1 January 2016.

The current contents are available on the website devoted to corporate governance of WSE-quoted entities www.corp-gov.gpw.pl and on the PZU's corporate website www.pzu.pl in the section dedicated to PZU's shareholders – "Investor Relations".

Code of Good Insurance Practices adopted on 8 June 2009 by the General Meeting of the Polish Chamber of Insurance ("PIU"), an organization associating insurance companies operating in the Polish market is another document determining the manner of business operations and of developing relations with stakeholders. The document is available on the website: piu.org.pl.

Furthermore, stakeholder relations are based on our internal PZU Code of Good Practices. The document is available on the website: www.pzu.pl.

On 22 July 2014, Polish Financial Supervision Authority issued Corporate Governance Rules for Supervised Institutions ("Rules").

The rules are a set of guidelines, which should be used by supervised entities from 1 January 2015 under the applicable law and with respect to the principle of proportionality.

The rules and information on how to use them can be found on the PZU website: http://www.pzu.pl/grupa-pzu/pzusa/zasady-ladu-korporacyjnego.

8.2 Application of Good Practices of Companies Quoted on WSE

In 2016, PZU followed the recommendations and regulations expressed in the Good Practices of Companies quoted on WSE, except for recommendation IV.R.2 which refers to enabling the shareholders to participate in general shareholders' meeting using electronic means of communication, especially by:

- real-time broadcast of the general shareholders' meeting,
- mutual real-time communication which allows shareholders to speak at the general shareholders' meeting, while physically being in a different location than the place where the meeting is held,
- exercising, in person or via proxy, voting right at the general shareholders' meeting.

At the moment, the PZU shareholder can watch a broadcast of the general shareholders' meeting. The company, however, has not made a decision to introduce the so-called e-GSM. PZU believes that there is a number of technical and legal factors which may obstruct the proper course of general shareholders' meeting. The legal concerns refer to the possibility of identification of shareholders and checking relevant documents of GSM participants. The risk related to technical problems, such as the Internet connection or a potential external interference with IT systems, may disturb the operations of the general shareholders' meeting and raise doubts as to the effectiveness of resolutions adopted in the course of such a meeting. If such risks materialize, this may impact proper application of the relevant principle as a whole.

Moreover, the following rules do not apply to PZU:

- rule I.Z.1.10 that refers to presenting on PZU's corporate website financial forecasts – provided that the company has decided to publish them – published at least over the last 5 years, along with the information on the degree of their materialization, because as at these financial statements PZU was not publishing financial forecasts and estimations;

- rule III.Z.6 that refers to non-distinguishing of an internal auditing function in a company's organization, because such a function was distinguished in PZU organization;
- recommendation IV.R.3 that refers to a situation where securities issued by a company are traded in several different countries (or on several markets) and in different legal systems, because PZU securities are traded exclusively on the Polish market.

Information on the PZU' s application of recommendations and rules included in Good Practices of Companies quoted on WSE 2016 was published by the Company on 24 March 2016.

8.3 Application of Corporate Governance Principles to Supervised institutions

The Management Board and the Supervisory Board of PZU declared their readiness to apply the Principles to the furthest objectively possible extent, taking into account the principle of proportionality and the *"comply or explain"* rule, arising from their content. These statements of the Management Board and the Supervisory Board of PZU were confirmed by their appropriate resolutions.

The Management Board and the Supervisory Board of PZU announced the decision on implementing the Principles during the General Shareholders' Meeting that took place on 30 June 2015. The General Shareholders' Meeting of PZU declared that while acting within its mandate it will follow the Corporate Governance Rules in the wording of Polish Financial Supervision Authority of 22 July 2014 with the exception of the rules that the General Shareholders' Meeting of PZU decided to waive.

Detailed information about the application of the Principles by PZU can be found on PZU's website. That includes the principles whose application is partial, that is:

- principle specified in § 8. 4. Principles facilitating the participation of all shareholders in the General Shareholders' Meeting, e.g. by ensuring the active electronic participation in meetings; it should be emphasized that the current shareholders of PZU can follow the broadcast of the meeting, but the Company decided not to introduce the so-called e-GSM; in the assessment of PZU, there are many technical and legal factors that could affect the proper conduct of the General Shareholders' Meeting. The legal concerns are related to the possibility of identifying shareholders and inspecting the ID cards of the GSM's participants; the risk of technical problems, e.g. with the Internet connection or a potential intrusion into information systems, can disrupt the work of the General Shareholders' Meeting and raise doubts about the effectiveness of the resolutions adopted during the meeting; the occurrence of the above-mentioned risks may affect the correct application of the principle in full;
- principle specified in § 21. 2. Principles which state that in the composition of the supervisory body there should be a separate function of a chairperson who manages the works of the supervisory body and that the choice of the chairperson of the supervisory body should be made based on the experience and team leadership skills, taking into account the criterion of independence; it must be emphasized that, in accordance with the Code of Commercial Companies and the By-laws of PZU, there is a separate function of a chairperson in the Supervisory Board of PZU; the composition of the Supervisory Board of PZU, including the office of the chairperson, are shaped according to the criterion of independence set out in the Act on Statutory Auditors; the election of the chairperson of the Supervisory Board is made on the basis of their knowledge, experience and skills, which confirm that the chosen person has the competencies necessary for the proper performance of their supervising duties; the application of the criterion of independence in the case of the chairperson in accordance with the PFSA's explanation of the

principle may raise doubts about the potential conflicts of law relating to shareholders' rights;

- principle specified in § 49. 3 of the Principles concerning appointment and dismissal in supervised institutions of the person heading the internal audit unit or the person heading the compliance unit, it should be noted that PZU complies with the principles specified in § 14 of the Principles fully, which means that PZU's Management Board is the only one entitled to and responsible for management of the operations of the company; furthermore, in accordance with the provisions of the labor law, the activities related to the labor law are performed by the governing body; in view of the above, PZU adopted a solution according to which the decision about appointment and dismissal of the person heading the internal audit unit is made, taking into account the opinion of the Audit Committee of the Supervisory Board; the same applies to the appointment and dismissal of the person heading the compliance unit; the Management Board consults the Audit Committee about such decisions.

The General Shareholders' Meeting of PZU decided against implementing the following principles:

- rule specified in § 10. 2 in the following wording: "Introduction of personal entitlements or other special entitlements for shareholders of a supervised institution should be justified and serve realization of the objectives of this supervised institution. Having such entitlements by shareholders should be reflected in a basic act regulating operation of the institution."

  – waiver from applying the principle is justified by the unfinished privatization of the Company carried out by the State Treasury;

- rule specified in § 12. 1 in the following wording: "The shareholders are responsible for providing immediate capital injection to the supervised institution in a situation in which it is necessary for maintaining the own capitals of the supervised institution on a level required by the legal or supervisory regulations and also when it is required for the reasons concerning safety of the supervised institution."

  – waiver from applying the principle is justified by the unfinished privatization of the Company carried out by the State Treasury;

- rule specified in § 28. 4 in the following wording: "A decision-making authority shall assess whether the agreed remuneration policy is beneficial to the development and safety of the supervised institution."

  – waiver from applying the principle is justified by the scope of application of the remuneration policy assessed by the decision-making authority being too broad. The remuneration policy for persons performing key functions and not being the members of the supervisory body or governing body should be assessed by their employer or principal, which is the Company represented by the Management Board and controlled by the Supervisory Board.

Moreover, the following rules do not apply to PZU:

- rule specified in § 11. 3 in the following wording: "In the event that the decision concerning a transaction with a related party was made by the General Shareholders' Meeting, all shareholders should have access to any information necessary for assessment of the terms on which the transaction is to be executed and its impact on the situation of the supervised institution."

  – in PZU the General Shareholders' Meeting does not make decisions concerning transactions with related parties;

- rule specified in § 49. 4 in the following wording: "In a supervised institution, where there is no internal audit unit or compliance unit, the entitlements referred to in items 1–3 shall be held by the people responsible for performance of those functions."

  – there is both an internal audit unit and a compliance unit at PZU;

- rule specified in § 52. 2 in the following wording: "In a supervised institution, where there is no audit unit or compliance assurance unit, and where no unit responsible for that area has been appointed, the information referred to in item 1 shall be submitted by the people responsible for fulfilling those functions."

  – there is both an internal audit unit and a compliance unit at PZU;

- the rules specified in Chapter 9 – Execution of Rights Resulting from Assets Acquired at Client's Risk, as PZU offers no products which involve managing assets at client's risk.

8.4 Control system applied during preparation of the financial statements

Financial statements are prepared within the PZU Finance Division including PZU Head Office (with the Accounting Office) and central units operating based on applicable regulations. PZU Finance Division is supervised by a Member of the Management Board of PZU.

The elements which facilitate completing the process are the accounting principles (policy), the chart of accounts with a commentary and other detailed internal regulations approved by the Management Board of PZU specifying the key rules of recording business events in PZU and dedicated reporting systems.

Data is prepared in the source systems using formal operating and acceptance procedures which specify the competencies of individual persons.

The reporting process is controlled by appropriately qualified, skilled and experienced staff.

PZU monitors the changes in the external regulations concerning e.g. the accounting policy (procedures) and reporting requirements of insurance undertakings and carries out appropriate adaptation processes.

The accounting records are closed and financial statements are prepared in accordance with detailed schedules, including the key activities and control points with assigned liability for timely and correct completion.

The key controls during preparation of the financial statements include:

- controls and permanent monitoring of the quality of input data, supported by the financial systems with defined rules of data correctness, in accordance with the PZU internal regulations concerning the control of correctness of the accounting data;
- data mapping from the source systems to financial statements supporting appropriate presentation of data;
- analytical review of financial statements by specialists to compare them with the business knowledge and business transactions;
- formal review of the financial statements to confirm compliance with the valid legal regulations and market practice in terms of required disclosures.

PZU internal audit periodically reviews the organization and the process of preparing the financial statements.

Activities within the consolidated financial reporting are coordinated through the organizational structure of the Finance Division in the PZU and PZU Życie Head Offices, which is shared, i.e. organized based on a personal union. PZU controls all the consolidated subsidiaries through Management Boards and Supervisory Boards of the companies.

The process of consolidated financial reporting is regulated by a number of internal acts. The acts regulate the accounting principles (policy) adopted by PZU Group and applied accounting standards.

Additionally, the process is also subject to detailed schedules including the key activities and control points with assigned liability for timely and correct completion.

Audit Committee

The Supervisory Board of PZU appoints three members of the Audit Committee. At least one of them must be an Independent Member and at least one must be qualified in accounting or auditing, as understood by the Act on Statutory Auditors and Their Self-Governing Body, Auditing Firms and on Public Oversight. The Audit Committee is an advisory and consultative body to the Supervisory Board and is appointed to improve the effectiveness of the supervision of the correctness of financial reporting, effectiveness of internal control, including internal audit and risk management, exercised by the Supervisory Board.

A statutory auditor appointed by the Supervisory Board of PZU based on the recommendation of the Audit Committee reviews interim separate and consolidated financial statements of PZU and audits its annual separate and consolidated financial statements.

8.5 Entity authorized to audit financial statements

On 18 February 2014, the Supervisory Board of PZU appointed KPMG Audyt Sp. z ograniczoną odpowiedzialnością. sp. k., with its registered office in Warsaw, ul. Inflancka 4A, 00-189 Warsaw, entered on the list of entities authorized to audit financial statements under No. 3546 by the National Chamber of Statutory Auditors as the entity authorized to audit financial statements.

The scope of the agreement includes in particular:

- audit of annual separate financial statements of PZU and of annual consolidated financial statements of PZU Group;
- review of interim separate financial statements of PZU and of interim consolidated financial statements of PZU Group.

The work referred to above includes three subsequent financial years ending, respectively, on: 31 December 2014, 31 December 2015, and 31 December 2016, with an option to extend the agreement for further two financial years ending, respectively, on 31 December 2017 and 31 December 2018.

Remuneration of the entity authorized to audit financial statements	1 January – 31 December 2016	1 January – 31 December 2015
Statutory audit of annual separate	1 365	1 488
Other attestation services	1 350	248
Tax advisory services	-	-
Other services	27	27
Razem	**2 742**	**1 763**

8.6 Share capital and shareholders of PZU; stock held by members of its authorities

On 30 June 2015, the General Shareholders' Meeting of PZU adopted the resolution on splitting all shares of PZU by decreasing the nominal value of each PZU share from PLN 1 to PLN 0.1 and increasing the number of PZU shares which constitute the share capital from 86,352,300 to 863,523,000. The split of shares was performed through the exchange of all shares in 1:9 ratio. The split of shares had no influence on the share capital of PZU.

On 3 November 2015, the District Court for the capital city of Warsaw, XII Economic Division of the National Court Register recorded the appropriate change to the By-laws of PZU.

On 24 November 2015, the Management Board of the National Depository for Securities adopted at the request of PZU a resolution No. 789/15 on determining the day of 30 November 2015 as the day of splitting 86,348,289 PZU shares with the face value of PLN 1 each to 863,482,890 PZU shares with the face value of PLN 0.10 each.

Therefore, the share capital of PZU is divided into 863,523,000 ordinary shares with the face value of PLN 0.10 each, giving right to 863,523,000 votes on the General Shareholders’ Meeting.

On 27 April 2016, a notice from the Ministry of Treasury was delivered to PZU that informed about a decrease in State Treasury’s share in the total number of votes and share capital of PZU. As per the above notice, that share amounted to 34.19% as at 31 March 2016.

As per the current report no. 17/2017, at the PZU Ordinary Shareholders' Meeting that was opened on 18 January 2017 and continued on 8 February 2017, the following shareholders held the majority share packages: State Treasury that held 295,217,300 of shares, which constituted 34.19% of PZU share capital and translated into 295,217,300 votes at General Shareholders' Meeting, and Aviva Otwarty Fundusz Emerytalny Aviva BZ WBK that held 43 176 660 of shares, which constituted 5.13% of PZU share capital and translated into 44,260,000 votes at General Shareholders' Meeting.

The Management Board of the Company has no knowledge about concluded agreements which may result in changes in the proportion of shares held by the shareholders.

PZU did not issue, redeem, or repay any debt or equity instruments that would provide its shareholders with special control rights.

From 2013 to 2016, no employee stock ownership plans existed in PZU.

In line with the By-laws of PZU, the voting right of the shareholders is restricted in a way that none of them can exercise more than 10% of the total number of votes at PZU at the date of the General Shareholders' Meeting, with the reservation that for the purpose of determining obligations of parties acquiring material blocks of shares provided for in the Act on Public Offering and the Act on Insurance Activity, such voting restrictions are considered non-existent. The voting right restriction does not apply to:

- shareholders who held shares entitling to more than 10% of the total number of votes in the Company as at the date of adopting a resolution of the General Shareholders Meeting;
- shareholders co-acting with shareholders defined in the point above based on agreements concerning joint voting rights attached to the shares.

For the purposes of voting rights restrictions, the votes of the shareholders being parent companies or subsidiaries will be added up in line with the principles specified in the By-laws.

In case of any interpretation doubts with respect to the voting restrictions, Article 65.2 of the Civil Code will apply **GLOSSARY**.

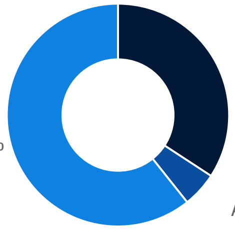
In line with the By-laws of PZU, the above voting restrictions will expire when a share of a shareholder who, at the date of adopting a resolution of the shareholders' meeting introducing the restriction, held shares entitling him to more than 10% in the total number of votes in the Company, drops below 5% of the share capital.

Votes from shares of PZU are not restricted.

Shares or rights to shares of PZU's managers and supervisors, as well as PZU Group Directors.

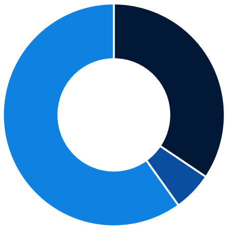
Both as the date of this Management's Report and as at the date of submitting the Management's Report for 2015 (i.e. 15 March 2016), none of the members of the Management Board, Supervisory Board or Directors of PZU Group held PZU shares or rights to shares.

PZU shareholding structure as at 31 December 2016



Source: current report no. 17/2017

PZU shareholding structure as at 31 December 2015



Source: current report no. 3/2016

8.7 By-laws of PZU

Amendments to the By-laws

The By-laws of PZU can be amended by the General Shareholders' Meeting in the form of a resolution passed by a majority of three fourths of votes. In cases specified in the Act on Insurance Activity such change must be approved by the PFSA **GLOSSARY** and then recorded in the National Court Register **GLOSSARY**. The Supervisory Board can approve the unified amended text of the By-laws.

8.8 General Shareholders' Meeting, Supervisory Board, and Management Board

General Shareholders' Meeting

The General Shareholders' Meeting is the highest body of PZU. The general operational principles and the rights of the General Shareholders' Meeting have been determined by the Code of Commercial Companies and the By-laws.

The By-laws are available on PZU's corporate website (www.pzu.pl) in the "Investors relations" section, tab: "Company".

The General Shareholders' Meeting did not issue its Regulations.

The General Shareholders' Meeting is a body authorized to make decisions concerning issues related to the organization and operations of the issuer. Resolutions of the General Shareholders' Meeting are adopted by an absolute majority of votes, except for cases specified in the Code of Commercial Companies or the By-laws.

The competencies of the General Shareholders' Meeting, in addition to those specified in the Commercial Companies Code **GLOSSARY** and the By-laws of PZU, include passing resolutions concerning the following:

- examination and approval of the Management Board report on the issuer's activities, financial statements for the previous financial year and acknowledgement of the fulfillment of duties by members of the company's authorities;
- profit distribution or loss coverage;
- making decisions concerning claims for redressing damage inflicted upon formation of the company or exercising management or supervision;
- disposal of the enterprise or its organized part or its lease or establishment of a limited property right;
- redemption of shares or issue of bonds;
- creating reserve capitals and making the decision whether to use them and if so, how;
- division of the Company, its merger with another company, its liquidation or dissolution;
- appointing and dismissing members of the Supervisory Board, subject to the right granted to the State Treasury to appoint and dismiss one member of the Supervisory Board;
- establishing the rules of remunerating members of the Supervisory Board;
- acquisition or disposal by the issuer of real property, perpetual usufruct or share in real property or in perpetual usufruct with a value exceeding the equivalent of a gross amount of EUR 30.0 million (thirty million euro).

In accordance with the By-laws, a majority of three fourths of votes is required to pass the General Shareholders' Meeting's resolutions on the following:

- amendments in the By-laws;
- a decrease in the share capital;
- disposal of the enterprise or its organized part or its lease or establishment of a limited property right.

A majority of 90% of votes at the General Shareholders' Meeting is required to pass resolutions relating to the following:

- preference shares;
- Issuer's business combination by transferring all its assets to another company;
- its merger by forming a new company;
- dissolving the Company (also as a result of moving its seat or the head office abroad);
- its liquidation, transformation or reduction in the share capital through redemption of a portion of shares without a similar capital increase.

The General Shareholders' Meeting is held:

- as an Ordinary General Shareholders' Meeting which should be held within six months from the end of each financial year;
- as an Extraordinary General Shareholders' Meeting which is convened in cases specified in the generally applicable law and the By-laws.

The General Shareholders' Meetings are held in Warsaw and convened by placing an appropriate announcement on PZU's website in accordance with the method for providing current information specified in the Act on Public Offering, Conditions Governing the Introduction of Financial Instruments to Organized Trading, and Public Companies of 19 July 2005, i.e. in the form of current reports. Such announcement should be made no later than 26 days before the date of the General Shareholders' Meeting. From the date of convening the General Shareholders' Meeting the announcement with materials presented to shareholders at the General Shareholders' Meeting are available on PZU's corporate website (www.pzu.pl) in section "Investors relations", tab "General Shareholders' Meeting". A duly called General Shareholders' Meeting is deemed valid regardless of the number of attending shareholders or number of represented shares. Ballots are open.
The secret ballot vote is used when appointing and dismissing members of the Issuer's bodies or liquidators, in cases of their personal responsibility towards the issuer and in personal cases, except when an open ballot method is required by the applicable law, upon request of any shareholder present or represented at the General Shareholders' Meeting. The rights of the shareholders and the method of exercising thereof at the General Shareholders' Meeting are specified in the Code of Commercial Companies **SŁOWNIK** and the By-laws. Only persons who were shareholders of the issuer 16 days before the date of the General Shareholders' Meeting have the right to participate in the Meeting (date of registration of attendance at the Meeting). Shareholders may attend the General Shareholders' Meeting and exercise the right to vote personally or through a proxy. The power of attorney to participate in the General Shareholders' Meeting and to exercise the voting right may be granted in writing or in an electronic form. One share of PZU gives the right to a single vote at the General Shareholders' Meeting, including restrictions with respect to exercising the voting rights described in the Company's By-laws. The shareholder has the right to vote in a different manner under each share held.

During the General Shareholders' Meeting each shareholder may provide resolution drafts concerning items on the agenda.

In accordance with the Code of Commercial Companies, detailed procedures concerning participation in the General Shareholders' Meeting and exercising the voting rights are always presented in an announcement of the General Shareholders' Meeting published on the date of convening the Shareholders' Meeting on PZU's corporate website (WWW.PZU.PL), section "Investors relations", tab "General Shareholders' Meeting".

Composition, powers and functioning of the Supervisory Board

Composition

The Supervisory Board (SVB) is composed of seven to eleven members. The number of members is specified at the General Shareholders' Meeting.

Members of the SVB are appointed by the General Shareholders' Meeting for a shared term which includes three consecutive full financial years.

At least one member of the SVB must be qualified in accounting or auditing, as understood by the Act on Statutory Auditors and Their Self-Governing Body, Auditing Firms and on Public Oversight. Furthermore, at least one member of the SVB should meet the independence criteria specified in the By-laws (Independent Member) concerning e.g. professional and personal relations, especially with members managing or supervising PZU and entities in PZU Group. The Independent Member has to present a written statement that all independence criteria provided for in the By-laws have been met and inform the Company when the criteria are no longer met. In addition, the By-laws give the State Treasury the right to appoint and dismiss one member of the SVB by way of a written statement submitted to the Management Board. The right will expire once the State Treasury ceases to be the Company's shareholder.

Composition of the SVB of PZU as at 1 January 2016:

- Zbigniew Ćwiąkalski - Chairman of the Board;
- Paweł Kaczmarek – Deputy Chairman of the Board;
- Dariusz Filar -Secretary of the Board;
- Zbigniew Derdziuk – Member of the Board;
- Dariusz Kacprzyk – Member of the Board;
- Jakub Karnowski – Member of the Board;
- Aleksandra Magaczewska – Member of the Board;
- Alojzy Nowak – Member of the Board;
- Maciej Piotrowski – Member of the Board.

The criteria of an Independent Member of the SVB were met by Dariusz Kacprzyk and Dariusz Filar.

On 7 January 2016, the Extraordinary General Shareholders' Meeting of PZU dismissed the following people from the SVB of the Company, with effect on 7 January 2016: Zbigniew Ćwiąkalski, Zbigniew Derdziuk, Maciej Piotrowski, Dariusz Kacprzyk, Jakub Karnowski, Aleksandra Magaczewska, Dariusz Filar.

Simultaneously, on 7 January 2016, it appointed the following people to the SVB of PZU: Piotr Paszko, Marcin Chludziński, Marcin Gargas, Maciej Zaborowski, Eligiusz Krześniak, Radosław Potrzeszcz and Jerzy Paluchniak.

On 19 January 2016, Paweł Kaczmarek was appointed Chairman of the SVB, Marcin Gargas – Deputy Chairman, and Maciej Zaborowski – Secretary of the Board.

Therefore, since 19 January 2016, composition of the SVB of PZU was as follows:

- Paweł Kaczmarek – Chairman of the Board;
- Marcin Gargas – Deputy Chairman of the Board;
- Maciej Zaborowski – Secretary of the Board;
- Marcin Chludziński – Member of the Board;
- Eligiusz Krześniak – Member of the Board;
- Alojzy Nowak – Member of the Board;
- Jerzy Paluchniak – Member of the Board;
- Piotr Paszko – Member of the Board;
- Radosław Potrzeszcz – Member of the Board.

Marcin Gargas, Maciej Zaborowski, Marcin Chludziński, Eligiusz Krześniak, Alojzy Nowak, Piotr Paszko and Radosław Potrzeszcz fulfilled the criteria of Independent Members of the SVB.

On 1 July 2016, Jerzy Paluchniak resigned from his membership in the PZU SVB as at 1 July 2016. On 1 July 2016, the General Shareholders' Meeting of PZU appointed Piotr Walkowiak as a Member of the SVB, effective as of 2 July 2016.

Therefore, since 2 July 2016, composition of the SVB of PZU was as follows:

- Paweł Kaczmarek – Chairman of the Board;
- Marcin Gargas – Deputy Chairman of the Board;
- Maciej Zaborowski – Secretary of the Board;
- Marcin Chludziński – Member of the Board;

- Eligiusz Krześniak – Member of the Board;
- Alojzy Nowak – Member of the Board;
- Piotr Paszko – Member of the Board;
- Radosław Potrzeszcz – Member of the Board.
- Piotr Walkowiak – Member of the Board.

On 7 July 2016, acting under § 20 section 7 of PZU's By-laws, the Minister of Treasury of the Republic of Poland appointed Jerzy Paluchniak as a Member of the SVB of PZU, and therefore the composition of the Board was as follows:

- Paweł Kaczmarek – Chairman of the Board;
- Marcin Gargas – Deputy Chairman of the Board;
- Maciej Zaborowski – Secretary of the Board;
- Marcin Chludziński – Member of the Board;
- Eligiusz Krześniak – Member of the Board;
- Alojzy Nowak – Member of the Board;
- Jerzy Paluchniak – Member of the Board;
- Piotr Paszko – Member of the Board;
- Radosław Potrzeszcz - Member of the Board;
- Piotr Walkowiak – Member of the Board.

On 4 August 2016, Piotr Walkowiak resigned from his membership in the PZU SVB as at 4 August 2016. Therefore, since 5 August 2016, composition of the SVB of PZU was as follows:

- Paweł Kaczmarek – Chairman of the Board;
- Marcin Gargas – Deputy Chairman of the Board;
- Maciej Zaborowski – Secretary of the Board;
- Marcin Chludziński – Member of the Board;
- Eligiusz Krześniak – Member of the Board;
- Alojzy Nowak – Member of the Board;
- Jerzy Paluchniak – Member of the Board;
- Piotr Paszko- Member of the Board;
- Radosław Potrzeszcz - Member of the Board.

The current term of office of the SVB of PZU started on 1 July 2015 and will end after the lapse of three financial years. 2016 was the first financial year of the company. The mandates of members of the SVB expire not later than on the date of the General Shareholders' Meeting approving the financial statements for the last full financial year of their term.

On 8 February 2017, Eligiusz Krześniak resigned from his membership in the SVB with immediate effect.

On 8 February 2017, the Extraordinary Shareholders' Meeting of PZU dismissed from the SVB of the Company the following members: Marcin Gargas, Piotr Paszko and Radosław Potrzeszcz.

Simultaneously, on 8 February 2017, it appointed the following people to the SVB of PZU: Agata Górnicka, Łukasz Świerżewski, Paweł Górecki, Bogusław Banaszak.

Therefore, from 8 February 2017 to the date of signing the separate financial statements, the composition of the SVB of PZU was as follows:

- Paweł Kaczmarek – Chairman of the Board;
- Maciej Zaborowski - Secretary of the Board;
- Bogusław Banaszak – Member of the Board;
- Marcin Chludziński – Member of the Board;
- Paweł Górecki – Member of the Board;
- Agata Górnicka – Member of the Board;
- Alojzy Nowak – Member of the Board;
- Jerzy Paluchniak – Member of the Board;
- Łukasz Świerżewski – Member of the Board.

As at 14 March 2017, from 14 March 2017, Paweł Górecki was appointed to the function of the Chairman of the SVB of PZU, Łukasz Świerżewski the Vice-Chairman and Alojzy Nowak the Secretary.

- Paweł Górecki - Chairman of the Board;
- Łukasz Świerżewski - Vice-Chairman of the Board;
- Alojzy Nowak - Secretary of the Board;
- Bogusław Banaszak - Member of the Board;
- Marcin Chludziński - Member of the Board;
- Agata Górnicka - Member of the Board;
- Paweł Kaczmarek - Member of the Board;
- Jerzy Paluchniak - Member of the Board;
- Maciej Zaborowski - Member of the Board.

Competencies

The SVB exercises constant supervision over the Company's activities in all aspects of its business. In accordance with the By-laws, the powers of the SVB include:

- a review of the Management Board's report on the activities of the Company and financial statements for the previous financial year in terms of their compliance with the accounting records, documents and facts;
- review of the motions of the Management Board concerning profit distribution or loss coverage;
- presenting the General Shareholders' Meeting with a written report on the results of the review described above and submitting a brief annual assessment of the situation of the Company, including internal controls and key risk management and an annual report on the work of the SVB;
- concluding, terminating and amending the agreements with members of the Management Board and setting the terms and conditions of remuneration and the amount of remuneration;
- appointing, suspending and dismissing the Chairman of the Management Board, members of the Management Board or the entire Management Board, as well as making decision to stop the suspension;
- agreeing to transfer the entire or portion of the insurance portfolio;
- accepting motions of the Management Board concerning acquisition, assumption or disposal of shares in companies, as well as the Company's participation in other entities – the SVB may specify the amount, terms and conditions and the way in which the Management Board may carry out the activities without the acceptance of the SVB;
- delegating members of the SVB to temporarily perform the functions of members of the Management Board who have been dismissed, resigned or cannot perform their functions for other reasons;
- accepting instructions concerning votes being cast by the Company's representatives during the General Shareholders' Meeting of PZU Życie concerning: an increase and decrease in the share capital, bonds issue, disposal and lease of a PZU Życie enterprise or establishment of a usufruct right, division of PZU Życie combination of PZU Życie with a different company, liquidation or termination of PZU Życie;
- selection of the entity authorized to audit the financial statements which will audit the annual financial statements of the company;
- wording of the consolidated amended By-laws;
- approval of the long-term plans for the development of the company and annual financial plans drafted by the Management Board;
- approval of the regulations of the Management Board;
- examination and evaluation of issues submitted by the Management Board for discussion during the General Shareholders' Meeting.

Moreover, the SVB grants consent to:

- acquisition or disposal of a real property, perpetual usufruct or share in the real property or in perpetual usufruct exceeding the equivalent of EUR 3.0 million.
- conclusion of a material agreement by the Company and its related party, as understood by the Ordinance on current and periodic information, excluding standard agreements concluded by the Company on an arm's length basis as part of its operating activities;
- conclusion of the agreement by the issuer with the underwriter referred to in Article 433.3 of the Code of Commercial Companies;
- advance payment against expected dividend;
- creation and closing of regional and foreign branches.

Mode of operation

The SVB adopts the regulations of the SVB specifying its organization and the manner of performing activities. The regulations of the SVB were adopted by its Resolution of 24 February 2016 and specify its composition and the way in which its members are appointed, the tasks and the scope of its activities and the manner of calling the SVB and conducting debates.

The By-laws stipulate that the SVB should meet at least once every quarter. The SVB may delegate its members to fulfill specific supervising activities on their own and to this effect appoint temporary committees. The scope of responsibility of a delegated member of the SVB and the committee is specified in a resolution of the SVB.

Resolutions of the SVB are adopted by an absolute majority of votes. In the event of a voting tie, the Chairman of the SVB has the casting vote. The resolutions of the SVB may be adopted using means of direct distant communication and in a written form. Additionally, the By-laws stipulate that a vote may be cast in writing through another member of the SVB.

The resolutions of the SVB are adopted in an open ballot, except for resolutions concerning appointment of the chairman, Deputy Chairman and the Secretary of the SVB, delegation of members of the SVB to temporarily fill in for members of the Management Board and for resolutions with respect to appointing, suspending and dismissing the Chairman of the Management Board, members of the Management Board or the entire Management Board as well and taking decision to stop such suspension which are adopted in a secret ballot. Moreover, a secret ballot may be chosen on request of a member of the SVB.

The SVB appoints the Chairman and the Deputy Chairman of the SVB from its members and it may also select the Secretary of the SVB.

In accordance with the Regulations of the SVB, apart from appointing the audit committee and promotion and compensation Committee, provided for in the By-laws to properly perform its supervision, the SVB may appoint other permanent advisory and consultative committees whose competencies, composition and way of work is specified by regulations adopted by the SVB. The regulations of the SVB stipulate that the SVB and the appointed committees may use the services of experts and advisory companies.

Members of the Management Board, employees of the Company competent for the discussed issue selected by the Management Board and other persons invited by the SVB may take part in the meetings of the SVB; however, they cannot cast votes. In specific cases, the SVB of PZU may also invite members of the management board or a SVB of a different company in PZU Group. Moreover, members of the SVB, upon consent of the SVB, may select one advisor authorized to take part in the meetings of the SVB devoted to reports and financial statements, and give their advice, provided that such person respects confidentiality and signs a confidentiality statement.

At present, the following committees function as part of the SVB of PZU:

- Audit Committee;
- Promotion and Compensation Committee;
- Strategy Committee.

The By-laws provide for appointing an Audit Committee by the SVB. The Committee is composed of three members, including at least one independent member qualified in accounting or auditing. Detailed tasks and terms and conditions of appointing members of the Audit Committee and its functioning have been specified in a resolution of the SVB, which views relevant competencies and experience of the candidates for members of the Committee.

In accordance with the Regulations of the Audit Committee adopted by a resolution of the SVB, the Audit Committee is an advisory and consultative body to the SVB and is appointed to improve the effectiveness of the supervision of the correctness of financial reporting and of internal control, including internal audit and risk management, exercised by the SVB. Moreover, the Audit Committee may apply to the SVB for commissioning specific controls in the Company to be exercised by an internal or external entity.

The SVB appointed the Audit Committee on 3 June 2008. Composition of the Audit Committee as at 1 January 2016:

- Dariusz Filar – Chairman of the Committee;
- Dariusz Kacprzyk – Member of the Committee;
- Paweł Kaczmarek – Member of the Committee.

Dariusz Filar was indicated by the SVB as an independent member, having accounting and audit qualifications as defined in Article 86.4 of the Act on Statutory Auditors.

In relation to the changes in the composition of the SVB of PZU, on 19th January 2016 the SVB of PZU established the following composition of the Audit Committee:

- Marcin Chludziński – Chairman of the Committee;
- Paweł Kaczmarek – Member of the Committee;
- Jerzy Paluchniak – Member of the Committee.

Mr Jerzy Paluchniak was indicated by the SVB as a member with qualifications in accounting or auditing as understood by the Act on Statutory Auditors **GLOSSARY** art. 86 par. 4 and 5 since 19 January 2016. Furthermore, Mr Marcin Chludziński meet the criteria of independence by the Act on Statutory Auditors art. 86 par. 4 and 5 since 19 January till 18 March 2016.

On 18 March 2016, the PZU SVB changed the composition of the audit committee into the following:

- Piotr Paszko – Chairman the Committee;
- Marcin Chludziński – Member of the Committee;
- Jerzy Paluchniak – Member of the Committee.

On 22 July 2016, the PZU SVB changed the composition of the audit committee into the following:

- Piotr Paszko – Chairman the Committee;
- Marcin Chludziński – Member of the Committee;
- Jerzy Paluchniak – Member of the Committee.

As at 31 December 2016, the composition of the Committee did not change.

In relation to the changes in the composition of the SVB of PZU Group, on 23 February 2017 the SVB of PZU Group decided that the Audit Committee should consist of 3 people, while simultaneously establishing the following composition of the Committee:

- Bogusław Banaszak – Chairman of the Committee;
- Marcin Chludziński – Member of the Committee;
- Jerzy Paluchniak – Member of the Committee.

In accordance with the Regulations of the SVB, once the Company's shares are quoted on the regulated market, as understood by the Act on Trading in Financial Instruments of 29 July 2005, the SVB may appoint a Promotion and Compensation Committee.

In accordance with the By-laws, detailed responsibilities and the method of appointing members of the Promotion and Compensation Committee, the way it works and remuneration are specified in a resolution of the SVB. The Committee should include at least one independent member. If the SVB includes five members elected in a vote, the Promotion and Compensation Committee is not appointed and its tasks are carried out by the entire SVB.

According to the regulations of the Promotion and Compensation Committee adopted by a resolution of the SVB of 4 April 2013, it is an advisory and consultative body to the SVB and is to improve efficiency of the Board's supervisory activities related to establishing the management structure, including organizational issues, remuneration system, remuneration principles and selection of properly qualified staff.

The SVB decided that the promotion and compensation committee would be composed of five persons. Composition of the Promotion and Compensation Committee as at 1 January 2016:

- Zbigniew Ćwiąkalski – Chairman of the Committee;
- Zbigniew Derdziuk – Member of the Committee;
- Dariusz Filar – Member of the Committee;
- Paweł Kaczmarek – Member of the Committee;
- Maciej Piotrowski – Member of the Committee.

In relation to the changes in the composition of the SVB of PZU, on 19 January 2016 the SVB of PZU decided that the Promotion and Compensation Committee should consist of 4 people, while simultaneously establishing the following composition of the Committee:

- Radosław Potrzeszcz – Chairman of the Committee;
- Marcin Gargas – Member of the Committee;
- Paweł Kaczmarek – Member of the Committee;
- Piotr Paszko – Member of the Committee.

On 18 March 2016, the PZU SVB changed the composition of the Promotion and Compensation Committee into the following:

- Radosław Potrzeszcz – Chairman of the Committee;

- Marcin Gargas – Member of the Committee;
- Paweł Kaczmarek – Member of the Committee;
- Eligiusz Krześniak – Member of the Committee.

As at 31 December 2016, the composition of the Promotion and Compensation Committee did not change.

In relation to the changes in the composition of the SVB of PZU, on 23 February 2017 the SVB of PZU decided that the Promotion and Compensation Committee should consist of 3 people, while simultaneously establishing the following composition of the Committee:

- Agata Górnicka – Chairwoman of the Committee;
- Paweł Górecki – Member of the Committee;
- Paweł Kaczmarek – Member of the Committee.

The Committee is dissolved once five members of the SVB are elected in a vote cast in groups and its rights are then taken by the entire SVB.

According to the regulations of the Strategy Committee adopted by a resolution of the SVB of 4 April 2013, it is an advisory and consultative body to the SVB and is to improve efficiency of the Board's supervisory activities related to consulting of all strategic documents presented by the Management Board (in particular, the Company development strategy) and presenting the SVB with recommendations on planned investments that materially impact the Company's assets.

Composition of the Audit Committee as at 1 January 2016:

- Alojzy Nowak – Chairman of the Committee;
- Zbigniew Derdziuk – Member of the Committee;
- Jakub Karnowski – Member of the Committee;
- Aleksandra Magaczewska – Member of the Committee;
- Maciej Piotrowski – Member of the Committee.

In relation to the changes in the composition of the SVB of PZU, on 19 January 2016 the SVB of PZU decided that the Strategy Committee should consist of 6 people, while simultaneously establishing the following composition of the Committee:

- Alojzy Nowak – Chairman of the Committee;
- Marcin Chludziński – Member of the Committee;
- Marcin Gargas – Member of the Committee;
- Piotr Paszko – Member of the Committee;
- Radosław Potrzeszcz – Member of the Committee;
- Maciej Zaborowski – Member of the Committee.

As at 31 December 2016 the composition of the Committee did not change.

In relation to the changes in the composition of the SVB of PZU Group, on 23 February 2017 the SVB of PZU Group decided that the Strategy Committee should consist of 6 people, while simultaneously establishing the following composition of the Committee:

- Alojzy Nowak – Chairman of the Committee;
- Bogusław Banaszak – Member of the Committee;
- Marcin Chludziński – Member of the Committee;
- Agata Górnicka – Member of the Committee;
- Łukasz Świerżewski – Member of the Committee;
- Maciej Zaborowski – Member of the Committee.

Management Board

Composition

In accordance with the By-laws of PZU, the Management Board (MB) is composed of three to seven members appointed for a shared term which includes three consecutive full financial years.

Members of the MB, including the Chairman of the MB, are appointed and dismissed by the Supervisory Board. The CEO of the new term appointed before the end of the current term may apply to the Supervisory Board for appointing other members of the MB of the new term before the end of the current term.

Since 1 January 2016, composition of the MB was as follows:

- Dariusz Krzewina – acting as Chairman of the MB;
- Przemysław Dąbrowski - Member of the Board;
- Rafał Grodzicki – Member of the MB;
- Tomasz Tarkowski – Member of the MB.

On 19 January 2016, Rafał Grodzki and Tomasz Tarkowski resigned as of 19 January 2016, and the PZU

Supervisory Board appointed Michał Krupiński, Rogera Hodgkiss, Beata Kozłowska-Chyła, Robert Pietryszyna as Members of the MB as of 19 January 2016, and Paweł Surówka as a Member of the MB as of 20 January 2016.

Therefore, since 20 January 2016, composition of the MB has been as follows:

- Michał Krupiński – Chairman of the MB;
- Przemysław Dąbrowski – Member of the MB;
- Roger Hodgkiss – Member of the MB;
- Beata Kozłowska-Chyła – Member of the MB;
- Dariusz Krzewina – Member of the MB;
- Robert Pietryszyn – Member of the MB;
- Paweł Surówka – Member of the MB.

On 18 March 2016, Przemysław Dąbrowski resigned as of 18 March 2016. On 19 March 2016, Paweł Surówka resigned as of 19 March 2016. On 19 March 2016, the PZU Supervisory Board appointed Sebastian Klimek and Maciej Rapkiewicz as Members of the MB, effective as of 22 March 2016.

Therefore, since 22 March 2016, composition of the MB has been as follows:

- Michał Krupiński – Chairman of the MB;
- Roger Hodgkiss – Member of the MB;
- Sebastian Klimek – Member of the MB;
- Beata Kozłowska-Chyła – Member of the MB;
- Dariusz Krzewina – Member of the MB,
- Robert Pietryszyn – Member of the MB;
- Maciej Rapkiewicz – Member of the MB.

On 13 May 2016, Robert Pietryszyn resigned from his membership in the MB. Moreover, on 13 May 2016, the PZU Supervisory Board appointed Andrzej Jaworski as a Member of the MB, effective as of 14 May 2016.

Therefore, since 14 May 2016, composition of the MB has been as follows.

- Michał Krupiński – Chairman of the MB;
- Roger Hodgkiss – Member of the MB;
- Andrzej Jaworski – Member of the MB;
- Sebastian Klimek – Member of the MB;
- Beata Kozłowska-Chyła – Member of the MB;
- Dariusz Krzewina – Member of the MB;
- Maciej Rapkiewicz – Member of the MB.

On 23 June 2016, Dariusz Krzewina resigned from his membership in the MB, and therefore the composition of the MB was as follows:

- Michał Krupiński – Chairman of the MB;
- Roger Hodgkiss – Member of the MB;
- Andrzej Jaworski – Member of the MB;
- Sebastian Klimek – Member of the MB;
- Beata Kozłowska-Chyła – Member of the MB;
- Maciej Rapkiewicz – Member of the MB.

On 30 August 2016, Sebastian Klimek resigned from his membership in the MB, and therefore the composition of the MB was as follows:

- Michał Krupiński – Chairman of the MB;
- Roger Hodgkiss – Member of the MB;
- Andrzej Jaworski – Member of the MB;
- Beata Kozłowska-Chyła – Member of the MB;
- Maciej Rapkiewicz – Member of the MB.

As of 17 October 2016 Beata Kozłowska-Chyła resigned from her membership in the MB. On 14 October 2016, the Supervisory Board appointed Tomasz Kulik as a Member of the MB. Therefore, the composition of the MB was as follows:

- Michał Krupiński – Chairman of the MB;
- Roger Hodgkiss – Member of the MB;
- Andrzej Jaworski – Member of the MB;
- Tomasz Kulik – Member of the MB;
- Maciej Rapkiewicz – Member of the MB.

As at 31 December 2016, composition of the MB was as follows:

- Michał Krupiński – Chairman of the MB;
- Roger Hodgkiss – Member of the MB;
- Andrzej Jaworski – Member of the MB;
- Tomasz Kulik – Member of the MB;
- Maciej Rapkiewicz – Member of the MB.

The current term of the MB of PZU started on 1 July 2015 and will last until the end of three consecutive financial years. The mandates of members of the MB expire not later than on the date of the General

Shareholders' Meeting approving the financial statements for the last full financial year of their term.

The MB exercises all management rights which have not been reserved by the provisions of law or provisions of the By-laws for the General Shareholders' Meeting or the Supervisory Board. The Company may be represented by two members of the MB acting jointly or one member of the MB acting with a commercial proxy. The MB adopts its regulations which are approved by the Supervisory Board. The regulations of the MB were adopted by the MB on 2 October 2012, amended with a Resolution of the Board of 8 April 2013, and approved by a resolution of the Supervisory Board of 16 April 2013.

The Regulations of the MB specify:

- the scope of MB's competencies and activities that require approval or confirmation by the Supervisory Board;
- competencies of the Chairman and Members of the MB;
- principles and organization of Board's activities, including its meetings and decision making procedures;
- rights and obligations of Board members upon dismissal.

In accordance with the regulations of the MB, resolutions of the MB are especially required for:

- adoption of a long-term plan for development and operations of the company;
- adoption of an action and development plan for PZU Group;
- adoption of an annual financial plan and a report on its implementation;
- approval of the financial statements for the previous financial year and the Management Report on the activities of the company;
- approval of a motion concerning profit distribution or loss coverage;
- determination of premiums in the compulsory and voluntary insurance and general voluntary insurance terms and conditions;
- determination of the scope and size of outward reinsurance and the tasks for inward reinsurance;
- adoption of an annual audit and control plan and a report on its implementation with conclusions;
- determination of the terms and conditions of investments, prevention and sponsoring;
- giving sureties and guarantees (excluding insurance operations) and taking out and giving credit facilities or loans by the Company (excluding credit facilities and loans given from the Company's Social Benefits Fund);
- appointment of a commercial representation.

In accordance with the regulations, meetings of the MB are held at least once a fortnight. The work of the MB is administered by the CEO whose powers include in particular:

- defining the scope of responsibility of each member of the MB;
- calling meetings of the MB;
- setting the agenda of the meeting of the MB;
- applying to the Supervisory Board for appointing and dissmissing members of the MB;
- designating a person to administer the work of the MB during the absence of the CEO.

The work of the MB is administered by the CEO who defines the scope of responsibility of each member of the MB.

Resolutions of the MB are adopted only in the presence of the Chairman or a person designated to administer the work of the MB during their absence.

Resolutions of the MB are adopted by an absolute majority of votes and in the event of a voting tie the CEO has the casting vote. The MB, upon consent of the CEO, may adopt resolutions in writing, on paper or in an e-form (i.e. using means of distant communication and a qualified electronic signature). The By-laws also provide that the meetings of the MB may be held using means of direct distant communication.

The CEO takes decisions in the form of orders and official instructions. Other Members of the MB administer the operations of the Company within the scope specified by the CEO.

The By-laws of PZU do not provide for any special rights of the MB concerning decisions to issue or redeem shares.

8.9 Remuneration of the members of the Group's bodies

Employment contracts concluded with the Members of the Management Board, approved by resolution of the Supervisory Board, do not include compensation for resignation or dismissal from their positions without a valid reason, or if the dismissal results from a business combination through an acquisition of the issuer.

Separate non-competition agreements regulate among others refraining from post-employment competition with PZU in exchange for damages. In 2014–2016, PZU Group companies included in consolidation did not grant any loans or similar benefits to members of their management boards, higher level managers or members of their supervisory boards.

Rules of granting annual bonuses to the Members of the Management Board

The bonuses of the Management Board's Members are dependent on their performance for the financial year. They are awarded by the Supervisory Board after the approval of the financial statements for the year.

The bonus amount depends on the performance of the business area supervised by the given Member of the Management Board; however, the areas that affect business results have much greater impact on remuneration than the support areas.

On 8 February 2017, Extraordinary Shareholders' Meeting of PZU adopted resolution no. 4/2017 on regulations that govern the forming of compensation of Members of the Management Board of Powszechny Zakład Ubezpieczeń Spółka Akcyjna. The next step will be the implementation of the regulation in question by the Supervisory Board of PZU.

Remuneration and other short-term employee benefits paid by PZU	**1 January – 31 December 2016**		**1 January – 31 December 2015**	
		incl. bonuses and special benefits:		incl. bonuses and special benefits:
Management Board, including:	**9,066**	**-**	**8,124**	**2,862**
Michał Krupiński	1,377	-	-	-
Rodger Hodgkiss	634	-	-	-
Andrzej Jaworski	434	-	-	-
Tomasz Kulik	- [1)]	-	-	-
Maciej Rapkiewicz	581	-	-	-
Beata Kozłowska-Chyła	634[2)]	-	-	-
Robert Pietryszyn	273	-	-	-
Paweł Surówka	176	-	-	-
Sebastian Klimek	579[3)]	-	-	-
Przemysław Dąbrowski	683[5)]	-	1,112	371
Dariusz Krzewina	668[6)]	-	1,281	507
Tomasz Tarkowski	121	-	995	332
Rafał Grodzicki	520[7)]	-	312	-
Andrzej Klesyk	1,950[4)]	-	2,970	1,170

Witold Jaworski	436[8)]	-	260	-
Ryszard Trepczyński	-	-	1 194[9)]	482
Top management (PZU Group Directors), including:	**4,503**	**199**	**3,799**	**1,530**
Aleksandra Agatowska	505	-	-	-
Tomasz Karusewicz	611	-	-	-
Bartłomiej Litwińczuk	241	-	-	-
Sławomir Niemierka	862	199	963	300
Roman Pałac	581	-	-	-
Paweł Surówka	455[10)]	-	-	-
Tobiasz Bury	706[11)]	-	1,276	606
Przemysław Henschke	542[12)]	-	936	312
Rafał Grodzicki	-	-	624	312
Management Board, including:	**1,241**	**-**	**1,224**	**-**
Paweł Kaczmarek	191	-	84	-
Maciej Zaborowski	143	-	-	-
Marcin Chludziński	119	-	-	-
Alojzy Nowak	120	-	120	-
Jerzy Paluchniak	118	-	-	-
Marcin Gargas	167	-	-	-
Eligiusz Krześniak	119	-	-	-
Piotr Paszko	119	-	-	-
Radosław Potrzeszcz	119	-	-	-
Piotr Walkowiak	11	-	-	-
Zbigniew Ćwiąkalski	3	-	180	-
Zbigniew Derdziuk	2	-	120	-
Dariusz Filar	2	-	132	-
Dariusz Kacprzyk	2	-	120	-
Jakub Karnowski	2	-	120	-
Aleksandra Magaczewska	2	-	156	-
Maciej Piotrowski	2	-	120	-
Tomasz Zganiacz	-	-	72	-

1) remuneration only from PZU Życie, amount in the following table
2) including remuneration resulting from competition prohibition in the amount of PLN 55 thousand
3) including remuneration resulting from competition prohibition in the amount of PLN 111 thousand
4) including remuneration resulting from competition prohibition in the amount of PLN 1.350 thousand
5) including remuneration resulting from competition prohibition in the amount of PLN 332 thousand
6) including remuneration resulting from competition prohibition in the amount of PLN 55 thousand
7) including remuneration resulting from competition prohibition in the amount of PLN 312 thousand
8) including remuneration resulting from competition prohibition in the amount of PLN 195 thousand
9) including remuneration resulting from competition prohibition in the amount of PLN 185 thousand
10) including remuneration resulting from the advisory function to the Management Board of PZU in the amount of PLN 345 thousand in the period of 24 April 2016 – 31 October 2016
11) including remuneration resulting from competition prohibition in the amount of PLN 371 thousand
12) including remuneration resulting from competition prohibition in the amount of PLN 312 thousand

Remuneration and other short-term employee benefits paid by other entities of PZU Group	1 January – 31 December 2016		1 January – 31 December 2015	
		including bonuses and special benefits:		including bonuses and special benefits:
Management Board, including:	**4,266**	**-**	**3,310**	**1,279**
Rodger Hodgkiss	599	-	-	-
Andrzej Jaworski	208	-	-	-
Tomasz Kulik	206	-	-	-
Maciej Rapkiewicz	208	-	-	-
Paweł Surówka	329	-	-	-
Beata Kozłowska-Chyła	329[1)]	-	-	-
Robert Pietryszyn	135	-	-	-
Sebastian Klimek	208[2)]	-	-	-
Przemysław Dąbrowski	368[3)]	-	799	400
Dariusz Krzewina	360[4)]	-	690	273
Tomasz Tarkowski	801[5)]	-	536	179
Rafał Grodzicki	280[6)]	-	504	168
Witold Jaworski	235[7)]	-	138	-
Ryszard Trepczyński	-	-	643[8)]	259
Top management (PZU Group Directors), including:	**2,332**	**107**	**1,546**	**492**
Aleksandra Agatowska	272	-	-	-
Tomasz Karusewicz	329	-	-	-
Bartłomiej Litwińczuk	147	-	-	-
Sławomir Niemierka	599	107	464	107
Roman Pałac	313	-	-	-
Tobiasz Bury	380[9)]	-	578	217
Przemysław Henschke	292[10)]	-	504	168

1) including remuneration resulting from competition prohibition in the amount of PLN 119 thousand (PZU Życie)
2) including remuneration resulting from competition prohibition in the amount of PLN 138 thousand (PZU Życie)
3) including remuneration resulting from competition prohibition in the amount of PLN 179 thousand (PZU Życie)
4) including remuneration resulting from competition prohibition in the amount of PLN 30 thousand (PZU Życie)
5) including remuneration resulting from competition prohibition in the amount of PLN 150 thousand (Link4)
6) including remuneration resulting from competition prohibition in the amount of PLN 168 thousand (PZU Życie)
7) including remuneration resulting from competition prohibition in the amount of PLN 105 thousand (PZU Życie)
8) including remuneration resulting from competition prohibition in the amount of PLN 100 thousand (PZU Życie)
9) including remuneration resulting from competition prohibition in the amount of PLN 200 thousand (PZU Życie)
10) including remuneration resulting from competition prohibition in the amount of PLN 168 thousand (PZU Życie)

Total estimated value of non-financial benefits granted by PZU and the subsidiaries of PZU	1 January – 31 December 2016	1 January – 31 December 2015
Management Board, including:	**1,057**	**1,224**
Michał Krupiński	79	-
Rodger Hodgkiss	36	-

Andrzej Jaworski	77	-
Tomasz Kulik	76	-
Maciej Rapkiewicz	101	-
Paweł Surówka	54	-
Beata Kozłowska-Chyła	105	-
Robert Pietryszyn	51	-
Sebastian Klimek	66	-
Przemysław Dąbrowski	92	191
Dariusz Krzewina	126	209
Tomasz Tarkowski	48	178
Rafał Grodzicki	51	129
Andrzej Klesyk	56	298
Witold Jaworski	39	40
Ryszard Trepczyński	-	179
Top management (PZU Group Directors), including	**605**	**600**
Aleksandra Agatowska	97	-
Tomasz Karusewicz	51	-
Bartłomiej Litwińczuk	51	-
Sławomir Niemierka	171	176
Roman Pałac	93	-
Tobiasz Bury	60	213
Przemysław Henschke	82	167
Rafał Grodzicki	-	44
Supervisory Board, including:	**-**	**11**
Zbigniew Ćwiąkalski	-	10
Waldemar Maj	-	1

Remuneration of Members of the Management Board of PZU, Capital Group Directors, and Members of the Supervisory Board of PZU paid, due or potentially due	**1 January– 31 December 2016**	**1 January– 31 December 2015**
a) Charged to costs	23 070	19,827
b) Resulting from incentive or bonus plans based on issuer's equity	-	-

09

9 Other

Correctness and reliability of presented financial statements

The Management Board of PZU declares that, to the best of their knowledge, the annual financial statements and comparable data of PZU have been prepared in accordance with the applicable accounting principles and provide a true, fair and clear view of the economic and financial position and the financial result of PZU and the management report of PZU presents a true picture of its development and achievements, including a description of the main risks and threats.

Selection of the entity authorized to audit financial statements

The Management Board of PZU represents that the entity authorized to audit financial statements - KPMG Audyt Sp. z o.o. sp. k. - which audited the annual consolidated financial statements was selected in accordance with the provisions of law and that the entity and certified auditors who audited the financial statements met the requirements to express an unbiased and independent opinion on the audited annual consolidated financial statements, in accordance with the applicable provisions of law and professional standards.

Significant agreements concluded between shareholders

By the date of issuing this Report on the activities of PZU, the Management Board of PZU has no knowledge about any agreements concluded between the shareholders, which could result in future changes in proportions of shares held by the existing shareholders.

Agreements concluded significant for the issuer's activity

On 8 December 2016, PZU and PFR concluded an agreement with UniCredit to purchase 32.8% of Bank Pekao shares for the total amount of PLN 10.6 billion.

On 16 October 2015, PZU issued a guarantee in relation to the liabilities of PZU Finance AB (publ) arising from the bonds issued by the company.

Related party transactions concluded differently than on arm's length basis

PZU Group companies provide services to each other, as part of their capital and business ties. With the exception of companies of the Tax Capital Group, transactions are concluded at arm's length.

Tax Capital Group

On 25 September 2014 a new Tax Capital Group agreement was signed, covering the following 13 PZU Group's companies: PZU, PZU Życie, LINK4 Towarzystwo Ubezpieczeń SA, PZU Centrum Operacji SA, PZU Pomoc SA, Ogrodowa-Inwestycje Sp. z o.o., Ipsilon Sp. z o.o., PZU Asset Management SA, TFI PZU SA, Ipsilon Bis SA, PZU Finanse Sp. z o.o., Omicron SA, Omicron Bis SA. Tax Capital Group was established for the period of 3 years from 1 January 2015 to 31 December 2017.

PZU is the parent entity and the company representing PGK in the above-mentioned agreement. Pursuant to Art. 25. In accordance with art. 25 section 1 of the CIT act, the tax capital group makes monthly settlements with the Treasury Office. PZU makes advance payments to the Treasury Office in scope of CIT owed from all companies, while PZU Życie provides PZU with advance CIT payments concerning the business activity of PZU Życie.

Loans and credits taken

The companies within PZU Group grant mutual loans to one another. The below table presents the list of loans granted in 2016 to entities related to the issuer:

Amount	date of granting the loan*	maturity date*	borrower	lender
PLN 250 million	2016-08-25	2016-10-18	PZU	PZU ŻYCIE
PLN 400 million	2016-05-27	2016-06-24	PZU	PZU Życie
PLN 350 million	2016-06-24	2016-07-25	PZU	PZU Życie
PLN 350 million	2016-07-27	2016-08-25	PZU	PZU Życie
PLN 70 million	2016-07-04	2030-12-31	PZU Zdrowie	PZU
PLN 80 million	2016-11-16	2026-12-31	TUW	PZU

* based on a cash flow

Guarantees and sureties issued and granted

On 31 March 2016, a guarantee agreement was concluded between PZU and Alior Bank (Current report no. 18/2016) for the total of PLN 2,548,855,794. On 1 July 2016, the guarantee was terminated by Alior Bank.

Information on off-balance sheet items as at the end of 2016 has been presented in **SECTION 6.7 STRUCTURE OF ASSETS AND LIABILITIES**.

Insurance contracts that exceed 25% of the total technical provisions and equity

In 2016, PZU did not conclude any insurance contract for a sum of a single risk insured, net of reinsurance, that exceed 25% of the total technical provisions **GLOSSARY**and equity.

Seasonal or cyclical business

Operations of PZU are not of a seasonal or cyclical nature to the extent that would justify application of the suggestions presented in the International Financial Reporting Standards.

Evaluation of financial resources management, including the ability to repay liabilities and definition of possible threats and activities, undertaken or planned by the Issuer to counteract these threats

The financial position of the Issuer is very good. It meets all the security requirements imposed by the Act on Insurance Activity **GLOSSARY** and the Polish Financial Supervision Authority **GLOSSARY**. A stable rating outlook of PZU confirms that the Issuer has a strong business position, high levels of equity, and is a competitive entity on the insurance market.

Financial forecast

PZU did not publish forecasts concerning financial results.

Disputes

In 2016 and by the date of signing of this Management's Report of PZU, PZU did not take part in any proceedings before court, body competent to hear arbitration proceedings or public authority body concerning liabilities or receivables of PZU or its direct and indirect subsidiaries with the value of at least 10% of the equity of PZU. The description of court cases and proceedings before the President of the Office of Competition and Consumer Protection **GLOSSARY** (OCCP) is included in the financial statements of PZU for 2016.

As at 31 December 2016, the total value of all 102,455 cases heard by courts, bodies competent to hear arbitration proceedings or public authority bodies involving PZU entities was PLN 3,249.6 million.
The amount includes PLN 2,968.0 million of liabilities and PLN 281.6 million of receivables of PZU companies, which accounted for 24.3% and 2.3% of the equity of PZU calculated in line with PAS, respectively.

This Management Report of PZU for 2016 includes 101 pages with sequential numbers.

Signatures of Members of PZU Management Board

Michał Krupiński – Chairman of the Management Board

Roger Hodgkiss – Member of the Management Board

Andrzej Jaworski – Member of the Management Board

Tomasz Kulik – Member of the Management Board

Maciej Rapkiewicz – Member of the Management Board

Warsaw, 14 March 2017

Appendix: Financial data

Data from the profit and loss account **(PLN thousand)**	**2016**	**2015**	**2014**	**2013**	**2012**
Gross written premiums	10,682,014	8,858,036	8,261,752	8,273,900	8,453,498
Net premiums earned	9,212,816	7,897,960	7,902,639	8,108,036	8,277,136
Claims and benefits	6,148,534	5,036,629	5,230,864	5,047,077	5,473,011
Acquisition expenses, including reinsurance commission	1,849,490	1,571,480	1,522,886	1,366,807	1,494,696
Administrative expenses	723,941	753,737	729,142	662,694	676,296
Technical result	536,523	636,334	564,429	1,061,855	640,118
Net investment result	1,897,566	2,023,981	2,568,038	4,633,302	2,472,660
Gross profit (loss)	1,876,333	2,475,921	2,854,524	5,390,880	2,924,381
Net profit (loss)	1,592,951	2,248,522	2,636,733	5,106,345	2,580,720

Main balance sheet items **(PLN thousand)**	**31 December 2016**	**31 December 2015**	**31 December 2014**	**31 December 2013**	**31 December 2012**
ASSETS, including:	**37,418,630**	**36,358,361**	**34,629,778**	**30,136,572**	**29,913,216**
Financial assets	31,476,581	32,356,048	31,030,939	27,609,398	27,591,485
Receivables	2,252,438	1,801,903	2,437,819	1,496,637	1,473,952
LIABILITIES, including:	**37,418,630**	**36,358,361**	**34,629,778**	**30,136,572**	**29,913,216**
Equity	12,219,012	12,378,733	12,328,724	12,259,761	13,452,581
Technical provisions	18,714,789	17,540,493	16,861,181	15,912,942	14,933,110
Other liabilities and special funds	5,156,199	5,109,816	4,598,574	1,280,359,	810,652
Accruals and deferred income	942,786	856,403	576,129	518,282	498,518

One-off events in PZU **(PLN million)**	**2016**	**2015**	**2014**	**2013**	**2012**
Agricultural insurance	(236.7)				
Change in the rates for annuity provision					(234.2)
Provisions for employee benefits due to the termination of the Collective Bargaining Agreement					147.8
Technical result on contract bonds Insurance in the corporate insurance segment					(93.2)
Reinsurance settlements in the scope of the Green Card cover				53.2	

Appendix: Glossary

Act on Insurance Activity – Act on Insurance Activity of 11 September 2015 (Journal of Laws of 2015, Item 1844), most of provisions effective as of 1 January 2016. The Act introduces the Solvency II requirements to the Polish legislature.

Act on statutory auditors – Act on statutory auditors and their self-governing body, auditing firms and on public oversight of 7 May 2009 (Journal of Laws of 2009, No. 77, item 649, as amended).

BLS (direct claims handling) – a system of handling a claim by an insurance company which issued MTPL insurance policy of the injured party, not the perpetrator. It has been operating in Poland since 1 April 2015 under PIU (Polish Chamber of Insurance). Once the claims handling process is finished, the insurance companies settle the amount as a lump-sum via the Polish Chamber of Insurance (PIU).

Code of Commercial Companies – Act of 15 September 2000 – Code of Commercial Companies (Journal of Laws of 2000, No. 94, item 1037, as amended).

compensation – the amount of money that the insurer pays aout from the insurance in the case of an event covered by the insurance contract

COR - Combined Ratio – combined ratio calculated for the non-life sector (class II). It is the ratio of all the insurance expenses related to insurance administration and payment of claims (i.e. the costs of claims, acquisition and administration) to earned premium in a given period.

cross-selling – a strategy for selling a given insurance product in conuction with other supplementary insurance product or a product offered by the insurer's partner, e.g. bank. The example of such products are bank and insurance products, such as credit insurance.

Civil Code – Act of 23 April 1964 – Civil Code (Journal of Laws No. 16 of 1964, item 93, as amended).

insurance agent – an entrepreneur performing agency activities under an agreement concluded with the insurance company. The agents' activities focus on: customer acquisition, concluding insurance contracts, participating in the administration and performance of insurance contracts and organizing and supervising the activities of the agency.

insurance broker – an entity authorized to pursue brokerage activities. A broker performs activities in the name of or on behalf of a person or entity seeking insurance coverage.

IPO (Initial Public Offering) – the first public offering of certain securities. The key elements of IPO are: drafting of a prospectus and proceedings before an authority that supervises the process of granting an admission for trading

Everest-– a system for managing non-life insurance which is being implemented in PZU.

NPS (Net Promoter Score) – a method of assessing loyalty of a given company's customers; calculated as the difference between promoters and critics brand

Solvency Capital Requirement, SCR – a capital requirement calculated as per Solvency II provisions. Calculation of the capital requirement is based on the calculation of the following risks market, actuarial (insurance), counterparty insolvency, catastrophe, and operating risk, and afterwards undergoes a diversification analysis. The ratio can be calculated under a standard formula or, once an applicable permit of a supervisory body has been obtained, using a whole or partial internal model of the company.

PFSA – Polish Financial Supervision Authority, www.knf.gov.pl

solvency margin – the amount of an insurance undertaking's shareholder funds no lower than the minimum guarantee fund which is required to ensure that the undertaking remains liquid.

PIU (Polish Chamber of Insurance) – insurance economic local authority which gathers all insurance companies operating in Poland.

S&P rating – a credit risk assessment performed by Standard & Poor's. An A- rating means that issuers of debt instruments have a high capability of servicing their obligations giving consideration to the emergence of factors diminishing that capability.

reinsurance – yielding all or a portion of an insured risk or a group of risks along with the commensurate portion of the premiums to some other insurance company – a reinsurer. As a result of reinsurance, there is a secondary split of the risks making it possible to minimize the risks to the insurance market.

outward reinsurance – reinsurance activity entailing an insurer (cedant) yielding a portion of the executed insurance contracts to a reinsurer/reinsurers in the form of a reinsurance contract.

inward reinsurance – reinsurance activity entailing a reinsurer or reinsurers accepting a portion of the insurance or groups of insurance yielded by the cedant.

technical provisions – provisions which should ensure full coverage of all current and future liabilities that may arise from insurance contracts. Technical provisions include in particular: provision for unearned premiums, provision for unpaid claims and provision for unexpired risks, provision where the investment risk is born by the policyholders, provision for bonuses and rebates for the policyholders.

gross written premium – a gross amount of premiums (without including the reinsurers' share) due on the insurance contracts executed in a financial year, regardless of the term of liability established by these contracts.

earned premium – a written premium in a given period giving consideration to the settlement of revenues (premiums) over time through movement in premium provision.

Solvency II – capital requirements for European insurance companies based on the risk undertaken. The requirements have been effective as of 1 January 2016.

technical rate – the rate used to discount technical provisions in life insurance and provisions for capitalized annuities in third party liability insurance. According to the Finance Minister's Ordinance of 28 December 2009 on the special accounting standards for insurance and reinsurance undertakings, the technical rates used by an insurance undertaking may not be higher than 80% of the weighted-average rate of return on investments covering technical provisions during the most recent three financial years. PFSA calculates and announces the maximum technical rate by 31 January of every year.

risk-free rate – the rate of return on risk-free financial instruments. PZU's risk-free rate is based on yield curves for treasury instruments, and it is also the basis for setting transfer prices in settlements between operating segments.

sum insured – the cash amount for which an insured object is insured. In non-life insurance the sum insured ordinarily constitutes the upper limit of the insurer's liability.

TSR – Total shareholder return (market price of shares at end of the period - market price of shares at the beginning of the period + dividend paid in the period) / market price of shares at beginning of the period

underwriting – the process of selecting and groupifying risks declared for insurance to estimate and accept, according to suitable terms and conditions, or reject an insurance risk.

OCCP – Office of Competition and Consumer Protection, www.uokik.gov.pl

solvency ratio – a statutory ratio (under Solvency II) specifying the level of capital security for the business conducted by an insurer; by law, this ratio should be above 100%.

DPS (dividend per share) – a market ratio that determines the value of dividend per share

DY (dividend yiels) – dividend per share / share market price

EPS (earnings per share) – a market ratio that determines the earnings attributable to a single share

P / BV – market price per share / book value per share

P / E – the company market price per share / profit per share

Prudent person principle – the rule laid down in Article 129. Of Directive of the European Parliament and of the Council on the taking-up and pursuit of the business of Insurance and Reinsurance Solvency II. The prudent person principle requires (re)insurance undertakings to invest assets in the best interest of policyholders, adequately match investments and liabilities, and pay due attention to financial risks, such as liquidity and concentration risk.

venture capital – mid- and long-term investments in non-public enterprises in the early stages of development, combined with managerial support, provided by specialized parties (venture capital funds). The objective of a venture capital investment is to generate profit from increased goodwill of the company and re-sell its shares or stocks after a given period

These Financial Statements contains forward-looking statements concerning the strategic operations.

Such forward-looking statements are exposed to both known and unknown types of risks, involve uncertainties and are subject to other significant factors which may cause that the actual results, operations, or achievements of PZU considerably differ from future results, operations, or achievements expressed or implied in the forwards-looking statements. The statements are based on a number of assumptions concerning the current and future business strategy of PZU and the external environment in which the Group will operate in the future. PZU expressly waives any and all obligations or commitments concerning distribution of any updates or adjustments to any of the assumptions contained in these Financial Statements of PZU, which shall aim to reflect the changes in PZU expectations or changes in events, conditions, or circumstances on which a given assumption has been made, unless provisions of the law provided otherwise. PZU stipulates that the forward-looking statements do not constitute a guarantee as to the future results, and the company's actual financial standing, business strategy, management plans and objectives concerning the future operations may considerably differ from those presented or implied in such statements contained in these Financial Statements of PZU. Moreover, even if the PZU's financial standing, business strategy, management plans and objectives concerning the future operations comply with the forward-looking statements contained in these Financial Statements of PZU, such results or events may not be treated as a guideline as to the results or events in the subsequent periods. PZU does not undertake to publish any updates, changes, or adjustments to information, data or statements contained in these Financial Statements of PZU if the strategic operations or plans of PZU shall change, or in the case of facts or events that shall affect such operations or plans of PZU, unless such an obligation to inform resulted from applicable provisions of the law. PZU is not liable for the effects of decisions made following the reading of the Financial Statements of PZU. At the same time, these Financial Statements of PZU may not be treated as a part of a call or an offer to purchase securities or make an investment. The Financial Statements of PZU does not constitute also an offer or a call to effect any other transactions concerning securities.