

TABLE OF CONTENTS

Letter from the PAFF Leadership	2
PAFF Mission Statement	5
The Foundation's Programs	6
Managers of the PAFF's Programs – Internet Guide	10
Consolidated Financial Statements	12
Notes to Financial Statements	15
Report of Independent Public Accountants	18
Board of Directors	19
Management	20

MESSAGE FROM THE PAFF LEADERSHIP

Nearly a year has elapsed since our Foundation began its operation. It was established in the United States in 1999, and opened its Representative Office in Warsaw at the beginning of 2000, and a few months later announced its first programs. The programs, as well as our subsequent endeavors were based on the “Mission Statement”, which was adopted by the Foundation’s Board of Directors, defining the broad objectives of the newly-established institution.

The creation of the Foundation was due to the success of the Polish-American Enterprise Fund (PAEF), a unique vehicle which provided significant United States’ assistance to the development of a market economy in Poland since 1990. Since its establishment, the Fund utilized its \$240 million of capital to support the development of the private sector, through investments, loan programs and assistance in training. Institutions established by the Fund have become part of the transition history of the Polish economy. These include: Enterprise Investors, the First Polish-American Bank (now owned by Fortis Bank), Enterprise Credit Corporation, Polish-American Mortgage Bank, the Micro Fund and the Enterprise Educational Foundation.

Funds deriving from the gradual liquidation of the PAEF investment portfolio are being contributed to the newly-established Polish-American Freedom Foundation’s endowment. At the same time \$120 mln is being returned to the U.S. Treasury; a first in U.S. foreign aid. The U.S. Government will receive this amount over three years. The first payment made by PAEF to PAFF amounted to \$40 million, and the second draw of \$40 million entered the Foundation’s account in September 2000, while the transfer of the remaining funds will take place within next years. Eventually, it is anticipated that the Foundation will capitalize at \$180 – 200 million. The current amount of its endowment already places PAFF among the largest foundations in the Region. Revenue to be generated from the corpus is intended to provide a stable funding source for the Foundation’s present and future operations.

The Polish-American Freedom Foundation’s statutory goal is to support the development of civil society, democracy and market economy, and to equalize opportunities for personal and social development in Poland, and to the extent possible, share this experience in other countries of Central and Eastern Europe.

Following the decision of the Board of Directors, the Foundation undertook activities in three programmatic areas during its first year of operation: education, support for local communities, and sharing with our neighboring countries the Polish experiences in transformation.

We announced the first seven pilot programs last June and have allocated \$1,725,000 towards their implementation. Full realization of these programs will vary from a few months to more than a year in some cases. While designing our pilot programs and consecutive undertakings, we have placed special emphasis on activities promoting the stimulation and strengthening of civic initiatives in those areas that have problems with their development, as well as educational efforts, targeting recipients mainly in villages and small towns.

In the field of education, our first programs included such things as support for reforms that are currently being implemented in Poland. We have financed the establishment of a non-commercial Interkl@sa Internet portal, to become an Internet guide for teachers, students, parents and educational authorities of the local government. Thanks to the “Computer for a Teacher 2000” Program, we have enabled purchase of PCs on preferential terms to teachers of junior high schools located outside of large metropolitan areas. This should give them a head start to be able to deliver training in the newly-established junior high schools, especially in view of the anticipated completion of the process of computerizing those institutions. Through implementation of the “English Teaching 2000” Program, we promote teaching of the English language in rural areas and in small towns. We have initiated a program to support the development of health service managers to more efficiently operate their care centers while the health care system in Poland is undergoing profound transformation.

In line with our emphasis on projects that reinforce civil society in Poland, especially in places located away from large metropolitan areas, the Foundation has taken steps to support the development of local communities. Under the “Act Locally” Program, the Foundation financially supported nearly 70 initiatives out of a total of more than 500 submitted proposals. We believe their implementation will help to solve problems and stimulate professional aspirations within local communities. After one year, these organizations whose projects are judged to be most effective will be awarded, and their experiences will be promoted in other small towns and villages.

The Foundation also supported the “Mutual Information Society” Program which is an important vehicle to support valuable civic initiatives and to reinforce the third sector in Poland. Under this Program, an information gathering and distribution system is being established which will be lasting, professionally managed and available to all. It collects and makes available information about and for non-governmental organizations, especially those operating at the local level.

The Lane Kirkland Scholarship Program that has involved visiting fellows from Ukraine (in the academic year 2000/2001) was our first international project. We believe that the participants in the Program, who come from countries of Central and Eastern Europe, will utilize the knowledge acquired in Poland regarding her systemic transformation, and contribute to a similar process in their respective countries.

While focusing on the implementation of our first programs, in the second half of 2000, we were simultaneously developing new undertakings. This second round of programs (approved by the Foundation’s Board in the Fall of 2000) lies within, and broadens the original three key areas of our operation. The total amount of grants awarded in round two (six new programs) is \$ 2,300,000 and includes, among others, a grant to continue support of the Educational Enterprise Foundation, established by the Polish-American Enterprise Fund.

Our Foundation has begun to address large and difficult issues such as developing innovative methods to deal with unemployment as well as finding ways to stimulate civic activity in rural areas. We recognize that our resources are modest compared to the enormous needs in both fields, however, we believe that some of activities under these programs will be successful and will provide models that can have a significant impact when applied on a wider scale throughout the country.

In the second round of new programs we have undertaken further projects related directly to education; one of them being a program to develop and implement high teaching standards in the educational sector, and especially in schools located away from metropolitan areas. In order to respond to a particularly serious need of non-governmental organizations, we have launched a program to train and develop financial officers working for institutions within Poland’s third sector. Also, regarding the sharing of Polish transformation experiences, we have initiated a new program to support relevant initiatives undertaken by Polish non-governmental organizations in their contacts with countries of Central and Eastern Europe.

It is noteworthy that in the first year of its operation, PAFF has become a major co – founder of eminent prizes awarded by the Prime Minister under the “Pro Publico Bono” national competition for the best civil initiative, celebrated on November 11 – the Polish Day of Independence (PAFF has allocated \$50,000 for the competition).

Representatives of our Foundation have taken part in several conferences of non-governmental organizations, including two important international events: the World Forum on Democracy (Warsaw, June 2000) and the General Assembly of European Foundation Center (Cracow, September 2000). During the initial period of our operation, we paid great attention to two-way consulting with non-governmental organizations, national, local, and regional. We have had meetings with over 200 leading foundations and associations, as well as individuals who are prominent in the development of this sector. Our partners in these discussions were most generous in sharing their experience and also expressed great interest in the plans of the Polish-American Freedom Foundation, indicating their desire for full cooperation. PAFF has implemented its undertakings to date mainly through Polish non-governmental organizations,

to whom it transfers resources to manage its specific programs. It was, therefore, a matter of great importance during these discussions to be able to select organizations that could administer our programs currently or in the future. Under our grant-giving programs, those interested in being funded submit their applications directly to the organizations playing the role of Program Managers, while decisions to award the grants are taken by expert committees appointed by PAFF.

Parallel to consulting with Polish third sector leaders, we have had meetings with representatives of the state authorities, the government, the Parliament, as well as academic circles, opinion makers and the media. The purpose of the meetings was both to introduce the newly-established Polish-American Freedom Foundation, and determine the level of expectations concerning its operation. All our partners in these discussions expressed their support of the Foundation's mission, and emphasized its need in Poland as well as in other countries of the Region which are in the process of transformation.

We end the first year of the activity of the Polish-American Freedom Foundation with the conviction that it constitutes a solid base for further development of its programs. We are ready to support approaches to problems that have not been tried before, and therefore run the risk that some of these attempts will not bring satisfactory results. Nevertheless, we believe that it is this type of prudent exploration that is necessary to create the potential for true progress.

We would like to express our gratitude to all those who have contributed to the successful commencement of the Polish-American Freedom Foundation, as well as those who have established cooperation with us, and kindly shared their knowledge and experience. We look forward to continued cooperation and synergy in addressing our shared concerns.



John P. Birkelund
Chairman of the Board of Directors



Jerzy Koźmiński
President & Chief Executive Officer

New York/Warsaw, February 2001

PAFF MISSION STATEMENT

The Polish-American Freedom Foundation seeks to advance democracy, civil society, economic development and equal opportunity in Poland and, ultimately, in other Central and Eastern European countries.

The Freedom Foundation builds on the Polish people's historic achievements in establishing free market democracy since 1989, a success that the United States has strongly supported.

The Foundation was made possible by the extraordinary accomplishments of the Polish-American Enterprise Fund, a pioneering U.S. initiative that promoted entrepreneurial development in a free Poland, working from the principle that the people, given an opportunity, some know-how assistance and initial capital, could succeed.

The Freedom Foundation will work from the same premise – that people provided with the opportunity can successfully control their own destinies and build their own democratic structures. It will provide grants and otherwise assist NGOs and local initiatives. It will support young leaders who will soon face the challenges of the new century. It will promote equal opportunity, and also reforms in education, public administration, and health care. It will support systemic changes and development of Poland's still troubled areas, such as the countryside.

The Foundation will implement its statutory goals in a flexible and open manner. It will develop partnerships with non-governmental organizations, both those that have proven themselves and new ones that show initiative and promise.

Poland's success in carrying out its free market, democratic transformation is already providing key experience for other nations emerging from communism. The Foundation will develop programs in order to share with Central and Eastern European peoples the experience and lessons learned from more than ten years of reforms.

Under the joint Polish and American leadership, the Foundation aims to promote the core values shared by both nations: freedom, democracy, and respect for each individual. These values have linked us for centuries and bring us together in solidarity as allies.

"Mission Statement" was adopted by the Foundation's Board of Directors in March 2000.

THE FOUNDATION'S PROGRAMS

The intention of the Foundation is that its programs are a response to the real social needs and that they are designed in a process of consultation and partner-like cooperation with institutions of the third sector in Poland. While carrying out its mission, the PAFF involves non-governmental organizations which are able to shoulder the role of managers of the Foundation's programs. The Foundation gives financial means to those organizations to administer projects developed by the PAFF. Under the grant programs, the interested partners can apply for support directly to the given program managers and the grant-allocation decisions are made by expert committees appointed by the PAFF.

The Foundation is open to information about valuable proposals and initiatives born in the third sector, corresponding with PAFF's programmatic line, and those which can be used for developing further undertakings of the Foundation.

PROGRAMMATIC FIELD I INITIATIVES IN EDUCATION

THE "EDUCATION ON THE INTERNET – INTERKL@SA POLISH EDUCATIONAL PORTAL" PROGRAM

The purpose of this Program is to create a Polish nationwide Internet portal that provides easy, fast, and inexpensive access to various educational resources and services for Polish schools, teachers, students, parents, as well as educational organizations and institutions. The "Education on the Internet" is a joint venture by the Polish-American Freedom Foundation and the "Interkl@sa" Program which was launched by members of the Parliamentary Committee for Education, Science, and Young People, and whose Secretariat is managed by the Foundation for Economic Education. The Foundation allocated \$245,000 for the Program.

Program Manager: The Foundation for Economic Education (Fundacja Edukacji Ekonomicznej)

THE "COMPUTER FOR A TEACHER 2000" PROGRAM

The purpose is to assist teachers to buy a personal computer in installments. It is intended for junior high school teachers in smaller towns and villages. The Foundation subsidizes the interest charges on the loan. Initially, some 2,000 teachers were to receive assistance under this Program. The Foundation allocated \$250,000 for the Program. In January 2001, the PAFF Board of Directors approved the Program's continuation for this year. The funds allocated for the second round will reach \$140,000, thus increasing the number of teachers benefiting from the Program by some 1,000.

Program Manager: The National Foundation for Computer Literacy (Ogólnopolska Fundacja Edukacji Komputerowej)

THE "ENGLISH TEACHING 2000" PROGRAM

The purpose is to support activities which improve the quality of English-language teaching and, in particular, create equal education opportunities for children and young people from villages and small towns. Under this Program, educational organizations and institutions were able to seek grants for projects related to teaching the English language. The committee of independent experts recommended 58 of 168 submitted applications to be financed as the best-prepared initiatives. The implementation of the approved projects started in November 2000. The Foundation allocated \$240,000 for the Program.

Program Manager: The Polish Children and Youth Foundation (Polska Fundacja Dzieci i Młodzieży)

THE “TRAINING FOR HEALTH CARE MANAGERS” PROGRAM

The Program is to help improve knowledge of modern health care management. In the 2000/2001 academic year, the Foundation will issue 200 grants to health care managers from health establishments outside major urban centers. The grants would cover part of their postgraduate education in health care management. The Program would also support financially actions to improve the quality of training. The Foundation allocated \$250,000 for the Program.

Program Manager: Society of Health Care Managers (Stowarzyszenie Menedżerów Opieki Zdrowotnej)

“THE LEARNING SCHOOLS” PROGRAM (LES)

The Program is intended to create within the Polish education system – which is undergoing systemic transformation – an efficient model of improving the quality of schools. This will be done through developing carefully designed training cycles for teacher groups and through the work of the The Learning Schools Club, a chain of co-operating schools whose teacher councils use skills gained at training courses to determine the standards of their own work, make a genuine evaluation of their own teaching practices, and exchange experience among themselves. The Learning Schools Club is expected to become an implementer of spreading good school practices, supporting and developing the education reform in Poland. Initially, the Program will be addressed mainly to schools in small towns and villages, especially to the junior high schools. The Foundation allocated \$260,000 for the Program (for 2 years).

Program Manager: Center for Citizenship Education Foundation (Centrum Edukacji Obywatelskiej)

THE “MANAGEMENT EDUCATION 2001” PROGRAM (MANED)

The Program aims at supporting management education through sponsoring projects concerning scholarships, publications, conferences, competitions and other initiatives ensuring better accessibility and higher quality of management education so that it can meet the challenges of contemporary market economy. The Program – comprising a wide range of activities – is to be carried out totally by The Educational Enterprise Foundation as the continuation of the EEF activities initiated ten years ago by the Polish-American Enterprise Fund. The grant scholarship program is aimed primarily at the most talented youth from small towns and villages who are studying economics and related subjects at universities and higher schools of business. The Foundation allocated \$350,000 for the Program.

Program Manager: Educational Enterprise Foundation (Fundacja Edukacyjna Przedsiębiorczości)

PROGRAMMATIC FIELD II: SUPPORT FOR LOCAL COMMUNITIES

THE “MUTUAL INFORMATION SOCIETY” PROGRAM (MIS)

The purpose of this Program is to create a broadly-accessible system for storing and disseminating information about and for non-governmental organizations and local initiatives (the Internet, telephone information lines, CD-ROM, publications, etc.). Opinions and analyses of issues important to the non-governmental sector, as well as models of success, are also being produced under this Program. The Program calls for cooperation with, and support for local organizations whose goal is the improvement of the information infrastructure of the third sector. The Foundation allocated \$250,000 for the Program.

Program Manager: Klon/Jawor Society (Stowarzyszenie Klon/Jawor)

THE “ACT LOCALLY” PROGRAM

The purpose of this Program is to support civic initiatives and the work of non-governmental organizations that operate in the area of community development. Under this Program it was possible to seek grants for projects which, regardless of specific activity, will help solve local problems and create lasting mechanisms for development. The committee of independent experts qualified 69 projects of 531 submitted for financial assistance. The Program will conclude with a competition in which awards will be given for the best-implemented projects. The Foundation allocated \$250,000 for the Program.

Program Manager: Academy for the Development of Philanthropy in Poland (Akademia Rozwoju Filantropii w Polsce)

THE “FINANCIAL MANAGEMENT FOR NGOS” PROGRAM (FIMANGO)

The purpose of the Program is to improve financial management over the finances of Polish NGO's. The Program finances the costs of producing modern, easy-to-use financial guides for persons responsible for the financial affairs of NGO's, delivered in the form of publications, CD-ROMs, and Internet presentations. An important component of the Program is a series of informative conferences, each lasting two/three days, for about 500 persons from NGOs. These activities are expected, among other things, to help the participants make successful applications for public resources available in Poland and from international organizations. The Foundation allocated \$140,000 for the Program. The PAFF's co-financing Partner in this Program – the Kronenberg Foundation – allocated \$30,000.

Program Manager: Civil Society Development Foundation (Fundacja Rozwoju Społeczeństwa Obywatelskiego)

THE “UNDOING UNEMPLOYMENT” PROGRAM (2U)

The aim of this pilot-Program, addressed chiefly to non-governmental organizations, is to obtain and spread experience in what is known as “outplacement” – a method of controlling unemployment which uses career consultation, training, labor exchange, with special stress on psychological aspects involved. The Program is to help generate grass-roots initiatives and encourage local institutions to carry out active unemployment prevention measures by way of designing and implementing specific projects. The intention is to work out effective models for local action and spread them to help solving the unemployment issue. The Foundation allocated \$550,000 for the Program.

Program Manager: Enterprise Development Foundation in Suwałki (Fundacja Rozwoju Przedsiębiorczości w Suwałkach)

THE “VILLAGE IN TRANSITION” PROGRAM (VITA)

The Program intends to inspire citizens' initiatives in selected rural areas with low social activity. It is to be achieved throughout cooperation between local communities and a group of NGO partners, experienced in working in rural regions. This cooperation consists, primarily, of training, consultancy, and joint implementation of certain undertakings which can seed development activities. The Program will also support the regular and comprehensive exchange of experience and information between organizations working for the benefit of rural communities. The Foundation allocated \$500,000 for the Program.

Program Manager: Rural Development Foundation (Fundacja Wspomagania Wsi)

THE “LANE KIRKLAND SCHOLARSHIP” PROGRAM

The Foundation launched a long-term grant Program designed primarily to share Poland’s experience in the transformation with other countries of Central and Eastern Europe. A pilot stage of this Program is held at several Polish educational establishments during the academic year 2000/2001. It accepted grantees from Ukraine and concentrated on issues connected with the economic, social, and political change. Modeled on the experience of the American Fulbright Program, the Program was named after the late Lane Kirkland who rendered great services for Poland. (Lane Kirkland was the long-time President of the AFL/CIO and a Member of the Board of Directors of the Polish-American Enterprise Fund.) The Foundation allocated \$240,000 for the Program.

Program Manager in academic year 2000/2001: The Center for East European Studies of the Warsaw University (Studium Europy Wschodniej Uniwersytetu Warszawskiego)

THE “REGION IN TRANSITION” PROGRAM (RITA)

The Program is intended to share transformation experience with other Central and Eastern European countries by supporting contacts of Polish non-governmental organizations in this region. The above goal is to be attained through expert support, education and establishing of cooperation with persons or institutions from these countries, through initiatives that would be primarily pursued in Poland. A major component of the Program will be participation in shaping new intellectual, economic and political leaders and opinion makers – ready and capable to undertake activities for democracy, market economy and civil society. The Program is addressed to Polish non-governmental organizations as well as educational institutions that are implementing projects with the objective of supporting the transformation processes in former Eastern Bloc countries. The Foundation allocated \$500,000 for the Program.

Program Manager: Foundation Education for Democracy (Fundacja Edukacja dla Demokracji)

MANAGERS OF THE PAFF'S PROGRAMS – INTERNET GUIDE



THE “EDUCATION ON THE INTERNET – INTERKL@SA POLISH EDUCATIONAL PORTAL PROGRAM

Program Manager: The Foundation for Economic Education
(Fundacja Edukacji Ekonomicznej)

<http://www.interklasa.pl>



THE “COMPUTER FOR A TEACHER 2000” PROGRAM

Program Manager: The National Foundation for Computer Literacy
(Ogólnopolska Fundacja Edukacji Komputerowej)

<http://www.ofek.waw.pl>



THE “ENGLISH TEACHING 2000” PROGRAM

Program Manager: Polish Children and Youth Foundation
(Polska Fundacja Dzieci i Młodzieży)

<http://www.pcyf.org.pl>



THE “TRAINING FOR HEALTH CARE MANAGERS” PROGRAM

Program Manager: Society of Health Care Managers
(Stowarzyszenie Menedżerów Opieki Zdrowotnej)

<http://stomoz.hosp.torun.pl>



“THE LEARNING SCHOOLS” PROGRAM

Program Manager: Center for Citizenship Education Foundation
(Centrum Edukacji Obywatelskiej)

<http://www.ceo.org.pl>



THE “MANAGEMENT EDUCATION 2001”

Program Manager: Educational Enterprise Foundation
(Fundacja Edukacyjna Przedsiębiorczości)

<http://www.fep.lodz.pl>



THE “MUTUAL INFORMATION SOCIETY” PROGRAM

Program Manager: Klon/Jawor Society
(Stowarzyszenie Klon/Jawor)

<http://www.ngo.pl>

THE “ACT LOCALLY” PROGRAM

Program Manager: Academy for the Development of Philanthropy in Poland
(Akademia Rozwoju Filantropii w Polsce)
<http://www.filantropia.org.pl>



THE “FINANCIAL MANAGEMENT FOR NGOS” PROGRAM

Program Manager: Civil Society Development Foundation
(Fundacja Rozwoju Społeczeństwa Obywatelskiego)
<http://free.ngo.pl/csdf/>



THE “UNDOING UNEMPLOYMENT” PROGRAM

Program Manager: Enterprise Development Foundation in Suwałki
(Fundacja Rozwoju Przedsiębiorczości w Suwałkach)
<http://www.frp.of.pl>



THE “VILLAGE IN TRANSITION” PROGRAM

Program Manager: Rural Development Foundation
(Fundacja Wspomagania Wsi)
<http://www.fww.org.pl>



THE “LANE KIRKLAND SCHOLARSHIP PROGRAM”

Program Manager: The Center for East European Studies of Warsaw University
(Studium Europy Wschodniej Uniwersytetu Warszawskiego)
<http://www.uw.edu.pl>



THE “REGION IN TRANSITION” PROGRAM

Program Manager: Foundation Education for Democracy
(Fundacja Edukacja dla Demokracji)
<http://www.edudemo.org.pl>

STATEMENT OF FINANCIAL POSITION

As of September 30, 2000

ASSETS

ASSETS:

Cash and cash equivalents (Note 6)	\$ 30,166,505	
Corporate commercial paper (Note 6)	<u>9,914,421</u>	
Total cash and cash equivalents		\$ 40,080,926
U.S. Government Agency Bonds (Note 6)		40,090,037
Accrued interest receivable		749,117
Fixed assets, net (Note 7)		99,787
Prepaid expenses and other assets		<u>16,986</u>
Total assets		<u>\$ 81,036,853</u>

LIABILITIES AND NET ASSETS

LIABILITIES:

Grants payable (Note 5)		\$ 1,200,000
Accrued expenses		<u>136,525</u>
Total liabilities		<u>1,336,525</u>

NET ASSETS:

Unrestricted:		
Excess of income over expenses		1,417,119
Grant disbursements		(525,000)
Cumulative translation adjustment		<u>8,209</u>
		900,328
Grants payable (Note 5)		<u>(1,200,000)</u>
Total unrestricted		(299,672)
Permanently restricted (Note 4)		<u>80,000,000</u>
Total net assets (Note 5)		<u>79,700,328</u>
Total liabilities and net assets		<u>\$ 81,036,853</u>

The accompanying notes are an integral part of this statement.

STATEMENT OF ACTIVITIES

For the period from inception (August 11, 1999) through September 30, 2000

CHANGES IN UNRESTRICTED NET ASSETS:

INCOME:

Interest income	<u>\$ 2,346,622</u>
Total income	<u>2,346,622</u>

EXPENSES:

Employee compensation and benefits	337,349
Other operating costs	239,143
Non-recurring costs	146,945
Occupancy	84,823
Depreciation	23,292
Other	<u>97,951</u>
Total expenses	<u>929,503</u>

EXCESS OF INCOME OVER EXPENSES

	1,417,119
Grants disbursed	(525,000)
Grants payable (Note 5)	<u>(1,200,000)</u>

NET DECREASE IN UNRESTRICTED NET ASSETS

\$ (307,881)

CHANGES IN PERMANENTLY RESTRICTED NET ASSETS:

Grants received	<u>80,000,000</u>
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INCREASE IN PERMANENTLY RESTRICTED NET ASSETS

\$ 80,000,000

INCREASE IN NET ASSETS (NOTE 5)

\$ 79,692,119

The accompanying notes are an integral part of this statement.

STATEMENT OF CASH FLOWS

For the period from inception (August 11, 1999) through September 30, 2000

CASH FLOWS FROM OPERATING ACTIVITIES:

Increase in net assets	<u>\$ 79,692,119</u>
Adjustments to reconcile increase in net assets to net cash provided by operating activities:	
Increase in permanently restricted net assets	(80,000,000)
Depreciation	23,292
Changes in operating assets and liabilities:	
Increase in accrued interest receivable	(749,117)
Increase in prepaid and other	(16,986)
Increase in liabilities	<u>1,336,525</u>
Net cash provided by operating activities	<u>285,833</u>

CASH FLOWS FROM INVESTING ACTIVITIES:

Endowment Fund investment portfolio activity:	
Sales of debt investments	31,447,733
Purchases of debt investments	(71,537,770)
Purchases of fixed assets	<u>(123,079)</u>
Net cash used by investing activities	<u>(40,213,116)</u>

CASH FLOWS FROM FINANCING ACTIVITIES:

Proceeds of permanently restricted grant contributions received	<u>80,000,000</u>
Net cash provided by financing activities	<u>80,000,000</u>

EFFECT OF EXCHANGE RATE CHANGES EQUIVALENTS

	<u>8,209</u>
Net increase in cash and cash equivalents	40,080,926

CASH AND CASH EQUIVALENTS, August 11, 1999 (inception)

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CASH AND CASH EQUIVALENTS, September 30, 2000

\$ 40,080,926

The accompanying notes are an integral part of this statement.

NOTES TO FINANCIAL STATEMENTS

As of September 30, 2000

1. ORGANIZATION

The Polish-American Freedom Foundation (the “Foundation”) is an U.S. not-for-profit corporation established on August 11, 1999 pursuant to an agreement between the Polish-American Enterprise Fund (the “Fund”) and the U.S. Government. The Foundation was created to advance the purposes of the Support for East European Democracy Act of 1989 by building upon the successful assistance programs and sound practices established by the Fund and to undertake other developmental initiatives designed to solidify Poland’s successful transition to democracy and free markets.

With the permission of the Minister of Foreign Affairs of Poland, the Foundation has opened a Representative Office in Poland whose purpose is to engage in activities to promote the Foundation and to provide information and consultation to the Foundation with respect to its activities.

2. BASIS OF PRESENTATION

In accordance with accounting principles generally accepted in the United States for not-for-profit organizations, the Foundation is required to report information regarding its financial position and activities according to the following classes of net assets:

Permanently restricted net assets are those that may never be spent by the Foundation. As of September 30, 2000 the Foundation had \$80 million of permanently restricted net assets.

Unrestricted net assets are the net assets of the Foundation that are not permanently restricted. Unrestricted net assets are expendable by the Foundation for operating costs and grants. As of September 30, 2000 the Foundation had \$(299,672) of unrestricted net assets (see note 5).

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Use of Estimates

The preparation of the financial statements in conformity with accounting principles generally accepted in the United States requires management to make estimates and assumptions that affect the amounts reported in the financial statements and related notes. Actual results could differ from those estimates.

Investments

U.S. Government agency obligations and corporate commercial paper are carried at fair market value in the accompanying statement of financial position.

Cash and Cash Equivalents

For purposes of the statement of cash flows, the Foundation considers all highly liquid financial instruments with a maturity of three months or less to be cash equivalents.

Grants

Grants are recorded as Grants payable when the grant is approved in accordance with policies set by the Board of Directors, negotiations have been finalized with the grantee and the grant agreement has been signed between the parties.

Translation of Foreign Currency

The functional currency of the Polish representative office is the Polish zloty. Expenses transacted in Polish zlotys are translated into U.S. dollars at the average exchange rates in effect during the period. There were no revenues

transacted in Polish zlotys. Polish zloty denominated assets (fixed assets, rent deposit) are translated at historical exchange rates. There were no investments denominated in Polish zloty. Polish zloty denominated liabilities (accrued expenses) are translated at the year-end spot currency rate.

Translation differences are not reported in the statement of activities but are charged directly to net assets.

Donated Services

Members of the Board donate significant amounts of their time to the Foundation's programs. The Foundation's directors receive no compensation or fees for serving as directors. No amounts have been reflected in the accompanying financial statements for such donated services, inasmuch as no objective basis is available to measure the value of such services. The Foundation's Polish directors receive a fee for providing advice and assistance to the Foundation. For the period from inception (August 11, 1999) through September 30, 2000 the total fee paid to all Polish directors amounted to \$20,000.

Depreciation and Amortization

Computer hardware, furniture, equipment and automobiles are depreciated on a straight-line basis over their estimated useful lives. Leasehold improvements are amortized on a straight-line basis over the lesser of their useful lives or the term of the lease.

Other Operating and Non-recurring expenses

Professional services, expenses of Board of Directors meetings and expenses for travel, lodging, meals, etc., incurred in connection with the Foundation's operations are classified as other operating expenses. Legal, accounting and other costs incurred to prepare the Foundation to begin operations are classified as non-recurring expenses.

4. POLISH-AMERICAN ENTERPRISE FUND GRANT

Pursuant to an agreement signed in 1999 between the Fund and the U.S. Government and in consultation with the Government of Poland, the U.S. Government has decided to return \$120 million of the Fund's assets to the U.S. Treasury and to use substantially all of the balance to endow the Foundation (the "Endowment Amount").

According to the terms of the grant agreement between the Fund and the Foundation (the "Grant Agreement") the Foundation may finance its activities from interest on or other earnings generated by the Endowment Amount.

The Grant Agreement prohibits the disbursement of any part of the Endowment Amount received from the Fund therefore the Endowment Amount is classified as a permanently restricted net asset.

According to the terms of the Grant Agreement, the Fund has the right to require repayment or transfer of all or any portion of the Endowment Amount paid or transferred to the Foundation together with any interest thereon if there exists foreign policy grounds described in Section 801 of the SEED Act.

Through September 30, 2000 the Foundation had received the following Endowment Amounts from the Fund (dollars in millions):

October 8, 1999	\$ 40.0
September 29, 2000	<u>40.0</u>
	\$ 80.0

5. NET ASSETS AND GRANTS PAYABLE

In accordance with accounting principles generally accepted in the United States, the Foundation is required to classify a grant as a grant payable at the time the grant agreement is signed. Grants payable are required to be recorded as a reduction of net assets and a liability of the Foundation. For purposes of compliance with the Grant Agreement, this reduction in net assets is not considered a disbursement of any part of the Endowment Amount. At September 30, 2000

the Foundation had \$1.2 million in Grants payable. In the normal course of operations this amount will be disbursed to grantees from future income only to the extent that no part of the Endowment Amount is spent.

In addition, as of September 30, 2000 the Foundation had approved 7 grants totaling \$2.5 million that, as of that date, were subject to the completion of grant negotiations and the signing of grant agreements to the satisfaction of all parties. Subsequent to September 30, 2000 the Foundation signed 3 of these grant agreements totaling \$930,000.

6. INVESTMENTS AND CASH AND CASH EQUIVALENTS

The Foundation has engaged a professional investment manager who makes all investment decisions according to the Foundation's investment policy and monitors the Foundation's investments.

As of September 30, 2000, the Foundation's cash and cash equivalents consisted of \$30.2 million in cash (principally money market funds) that was deposited at one high quality U.S. financial institution and \$9.9 million in high quality U.S. corporate commercial paper that had maturities, when purchased, of less than 90 days.

The Foundation's investment manager invests in multiple issuers of corporate commercial paper investments and multiple issues of U.S. Government Agency Bonds. As of September 30, 2000, the Foundation's investments in U.S. Government Agency Bonds amounting to \$ 40.1 million had maturities of less than one year.

7. FIXED ASSETS

As of September 30, 2000, fixed assets consisted of:

Computer equipment and software	\$ 35,631
Furniture and equipment	50,058
Automobiles	36,444
Leasehold improvements	<u>946</u>
	123,079
Less – Accumulated depreciation	<u>(23,292)</u>
Net book value	<u>\$ 99,787</u>

8. LEASE COMMITMENTS

The Foundation is committed to make minimum annual rental payments for office space under an operating lease entered into in December 1999, which expires as of December 31, 2002. Lease commitments for the fiscal years subsequent to September 30, 2000 are approximately \$103,000 in 2001, \$103,000 in 2002 and \$25,000 in 2003.

9. TAX STATUS

United States

The Foundation is exempt from U.S. Federal income taxes under Section 501(c)(3) of the U.S. Internal Revenue Code (the "Code"), and has been classified as an organization that is not private a foundation as defined in Section 509(a)(1) of the Code. In addition, the Foundation is exempt from payments of state and local income taxes.

Poland

The Foundation's Representative Office in Poland is not subject to Polish corporate income taxation.

REPORT OF INDEPENDENT PUBLIC ACCOUNTANTS

To the Board of Directors of Polish-American Freedom Foundation:

We have audited the accompanying statement of financial position of Polish-American Freedom Foundation as of September 30, 2000, and the related statements of activities and cash flows for the period from inception (August 11, 1999) through September 30, 2000. These financial statements are the responsibility of the Foundation's management. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audit in accordance with auditing standards generally accepted in the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Polish-American Freedom Foundation as of September 30, 2000, the results of its activities and its cash flows for the period from inception (August 11, 1999) through September 30, 2000 in conformity with accounting principles generally accepted in the United States.

Arthur Andersen LLP

New York, November 23, 2000

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U.S. Ambassador to Poland, ex-officio participating in the work of the Board of Directors

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C. Douglas Ades

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Program Director

Jacek Michałowski

Program Director

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