

*I*n 1989 the United States Congress made a decision to establish the Polish-American Enterprise Fund which became an important force in the development of a market economy in Poland during the next ten years. Because of the Fund's success, it was possible to return half of the original U.S. government grant to the U.S. Treasury, as well as to establish the Polish-American Freedom Foundation. In 2000, the Foundation opened its Representative Office in Poland and began operations. Its mission is to strengthen civil society, democracy and the market economy in Poland, including efforts to equalize opportunities for individual and social development as well as to support the transformation processes in other countries of Central and Eastern Europe.

During the first two years, the Foundation's programs covered four areas of activity: initiatives in the field of education, development of local communities, citizen in a democratic state of law, and the sharing of Polish transformation experiences. Most PAFF programs are managed by experienced non-governmental organizations, which cooperate closely with the Foundation. Independent selection committees make decisions to provide the funding for specific projects submitted under grant-giving programs of the Foundation.

The Polish-American Freedom Foundation is financing its operation primarily with revenues generated by its endowment, the source of which are proceeds from the completed capital projects and programs of the Polish-American Enterprise Fund; eventually the endowment should total \$180-200 million. The Fund has transferred \$137 million to the Foundation's endowment fund to date.

Table of Contents

Letter from the PAFF Leadership	2
Three Years of the Foundation's Mission	4
Facts and Figures 2000-2002	14
The Foundation's Programs 2000-2002	16
Report of Independent Auditors	18
Financial Statements	19
Notes to Financial Statements	22
Board of Directors	26
Management and Staff	27

Letter from the PAFF Leadership

It has been nearly three years since the Polish-American Foundation began its activity. We are pleased with the Foundation's achievements during this relatively short period of time, and also with the valuable experience we have gained that should provide a strong basis for our future efforts. The Foundation's activities to date include 20 programs in four thematic fields. The aggregate amount of grants since inception have totaled over \$9 million. They have supported the initiatives of nearly 800 non-governmental organizations and educational institutions, and provided more than 2,700 scholarships. Our activity follows the Foundation's mission – to support changes initiated in Poland in 1989, and to share the Polish transformation experiences with other countries of Central and Eastern Europe. Programs to fulfill our mission in Poland vary in forms, but they are focused on two goals: to equalize educational opportunities, and to activate and reinforce citizens' energy in areas suffering from difficult problems – mainly in villages and small towns.

We are currently reviewing the past three-years activities with the aim of making our programs even more effective and responsive to emerging social needs. We realize that our resources are modest, when compared with the needs, and therefore are dedicated to ensuring that they are used as efficiently as possible. Consequently, we are particularly focusing on activities that have the potential to be replicated and, when implemented on a broad scale, can bring about truly significant change.

In 2002 we made grants of over four million dollars. Despite a decline in the current market value of our endowment, which was considerably less than the average for U.S. foundations, the Board of Directors made the decision to maintain this level of funding in the year 2003. We believe this is appropriate in view of expected additional capital contributions derived from the continuing liquidation of the Polish-American Enterprise Fund and in light of particularly pressing social circumstances within Poland. As a result of these contributions we anticipate the endowment will eventually reach \$200 million.

With respect to the Foundation's programmatic activity, in 2002 we continued to emphasize educational initiatives, particularly those that serve to equalize opportunities, and modernize this critical sector. Last May, we completed the "Computer for a Teacher" Program that enabled 3,000 teachers from rural areas and small towns to purchase their own PCs. The Program was the first to undergo external evaluation. This assessment confirmed the effectiveness of the Program, and stimulated development of a new initiative – the "Computer Long Distance Training" Program. By the end of 2002, this new pilot program involved nearly 2,000 teachers. The "Computer Long Distance Training" is closely linked with another PAFF undertaking, the Interkl@sa Portal, currently the largest interactive educational website in Poland. Its resources are regularly used by thousands of students, teachers and others in educational institutions. We have continued our "Leveling the Playing Field" Program aimed at equalizing educational opportunities for youth from neglected areas of Poland. Reaching youth from these areas was also the concept underlying a new initiative in 2002 – the "Bridge Scholarships" Program. This Program was conducted jointly with the Agricultural Property Agency of the State Treasury, The National Bank of Poland, and a coalition of 21 local non-governmental organizations. Together, the partners have raised funds exceeding one million dollars, enabling 1,052 first year university-level scholarships. These were awarded to high school alumni from rural areas, mainly from former state-owned, large farming estates.

Two other pilot initiatives, launched in 2000, reached their final stage of implementation. The "Undoing Unemployment" Program has helped more than 1,000 individuals, mainly youth and professional groups threatened with structural unemployment. Almost a half of participants have already used their newly-acquired knowledge to find jobs or to begin their own business activity. Our current task is to have this experience replicated on a larger scale. Through our second pilot initiative, the "Village in Transition"

Program, we have sought to reach communities that are in more difficult circumstances than those targeted by our other undertakings, to help them develop specific projects that respond to important local needs. At the same time, this Program has created a forum for regular cooperation among non-governmental organizations working for the benefit of rural areas.

We have been gratified by the success of our two programs to share Polish experiences with our neighboring countries. In the academic year 2002/03, 41 young leaders from Ukraine, Belarus and Russia (District of Kaliningrad) began study at Polish universities under the Lane Kirkland Scholarship Program. Thirty other Kirkland Fellows left Poland in the summer after spending two semesters in Warsaw, Poznan, Katowice and Lublin. Additionally, Polish non-governmental organizations continued to implement several dozen projects in countries of Central and Eastern Europe, thanks to financial support provided by the “Region in Transition” Program (RITA).

Because of the historic conclusion of negotiations with European Union at the Copenhagen Summit in December 2002, the prospect of European integration has now become a reality for Poland. This opens new perspectives for the Poles – both new opportunities and challenges. To the extent possible with our limited resources, the Foundation will seek to support the integration process, in our new “EURO-NGO” Program, aimed at assisting non-governmental organizations to operate in new conditions, following Poland’s accession to the EU, mainly preparing them to use effectively EU funds.

The year 2002 began sadly for us with the loss of John H. D’Arms, member of the PAFF Board of Directors, who died in January at the age of 67. John served with us from the outset as a preeminent scholar and widely respected educator, his counsel and friendship have been profoundly appreciated. We shall miss him.

We would like to thank all those who have contributed to our efforts during the year, in particular our Program Managers, whose initiative and high standards have been unflinching. We would also like to thank, in a very special way, the members of our Board of Directors. Their knowledge and experience have provided invaluable support in the development of the Foundation since its inception.



John P. Birkelund
Chairman of the Board of Directors



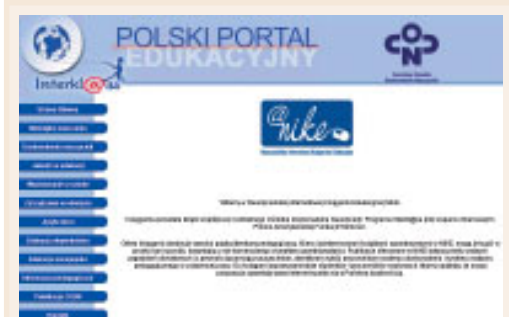
Jerzy Koźmiński
President and Chief Executive Officer

New York / Warsaw, April 2003

Three Years of the Foundation's Mission

INITIATIVES IN EDUCATION

► The “Education on the Internet – Polish Educational Portal Interkl@sa” Program



► www.interklasa.pl

The offer of the Teachers' Internet Education Library, developed in the Portal, currently includes 30 publications, such as those on methodology of teaching, management in the educational sector, foreign languages tuition and European education.

One of the largest in Poland, non-commercial, and currently the largest educational portal, the www.interklasa.pl, has been operating since 2001. It is a joint undertaking by the Polish-American Freedom Foundation and the Interkl@sa Initiative, created on the basis of modern technological infrastructure, provided by the Poznań-based Super-Computer Network Center (Poznańskie Centrum Superkomputerowo-Sieciowe).

The Portal provides its service to schools, teachers, students and their parents, as well as to educational institutions and non-governmental organizations. Its abundant offerings are being added to on a regular basis. They include topical services, lessons' scenarios, materials to teach different topics, information about training methodology and a news service, free e-mail accounts, www.sites and numerous chat groups. Among the new resources are: the “Interactive Schools' Map” with over 26,000 educational centers, the “Multimedia Library” with 81 educational programs, and the Teachers' Internet Educational Library (www.nike.interklasa.pl), developed in collaboration with the National Center for Teachers' Education.

Thanks to the fact that two popular educational services, “Eduseek” and “6plus” resources were obtained in 2002, www.interklasa.pl has become the leading educational portal in Poland, regularly visited by several thousand registered users. The sign of its popularity is the number of ‘hits’, being close to 30 million in December 2002 alone.

- The Foundation's grant: \$175,000
- Program Manager: The Foundation for Economic Education (Fundacja Edukacji Ekonomicznej)

► The “Computer for a Teacher” Program

We have completed the two-year “Computer for a Teacher” Program, the objective of which was to facilitate junior high-school teachers from rural areas and small towns to purchase PCs for their personal use under a preferential installment scheme. The interest on the loans was covered by PAFF. The Program, implemented in collaboration with the National Foundation for Computer Literacy, raised great interest among teachers; 3,000 individuals took advantage of the offer.

The “Computer for a Teacher” was the first PAFF Program to become subject to an independent, external evaluation. The results of the survey carried out by the “Pentor” Institute confirmed the fact that the purchase of computers enabled teachers to be better prepared to work with the youth, and that it encouraged them to use the educational Internet resources in general, and those of the Interkl@sa Portal in particular. Those surveyed positively evaluated the course of the Program and expressed their interest in training to enhance their use of computers at school and in their own learning process.

The cooperation developed among companies providing loans, distributors of hardware and organizations specialized in computer education is a valuable model that can be replicated in other communities.

- The Foundation's grant: \$390,000
- Program Manager: The National Foundation for Computer Literacy (Ogólnopolska Fundacja Edukacji Komputerowej)

► The “Computer Long Distance Training” Program

The Program, initiated in September 2002, is a unique undertaking to improve teachers' knowledge and skills by providing free distance computer training via Internet.

During its pilot stage, the Program was addressed to the participants of the recently completed “Computer for a Teacher” Program and to teachers taking part in the training under the Interkl@sa Initiative.

The Program consists of two modules: distance training through a dedicated service on the Interkl@sa Portal (www.kurs.interklasa.pl), and workshops organized in venues close to the respective trainees' groups' residences. The training subject content includes, among other things, the knowledge of mechanisms to use and develop www. sites, presentations, spreadsheets, as well as the development of tools to evaluate the knowledge acquired by the students (tests, quizzes). The training course is completed by an exam and a certificate that is recognized by the Ministry of National Education and Sports. All those trainees who successfully pass the final test will have the cost of Internet connection partly refunded by PAFF.



► www.kurs.interklasa.pl

Thanks to “Computer Long Distance Training” courses, teachers can learn about how to develop interesting multimedia presentations that can be used in the work with students.

By the end of 2002, over 2,000 teachers received invitations to take part in the Program, together with passwords to be able to access the www.kurs.interklasa.pl site; the ultimate target is 3,000 teachers.

- The Foundation's grant: \$180,000
- Program Manager: The National Foundation for Computer Literacy (Ogólnopolska Fundacja Edukacji Komputerowej)

► The “English Teaching” Program

The second edition of the Program, initiated in 2002 is once again attracting interest. Its objective is to equalize educational opportunities of children and young people from rural areas and small towns in the field of English language learning. Two modules were implemented under the Program in 2002: the Small Grants and “Teaching English Teachers”. The third module, i.e. “Follow me” has been developed for implementation. It is a continuation and extension of selected, model projects funded under the previous edition of the Program.

Out of 41 best projects financed under the Small Grants module, the Anglo-Saxon Culture and the English Language Amateurs' Clubs prevail. The Clubs' operation involves meetings, discussions, reading of literature, sessions using computers, as well as group viewing and commenting on movies in English. English libraries were established in most of the Clubs and theatre groups of performers are also active there. Several projects plan to carry out literature competitions for the best brochure presenting a theatre play. Activities carried out under the projects have involved approx. 7,000 students and teachers.

Additionally, more than 150 English language teachers from rural areas and small towns will take part in free training courses. With the training, they will improve their skills in what teaching methodology, running integration courses with the youth, and using the Internet in the training process.

The Program, and its “Teaching English Teachers” module in particular, is being implemented in collaboration with the Kosciuszko Foundation.

- The Foundation's grant: \$263,000
- Program Manager: The “Nida” Development Foundation (Nidzicka Fundacja Rozwoju “Nida”)

► The “Training for Health Care Managers” Program

22 educational centers qualified for the Program, which delivered training in the field of health care management. Those centers that submitted the most interesting training improvement plans, received subsidies to help them implement their projects. Also, out of 300 applications, nearly a 100 scholarships were granted to physicians from rural areas and small towns to undertake post-diploma studies.



► A training conference about health service in large metropolitan areas was organized in October. Top experts in the field from New York City, Berlin, Warsaw took part in the Conference, held at the Warsaw University Library Building. Henry Wejnert presented the way health service is organized and funded in NYC, while Reinhard Ross and Uwe Reinicke presented the way it is organized in Berlin.

In 2002, besides continuation the effort to improve the post-diploma studies course and its public accreditation, the Program's training system was enriched by experiences from modern medical care systems in other countries. The vehicles used to achieve this were two conferences with several hundred physicians and post-diploma students in health service management participating.

During the first one, held in Warsaw in May 2002, representatives of European Health Care Managers Forum from Denmark, the Netherlands, the United Kingdom, Portugal, and Polish participants of training courses for managers in France, presented western models of health sector managers' training. During the conference a panel discussion was held about opportunities and problems for the Polish health care system in relation to Poland's joining the EU.

A conference to summarize the Program's achievements is being organized.

- The Foundation's grant: \$200,000
- Program Manager: The Society of Health Care Managers (*Stowarzyszenie Menedżerów Opieki Zdrowotnej*)

► The “Learning Schools” Program (LES)

The objective of this Program, implemented since 2001 by the Center for Citizenship Education, is to develop and disseminate model to improve the quality of schools' operation throughout the Polish educational sector, using experiences of non-governmental organizations and based on solutions tested abroad. Thanks to training courses for teachers, schools are implementing new methods to define tasks, assign responsibility to have them accomplished, and develop effective mechanisms to regularly monitor the results.

122 schools from all parts of Poland joined the Program in 2002, both from large cities, including Gdańsk, Olsztyn and Rzeszów, and smaller ones, such as Czaple, Terespol Pomorski, Poddębice or Wróblew. Program participants established the “Learning Schools Club”; a platform for cooperation and exchange of experiences. By the end of 2002, the Program was operating in 177 schools.

A group of 35 trainers was developed and they trained 965 teachers in 2002. 1,239 teachers were trained in total 719 of whom were from rural areas and small towns. They transferred their knowledge to over 5,000 of their colleagues. An Internet database with materials and tools was established, including didactic aids to support teachers in meeting “LES” standards in their everyday work (e.g. lessons' plans, questionnaires, methods to arrange the classroom space).

The “Learning Schools' Academy” is providing teachers with an rich offering of training packages that supplement regular activities under the “Learning Schools Club”.

In 2002, the “Learning Schools” Program provided inspiration and a basis for undertaking a mass, national “School with a Class” campaign. This was launched by the Center for Citizenship Education and “Gazeta Wyborcza” daily. Currently, over 4,500 schools take part in it. The campaign will help attract new schools from rural areas and small towns to “LES” Program.

- The Foundations grant: \$260,000
- Program Manager: Center for Citizenship Education (*Centrum Edukacji Obywatelskiej*)

► The “Management Education 2002” Program (MANED)

The Program is a continuation of a project initiated by the Polish-American Enterprise Fund in 1991, and implemented by the Educational Enterprise Foundation (EEF). Its objective is to support higher education in the field of economy and management through scholarships, publications, conferences, competitions and other initiatives undertaken to enhance access to and the quality of education. The Program priority in 2002 was to equalize educational opportunities for young people from rural areas and small towns, to enable them to meet the requirements of both national and international job market in future.


925 students from 46 private business schools, providing high quality education, obtained scholarships under the Program in 2001-2002. The number of scholarships granted by the Educational Enterprise Foundation is more than 20,000 since 1991. Also, 11 colleges/universities obtained special grants to buy new publications for their libraries. Two seminars on training quality and accreditation were organized; they have joined in the important government and civil effort to promote high quality educational institutions. The Educational Enterprise Foundation has continued its support of the participation of Polish student teams in the international Internet, “Global Internet Marketplace Competition”, where they traditionally score among the highest. Six, subsequent, subsidized books were published. They provide significant support to economy students, and are translations of classical economy literature.

Cooperating with academics from colleges/universities who provide education in economy and management, EEF organized or co-financed five conferences with over 500 participants. Two competitions for students of economy were carried out: “Enterprise and Management” and “My studies and the challenges of my future career”.

- The Foundation's grant: \$400,000
- Program Manager: Educational Enterprise Foundation (Fundacja Edukacyjna Przedsiębiorczości)

► The “Equal Opportunities” Program

The objective of this Program, initiated in 2001, was to support and to inspire local initiatives in rural areas and small towns aimed at equalizing educational opportunities for children and young people. Local non-governmental organizations, schools and other educational centers, and informal youth groups from all over Poland participated in the Program, undertaking activities aimed at junior high-school and high school students, as well as teachers and parents.



► A special round of the Program demonstrated ways to cope with the effects of a natural disaster and how to assist local communities. Experiences gathered provided the content for the “I am on a Bridge, i.e. How to Help a Child During the Flood” guidebook. The Publication (circulation: 2,000 copies), was sent to educational centers/schools and non-governmental organizations operating in areas suffering from the flood.

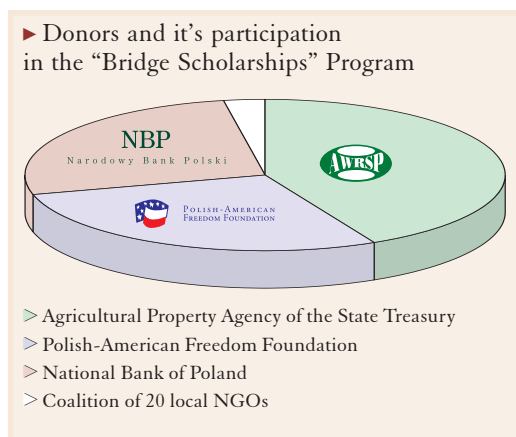
Thanks to three Program rounds 125 valuable initiatives were supported, with 75,000 individuals taking part. Over one-third are beneficiaries of a special round of the Program, implemented in areas suffering from the flood of 2001 (the voivodships: małopolskie, lubelskie, pomorskie, podkarpackie and świętokrzyskie).

The Program allowed young people to participate in various types of activities that developed their interests, made their learning more efficient, and helped them acquire skills useful both at school and in adult life. These included mainly computer training, language training, reading and journalism, designed both for talented young people as well as those having learning problems. Taking into account the substantial level of interest in the Program, the Foundation decided to continue it in 2003.

- The Foundation's grant: \$243,000
- Program Manager: Polish Children and Youth Foundation (Polska Fundacja Dzieci i Młodzieży)

► The “Bridge Scholarships” Program

The growing disparity in access to university studies between young people from rural areas and their counterparts from large cities is a serious social problem. Young people from villages, especially from former state-owned farming estates, account for a marginal share of all those studying in universities. Many talented young people do not even consider undertaking these studies because of the difficult financial condition of their families. The “Bridge Scholarships” Program is aimed at helping young people from those environments to go to university by providing scholarships for the first year of the studies.



The Program was addressed to areas requiring special support, mainly the youth from communities of former state-owned large farming estates, as well as those covered by local scholarship funds operating in rural areas and small towns.

3,100 individuals expressed their will to take part in the Program, and 45% of them passed entry exams to colleges/universities and obtained their students' books of registration of courses. 1,444 scholarship applications were submitted. Finally, 1,052 individuals who met the requirements were qualified to the Program.

Besides the Foundation, other partners co-funded the scholarships: Agriculture Property Agency of the State Treasury, the National Bank of Poland, and a coalition of 20 local non-governmental organizations cooperating with the Batory Foundation and the Academy for the Development of Philan-

thropy in Poland. Funds obtained from all the donors amounted to the three times the amount of the grant allocated by PAFF.

After the first year of the Program, all indications are that Bridge Scholarships provide an effective approach to assist youth from the neglected areas to continue their education.

During the pilot period of the Program's implementation, the Educational Enterprise Foundation, has developed model know-how that provides a solid basis for the Program's development in future.

- The Foundation's grant: \$245,000
- Program Manager: Educational Enterprise Foundation (Fundacja Edukacyjna Przedsiębiorczości)

SUPPORT FOR LOCAL COMMUNITIES

► The “Mutual Information Society” Program (MISANGO)

This professional information system on and for for non-governmental organizations and civil initiatives has been operating since 2001. It is the first of that kind in Poland and is also unique in Europe. It's important component is a non-profit Portal for NGOs (www.ngo.pl) regularly supplemented by new resources, including 57,000 records in total (among them, databases of Polish and international organizations, structural funds, job offers for volunteers) and a very popular newsletter, electronically already subscribed to by 1,000 users, and 30 topical services such as: legal, accounting, the European Union. Beginning in March 2002, the Portal also offered tools such as discussion forums, comments and a News Weekly “Wiadomości.ngo.pl”. Beginning from October 2002, the pilot “Group” service became available. It is an integrated package of several applications (a chat, calendar, ads, e-mail), which can be used for mutual exchange of information within a specific user group. The tool has created broad interest: by December 2002, approx. 1,000 users registered in chat groups, and over 50 virtual communities were registered.

The System also includes: the Informatory (in 2002 used by over 4,200 those interested), the info line 0-801-646-719 (nearly 1,800 over-the-phone pieces of advice), and brochures under the “It's Worth to Know More” series, published in 100,000 copies in total.

Professional research of non-governmental organizations was carried out under the Program in 2002, the result of which was the first statistical report about the third sector in Poland.

- ▶ The Foundation's grant: \$245,000
- ▶ Program Manager: Klon/Jawor Society (Stowarzyszenie Klon/Jawor)

▶ The "Act Locally II" Program

The objective of the second edition of the Program, implemented in 2000-2001, is to support civil initiatives that solve local problems and stimulate new aspirations among communities in rural areas and small towns.

The Program is implemented through three types of activity. The first one involves promotion of successful model solutions to social problems, developed during the first edition of the Program, to adapt them for other communities. The second is to stimulate citizens' activities through the implementation of 38 new projects in five voivodships being in extremely difficult social and economic condition (warmińsko-mazurskie, kujawsko-pomorskie, podkarpackie, łódzkie and świętokrzyskie). In the third pilot area of activity, three local organizations extended PAFF grants to support 51 local initiatives (out of 119 proposals), implemented in Biłgoraj, Leżajsk and Bystrzyca Kłodzka; each of those local grant competitions involved 56% PAFF funding, and the remainder was given by local donors.

The projects implemented under the Program included the following activities: to counteract unemployment, to stimulate the development of small enterprises, provide social services to marginalized groups (including the elderly and the handicapped), to equalize opportunities in access to education and culture, to improve public security, to preserve cultural heritage, to protect the natural environment, and to support the development of citizens' organizations. All the projects engage volunteers and provide at least 20% of the cost from local sources.

355 grant applications were submitted in total for all grant competitions under the "Act Locally" Program, of which 99 projects were supported. It is planned to complete the Program in mid-2003.

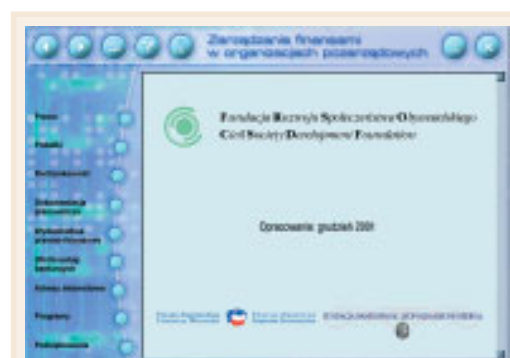
- ▶ The Foundation's grant: \$300,000
- ▶ Program Manager: The Academy for the Development of Philanthropy in Poland (Akademia Rozwoju Filantropii w Polsce)

▶ The "Financial Management for NGOs" Program

The Program, completed in 2002, was to improve financial management of non-governmental organizations.

The Program Manager assessed the educational needs of 500 non-governmental organizations. As a result training courses covering various areas were organized and easy-to-comprehend guidebooks for financial officers of the third sector were published. Nearly 300 individuals took part in 17 training sessions.

1,500 copies of free guidebooks covering legal and financial subjects were published; they presented a body of knowledge on financial management which takes into account the Polish reality in relation to non-governmental organizations. A dedicated web site on auditing non-governmental organizations was also developed (<http://free.ngo.pl/csdj/audyt/>).



- ▶ A CD-ROM with useful information in the area of law, finance, taxation, accountancy, and financial and accounting software, supplements the written materials.

Positive experiences from the Program and a clear demand expressed by the third sector made us decide to launch another edition of the Program in 2003 to be dedicated to computer training for non-governmental organizations' accountants.

PAFF's partner in co-funding the Program is the Leopold Kronenberg Banking Foundation.

- ▶ The Foundation's grant: \$90,000
- ▶ Program Manager: The Civil Society Development Foundation (Fundacja Rozwoju Społeczeństwa Obywatelskiego)

► The “Village in Transition” Program (VITA)

The “VITA” Program, implemented in 2001-2002, was to stimulate grass-roots civil initiatives in relatively inactive rural communities, and to initiate regular exchange of information and experiences between non-governmental organizations working for the benefit of rural areas.

The core part of the Program consisted of three undertakings to stimulate activity among local communities and was implemented by four non-governmental organizations in selected regions of Poland. Those included a joint undertaking by the Foundation for the Development of Polish Agriculture and the Ideal Gmina Foundation, implemented in the powiats of Mława and Płock; an undertaking implemented by the Foundation of Social and Economic Initiatives in the powiats of Maków and Kętrzyn, and an undertaking implemented by the Foundation Partnership for Environment in Bieszczady, Polesie and in Central and Western Pomerania.

The activities were carried out in three stages. The information stage targeted over 1,500 individuals in 266 local communities. Then, 110 training courses followed, adjusted to the current needs of local communities, with nearly 3,000 participants representing 227 communities from 112 gminas. With the support of expert advisors 63 projects were developed, aimed mainly at inspiring local milieus to independently solve their problems and overcome barriers. The beneficiaries' own contributions exceeded the total grants' amount. All the projects are being continued, using the tools and structures developed under the Program.

A mechanism was also developed to exchange experiences between organizations and institutions operating for the benefit of rural areas. The “Atlas of Rural Initiatives” with a presentation of 120 model local projects that can be replicated in other regions, serves this purpose.

- The Foundation's grant: \$500,000
- Program Manager: The Rural Development Foundation (Fundacja Wspomagania Wsi)

► The “Undoing Unemployment” Program

The objective of this pilot Program, implemented in 2000-2002, was to stimulate grass-roots initiatives to encourage local institutions to actively fight unemployment through outplacement, a methodology that is used to change attitudes of those unemployed or threatened with unemployment.



► Local authorities, employers, professional and citizens' organizations were invited to cooperate with individual projects. This led to the establishment of local pacts to counteract unemployment and its negative effects. Experiences gathered during the process were included in a guidebook as model activities. The guidebook includes presentations of tools and methods applied while implementing the projects.

The Program involved 1,165 individuals in five projects, addressed to diverse professional and social groups – all threatened with structural unemployment, namely: Polish State Railroads' workers, nurses and midwives, those from rural areas, and young people looking

for their first jobs. Program participants received psychological and legal assistance and were given the opportunity to improve their skills. Each Program beneficiary also used the job exchange, supported by a dedicated database with 3,000 job offers.

The results of the Program went beyond original expectations; soon afterwards, nearly a half of the participants found new jobs, or created them by becoming self-employed, while, 995 (over 85%) of the participants developed new skills that increased their chances in the job market.

- The Foundation's grant: \$550,000
- Program Manager: The Enterprise Development Foundation in Suwałki (Fundacja Rozwoju Przedsiębiorczości w Suwałkach)

► The “Citizens and Local Government” Program

The Program objective is to support initiatives undertaken by non-governmental organizations which enhance the development of lasting, transparent mechanisms of their cooperation with local government in rural areas and small towns in the field of: exchange of information, needs assessment in local communities, consulting about local government decisions, joint projects undertaken in order to solve local problems, and cooperation agreements that involve non-financial assistance and outsourcing off-services.

The first stage of the Program involved an analysis of nine earlier assistance programs, implemented by various organizations and institutions, aimed at the improvement of cooperation between local authorities and non-governmental organizations. The material developed as a result (available on: www.frdl.org.pl), includes a list of 10 publications and 32 training and advisory institutions as well as several examples of models of cooperation between non-governmental organizations and local authorities at the gmina, powiat and voivodship level.

The second stage of the Program, planned for 2003, involves the subsidizing of approximately 20 annual citizens' projects that are to accomplish the Program objectives according to the needs of their respective local communities and in collaboration with the local authorities. Projects will be supported that will introduce transparent decision-making procedures in local government and increased participation by organizations and citizen groups in joint-decisions about issues concerning a given local community and thus resulting in better satisfaction of the residents' needs as well as supporting the fight against corruption at the local level.

- ▶ The Foundation's grant: \$255,000
- ▶ Program Manager: Foundation in Support of Local Democracy (Fundacja Rozwoju Demokracji Lokalnej)

▶ The "Pro Publico Bono" Award

The fourth edition of the Nationwide "Pro Publico Bono" Competition for the Best Civil Initiative, under the auspices of the Polish Ombudsman, took place in 2002. As in the two previous rounds, the Polish-American Freedom Foundation financed the prizes and provided for the operating expenses.

The Competition is aimed at finding and giving awards to the most valuable civil initiatives with special emphasis put on cooperation with the local government within the field of: education, culture and national heritage, health protection, social and charitable assistance, development of the environment and of the region, and also social diplomacy and European integration, at the national, regional and local levels.



▶ Winners of Round Four of the Competition

301 organizations competed for prizes during round four of the Competition. Awards were given to 20 of them during a ceremony in Kraków on 11th November 2002. Main prizes were awarded to: the "Silesian Town" Foundation in Support of Children (Fundacja na Rzecz Dzieci "Miasteczko Śląskie") – under local initiatives' category and the Karta Center Foundation (Fundacja Ośrodek Karta) – under national initiatives' category. The awarded organizations declared that they would use their prizes to continue their activity, to implement new projects or to finance the purchase of new equipment and modernize premises used for statutory purposes.

In 2002, the Competition was accompanied by activities to integrate its past winners, using, among other vehicles, the Internet (www.propublicobono.pl) chat group, topical seminars and meetings with local government officials in those communities that had been awarded during earlier rounds of the Competition.

- ▶ The Foundation's grant: \$160,000
- ▶ Program Manager: The "Pro Publico Bono" Competition Foundation (Fundacja Konkurs "Pro Publico Bono")

CITIZEN IN A DEMOCRATIC STATE OF LAW

▶ The "Supporting Legal Reforms – Computer Training" Program

In an effort to support Polish reforms, the Foundation initiated a Program in 2001 to increase efficiency of operation among those working for judiciary institutions through training in the use of modern computer techniques. The Program was implemented by the Foundation Center for Judges Training "Iustitia".

In addition to the Training Center in Warsaw, established previously by the "Iustitia" Foundation (with the American Bar Association), four new centers were opened thanks to PAFF's grant: in Białystok, Wrocław,

Szczecin and Kraków. The centers offer computer training to learn how to use basic software that is useful to judges and judicial administrative staff. In 2001-2002, 1,314 participants took part in 112 training courses, 726 of whom were judges and 588 were administrative employees of the judicial system. A large percentage of the participants were from courts of justice located outside large metropolitan areas.

Thanks to the assistance of the Ministry of Justice and cooperation with sector publishers plus software and hardware manufacturers, the Program managed to attract additional funding – exceeding the amount of PAFF's grant.

The key achievement of the Program was the development of an efficient computer training center model. The new training centers will be able to continue their training activity, with the Ministry of Justice's support. Their experiences can also be used by other institutions willing to undertake similar initiatives.

A conference to summarize the results of the Program will be held in Kraków in May 2003.

- ▶ The Foundation's grant: \$190,000
- ▶ Program Manager: The Foundation Center for Judges Training "Iustitia" (Fundacja Centrum Szkolenia Sędziów Polskich "Iustitia")

▶ The "Citizen and Law" Program

The objective of the Program (to be implemented by mid-2003) is to support the development and offering of citizen advice and legal information to the disadvantaged, especially in local communities and small towns.

The scope and the quality of this type of advice is to increase, thanks to reinforcing selected non-governmental organizations and improving skills of their staff. The Program promotes the idea of free advice provided by NGOs, local government officials, lawyers and law students.

The Program is being implemented through financial support to 22 projects selected through competition (from the 192 submitted), which offer model solutions, stimulate civil energy and convey an educational message. The awarded projects (implemented all over Poland, including towns such as: Starachowice, Konin, Łomża, Nowy Sącz, or Kraków), are addressed to diverse social groups: victims of violence, the unemployed, patients of psychiatric institutions, the Roma, members of dysfunctional families, and the handicapped.

Additionally, within the framework of the Program and in collaboration with the Association of Citizen Advice Bureaus (Związek Biur Porad Obywatelskich), the Non-governmental Advice Forum (Pozarządowa Platforma Poradnicza) was established, the purpose of which is to exchange information between organizations that provide this type of advice. The activity undertaken by the Forum has already resulted in the establishment of a web site and information service (www.platformaporadnicza.ngo.pl), and developed cooperation between those organizations in offering their services to diverse social groups.

- ▶ The Foundation's grant: \$352,000
- ▶ Program Manager: Institute of Public Affairs (Instytut Spraw Publicznych)

SHARING OF POLISH EXPERIENCES IN TRANSFORMATION

▶ The Lane Kirkland Scholarship Program

The Foundation launched a long-term Program in 2000 to share the Polish experience of system transformation by providing scholarships for leaders from countries of Central and Eastern Europe, willing to act for the development of democracy, market economy and civil society.

42 visiting fellows participated in the Program during the academic years 2000/2001 and 2001/02. In 2002/03, 41 fellows joined the Program. They came from: Ukraine (19), Belarus (13), Slovakia (4), Lithuania (3) and Russia – the Kaliningrad District (2).

The Kirkland visiting fellows, selected each year through a three-stage competition, are active young people from public administration, academics, businessmen, representatives of non-governmental organizations, the media and politics. The Program gives them an opportunity to participate in individually tailored, two-semester post-diploma studies at Polish universities as well as in internships in various institutions.



► On 15th July 2002, the Closing Ceremony of the second year of the Lane Kirkland Scholarship Program was held in the Senate Room of Warsaw University. Mr. Marek Borowski, Speaker of the Polish Parliament took part in the ceremony, and Mrs. Irene Kirkland, the wife of the late Patron of the Program was the Guest of Honor.

The group of 2001/02 visiting fellows demonstrated a high level of scientific/research activity. Besides diploma theses that they were obliged to write as scholarship holders, many (in collaboration with their Polish tutors) published articles in scientific magazines. Having returned home, they continue their careers, using the knowledge and contacts established in Poland. Some are invited to lecture at universities where they worked during the scholarship, while others implement joint projects with Polish partners. Regular contacts will be maintained with all of them.

- The Foundation's grant: \$610,000
- Program Manager: Polish-U.S. Fulbright Commission (Polsko-Amerykańska Komisja Fulbrighta)

► The "Region in Transition" Program (RITA)

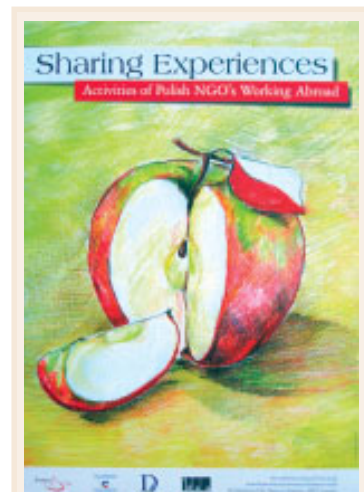
The Program's second edition was carried out in 2002. It was addressed to Polish non-governmental organizations and educational institutions that implement or intend to implement projects to share Polish experiences of social and economic transformation with other countries of Central and Eastern Europe. The Program supports and initiates projects undertaken by Polish organizations together with partners from the Region as well as helps exchange information and experiences among Polish NGOs that are interested in activities in Central and Eastern Europe.

Cooperation with partners from Eastern Ukraine and the Russian Kaliningrad District was a priority in 2002. It was a new approach to introduce small grants for local organizations implementing trans-border projects. Those included some very valuable initiatives, concentrating mainly on solving local social problems.

269 proposals were sent to the grants competition, of which nearly two-thirds were from organizations that had not participated during the first round of the Program in 2001. 69 projects were financed, which aimed at cooperation with partners in 20 countries.

Atlases of non-governmental organizations in the Kaliningrad District, in Ukraine and Belarus, were published under the Program. In collaboration with the "Mutual Information Society" database of foreign non-governmental organizations (over 240 records) and the database with information about the activity of Polish NGOs in Central and Eastern Europe (nearly 550 records) was enlarged.

- The Foundation's grant: \$600,000
- Program Manager: Education for Democracy Foundation (Fundacja Edukacja dla Demokracji)



► Funds from the Program were used to finance the "Sharing Experiences" exhibition about the activity of Polish non-governmental organizations, presented at the 12th Economic Forum in Krynica.

Facts and Figures 2000-2002

...modern technologies

- ▶ **Polish Educational Portal "Interkl@sa" www.interkasa.pl**
– largest Web educational resources in Poland: topical services, lessons' scenarios, news service, free e-mail accounts, educational library, Internet bookstore: **3500** registered users, over **40 million** "hits"
- ▶ **3000** beneficiaries of the **"Computer for a Teacher"** Program, **1000** e-mail accounts
- ▶ **2000** teachers from small cities and villages has been taking part in the **"Computer Long Distance Training"** Program.
- ▶ **The Non-governmental Organizations Portal www.ngo.pl**
– the unique undertaking in Europe: **16** databases – **57 000** records, news service, **1000** subscribers of the newsletter, **30** topical services, discussion forums, the pilot intranet "Group" service
- ▶ **4** computer training centers for judges and judicial administration staff: **112** training courses, **1314** beneficiaries of the **"Supporting Legal Reforms"** Program

...equalizing opportunities

- ▶ **58** completed projects in the first round of the **"English Teaching"** Program: **13 000** students and teachers directly covered by the Program (**14 000** – indirectly), second round at the similar scale was launched in 2002.
- ▶ **125** accomplished projects in three rounds of the **"Equal Opportunities"** Program: **75 000** participants, special round addressed to people who have suffered from the flood in 2001.
- ▶ **1052** **"bridge scholarships"** granted for high school alumni from rural areas for the first year of studies.
- ▶ **177** schools have been participating in the **"Learning Schools"** Program: **1239** teachers have been trained, The „Learning Schools Academy" began to operate.
- ▶ **3500** scholarships for students of economy from small towns and villages granted under the **"Management Education"** Program in 2000-2002, **44** universities involved in co-operation, **23** publications.

...supporting human potential

- ▶ **156** scholarships have been granted to health care managers under the **"Training for Health Care Managers"** Program; **2000** postgraduate participants, **23** training centers, **4** international conferences, **2** publications.
- ▶ Nearly **300** participants took part in training courses for financial officers of the non-governmental organizations, **17** training sessions, **5** free-of-charge guidebooks, CD-ROM, a dedicated website on auditing NGOs.
- ▶ The **"Citizen and Law"** Program: over **12 000** free-of-charge advices for over **3500** individuals in difficult life and financial condition, **22** accomplished projects

...reinforcing citizens' energy

- ▶ Over **190** initiatives supported under the **"Act Locally"** Program: **207 000** beneficiaries of the first round and **3500** volunteers; **12** model local initiatives; second edition was launched in 2002.
- ▶ **1165** individuals were covered by the **"Undoing Unemployment"** Program which utilized the "outplacement" methodology – nearly a half of them found new jobs: **5** large projects were realized.
- ▶ **63** accomplished projects in **7** voivodships under the **"Village in Transition"** Program: **120** local communities covered by the Program, **110** training courses, nearly **3000** participants, creation of the "Atlas of Rural Initiatives".
- ▶ **20** initiatives financed in the **"Citizens and Local Government"** Program.
- ▶ **59** prizes financed by PAFF in **3** editions of the **"Pro Publico Bono" Competition** for the Best Civil Initiative in Poland.

...sharing of Polish experiences

- ▶ **83** fellows from **5** countries – Ukraine, Belarus, Russia (Kaliningrad District), Lithuania and Slovakia participated in the **Lane Kirkland Scholarship Program** in 2000-2002.
- ▶ **100** projects in total has been supported under two editions of the **"Region in Transition"** Program; a co-operation with non-governmental organizations from **11** countries including: Ukraine, Belarus, Lithuania, Russia, Slovakia, Romania, Georgia, Azerbaijan, Kazakhstan and Moldova, has been developed.

The Foundation's Programs 2002-2002

INITIATIVES IN EDUCATION

▶ **The “Polish Educational Portal Interkl@sa” Program**

Program Manager: The Foundation for Economic Education

<http://www.interklasa.pl>

▶ **The “Computer for a Teacher” Program**

Program Manager: The National Foundation for Computer Literacy

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

▶ **The “Computer Long Distance Training” Program**

Program Manager: The National Foundation for Computer Literacy

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

▶ **The “English Teaching” Program**

Program Manager: The “Nida” Development Foundation

<http://www.nida.pl>

▶ **The “Training for Health Care Managers” Program**

Program Manager: Society of Health Care Managers

<http://www.stomoz.pl>

▶ **The “Learning Schools” Program**

Program Manager: Center for Citizenship Education Foundation

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

▶ **The “Management Education 2002” Program**

Program Manager: Educational Enterprise Foundation

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

▶ **The “Equal Opportunities” Program**

Program Manager: The Polish Children and Youth Foundation

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

▶ **The “Bridge Scholarships” Program**

Program Manager: Educational Enterprise Foundation

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

CITIZEN IN A DEMOCRATIC STATE OF LAW

▶ **The “Supporting Legal Reforms – Training & Computers” Program**

Program Manager: The Foundation Center for Judges Training “Iustitia”

<http://www.iustitia.pl>

► **The “Citizen and Law” Program**

Program Manager: The Institute of Public Affairs

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

SUPPORT FOR LOCAL COMMUNITIES

► **The “Mutual Information Society” Program**

Program Manager: Klon/Jawor Society

<http://www.ngo.pl>

► **The “Act Locally II” Program**

Program Manager: The Academy for the Development of Philanthropy in Poland

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

► **The “Financial Management for NGOs” Program**

Program Manager: Civil Society Development Foundation

<http://free.ngo.pl/csdf/>

► **The “Undoing Unemployment” Program**

Program Manager: Enterprise Development Foundation in Suwałki

<http://www.frp.pl>

► **The “Village in Transition” Program**

Program Manager: Rural Development Foundation

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

► **The “Citizens and Local Government” Program**

Program Manager: Foundation in Support of Local Democracy

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

► **The “Pro Publico Bono” Award**

Program Manager: The “Pro Publico Bono” Competition Foundation

<http://www.propublicobono.pl>

SHARING OF POLISH EXPERIENCES IN THE TRANSFORMATION

► **The Lane Kirkland Scholarship Program**

Program Manager: Polish-U.S. Fulbright Commission

<http://www.fulbright.edu.pl>

► **The “Region in Transition (RITA) II” Program**

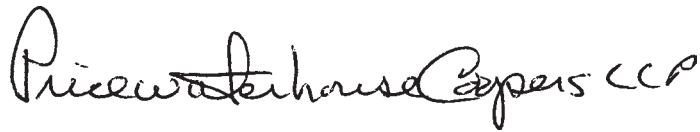
Program Manager: The Foundation Education for Democracy

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

Report of Independent Auditors

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

In our opinion, the accompanying statement of financial position and the related statements of activities and cash flows present fairly, in all material respects, the financial position of the Polish-American Freedom Foundation (the “Foundation”) at 31 December, 2002 and the changes in its net assets and its cash flows for the year then ended in conformity with accounting principles generally accepted in the United States of America. 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 of these statements in accordance with auditing standards generally accepted in the United States of America, which 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, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.



April 30, 2003

S **STATEMENT OF FINANCIAL POSITION AS OF DECEMBER 31, 2002**

ASSETS

ASSETS:

Cash and cash equivalents (Note 6)	\$ 23,675,809
Fixed income investments (Note 6)	47,822,185
Equity investments (Note 6)	52,689,816
Accrued interest receivable	346,004
Fixed assets, net (Note 7)	45,912
Prepaid expenses and other assets	62,224

Total assets	\$ 124,641,950
--------------	----------------

LIABILITIES AND NET ASSETS

LIABILITIES:

Grants payable (Note 5)	\$ 809,144
Accrued expenses	151,520

Total liabilities	960,664
-------------------	---------

Commitments (Note 8)

NET ASSETS:

Unrestricted net assets (Notes 2, 4)	123,681,286
--------------------------------------	-------------

Total liabilities and net assets	\$ 124,641,950
----------------------------------	----------------

The accompanying notes are an integral part of these financial statements.

STATEMENT OF ACTIVITIES FOR THE YEAR ENDED DECEMBER 31, 2002

Changes in unrestricted net assets:

Income:

Interest and dividend income	\$ 2,835,882
Support (Note 4)	17,000,000
Net realized and unrealized depreciation on securities	(10,502,306)
Total income	<u>9,333,576</u>

Expenses:

Employee compensation and benefits	627,119
Other operating costs	317,009
Occupancy	125,706
Depreciation	39,179
Other	<u>131,166</u>

Total expenses	<u>1,240,179</u>
----------------	------------------

Excess of expenses over income, before grants	8,065,697
---	-----------

Grants (Note 5)	(4,402,403)
-----------------	-------------

Translation adjustment	<u>521,752</u>
------------------------	----------------

Increase in unrestricted net assets resulting from operations	4,212,746
---	-----------

Reclassification of permanently restricted to unrestricted net assets (Note 2)	<u>120,000,000</u>
--	--------------------

Total increase in unrestricted net assets	124,212,746
---	-------------

Changes in restricted net assets:

Reclassification of permanently restricted to unrestricted net assets (Note 2)	<u>(120,000,000)</u>
--	----------------------

Total decrease in restricted net assets	<u>(120,000,000)</u>
---	----------------------

Total increase in net assets	4,212,746
------------------------------	-----------

Net assets, beginning of the year	<u>119,468,540</u>
-----------------------------------	--------------------

Net assets, end of the year	<u>\$ 123,681,286</u>
-----------------------------	-----------------------

The accompanying notes are an integral part of these financial statements.

STATEMENT OF CASH FLOWS FOR THE YEAR ENDED DECEMBER 31, 2002

Cash flows from operating activities:

Increase in net assets	\$ 4,212,746
Adjustments to reconcile net increase in net assets to net cash provided by operating activities:	
Net realized and unrealized depreciation on securities	10,502,306
Depreciation	39,179
Increase in accrued interest receivable	(29,966)
Increase in prepaid and other	(24,802)
Decrease in liabilities	(28,916)
Increase in grants payable	240,144
Net cash used from operating activities and grants	<u>14,910,691</u>

Cash flows from investing activities:

Endowment Fund investment portfolio activity:	
Proceeds from sales/redemption of investments (Note 6)	134,207,480
Cost of investments purchased (Note 6)	(242,338,830)
Cost of fixed assets purchased	(11,404)
Net cash used by investing activities	<u>(108,142,754)</u>
Net decrease in cash and cash equivalents	(93,232,063)
Cash and cash equivalents, beginning of year	<u>116,907,872</u>
Cash and cash equivalents, end of year	<u>\$ 23,675,809</u>

The accompanying notes are an integral part of these financial statements.

Notes to Financial Statements

1. ORGANIZATION

The Polish-American Freedom Foundation (the "Foundation") is a 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.

The Foundation concentrates its efforts in four main program areas: (i) Initiatives in Education, (ii) Support for Local Initiatives, (iii) Regional Outreach - Sharing Polish Experience in Transformation, and (iv) Citizen in a State of Law. The Foundation generally seeks an external program manager (typically a well established non-governmental organization in Poland) to execute the objectives of each individual grant, thereby leveraging the Foundation's resources.

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 classify information regarding its financial position and activities into certain classes of net assets. As at December 31, 2002, the entire balance of net assets was classified as unrestricted. Unrestricted net assets are those net assets that are not restricted by donor imposed stipulations. As a result of an amendment to the Grant Agreement (defined in note 4) in February 2002, the amount of \$120,000,000, previously classified as permanently restricted net assets, were reclassified as unrestricted net assets.

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

Equity and fixed income investments are generally valued based upon the bid price as quoted on major exchanges. However, certain fixed income securities are valued based upon yields or prices of securities of comparable quality, coupon, maturity and type as well as indications as to values from brokers and dealers.

The Foundation engages professional investment managers who make investment decisions according to the Foundation's investment policy and monitor the Foundation's investments.

Cash and Cash Equivalents

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

Grants

Grants are recorded as grants expense in the statement of activities and grants payable in the statement of financial position when the grant is approved in accordance with policies set by the Board of Directors, negotiations have been finalized with the grantee and the parties have signed the grant agreement.

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. Polish zloty denominated assets and liabilities are translated at the year-end spot currency rate.

Translation adjustments are charged directly to unrestricted net assets.

Donated Services

The Foundation's directors receive no compensation or fees for serving as directors. Such directors donate significant amounts of their time to the Foundation's programs. 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 non-executive Polish directors receive a fee for providing advice and assistance to the Foundation. For the year ended December 31, 2002 the total fees paid to all Polish non-executive directors amounted to \$38,000.

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 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.

Credit risk

Credit risk is the possibility that loss may occur from counterparty failure to perform according to the terms of a contract. Unless noted otherwise, collateral or other security is not normally required by the Foundation to support financial instruments with credit risk. As at 31 December 2002 the Foundation had credit exposure mainly to debt instruments in the Foundation's portfolio. The maximum risk of accounting loss from these financial instruments is represented by their respective balance sheet amounts.

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 Fund has returned \$120 million of the Fund's assets to the U.S. Treasury and intends to use substantially all of the remaining balance of its assets to endow the Foundation (the "Endowment Amount").

According to the terms of the grant agreement between the Fund and the Foundation, as amended, (the "Grant Agreement"), the Foundation shall be operated as a perpetual endowment, with the long-term objective of earning an average annual return on the Endowment Amount which exceeds average annual disbursements to Beneficiaries and for Expenses as defined in the Grant Agreement.

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 exist foreign policy grounds described in Section 801 of the SEED Act.

The Foundation has received the following Endowment Amounts from the Fund (dollars in millions):

October 8, 1999	\$ 40.0
September 29, 2000	40.0
September 27, 2001	40.0
October 4, 2002	17.0
	<u>\$ 137.0</u>

5. GRANTS AND GRANTS PAYABLE

Grants

In accordance with accounting principles generally accepted in the United States, the Foundation is required to record the total amount of a grant as an expense at the time the grant agreement is signed. As programs develop the Foundation and the grantee may agree to decrease the amount of a grant to reflect changes in a program not anticipated at the time the grant agreement was signed. For the year ended December 31, 2002 the Foundation signed \$4,405,395 of new grant agreements and reduced the amount of grant agreements signed in prior periods by \$2,992, resulting in an expense for grants of \$4,402,403 reported in the accompanying statement of activities.

Grants Payable

Each time the Foundation records an expense to reflect the signing of a new grant agreement it also records a grant payable to reflect a liability to fund the full amount of the grant. In practice, the Foundation generally disburses grants to grantees over time, as funds are required to meet the costs of each program. As a result, the amount recorded as an expense for Grants in the statement of activities generally does not equal the amount of grants disbursed by the Foundation in a fiscal period. For the year ended December 31, 2002, the Foundation disbursed \$4,162,259 of grants as compared to \$4,405,395 of new grant agreements signed. The following table sets forth the changes in grants payable for the year ending December 31, 2002:

Grants disbursed		\$ 4,162,259
Grant agreements signed	\$ (4,405,395)	
Decrease in amount of grant agreements signed in prior periods	2,992	
Grant expense reported in statement of activities		(4,402,403)
Net change in grants payable		(240,144)
Grants payable, beginning of period		(569,000)
Grants payable, end of period		<u>\$ 809,144</u>

In addition, as of December 31, 2002 the Foundation had approved 9 grants totaling \$3.1 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 December 31, 2002 the Foundation signed 8 of these grant agreements totaling \$2.1 million.

6. CASH AND CASH EQUIVALENTS AND INVESTMENTS**Cash and cash equivalents:**

As of December 31, 2002, the Foundation's cash and cash equivalents consisted of \$23.7 million in cash (principally money market funds) that was deposited in various high quality U.S. financial institutions. Substantially all of the cash and cash equivalents balance was held by the Foundation's various investment managers and was available for investment in fixed income and equity securities.

Investments:

Following is the cost, fair value and percentage of net assets by classification for investments in the Foundation's investment portfolio (in thousands):

	Cost	Fair value	% of net assets
Fixed income investments:			
U.S. fixed income	\$ 34,869,285	\$ 35,541,407	28.7%
PLN fixed income	11,894,445	12,280,778	9.9%
Total fixed income investments	<u>46,763,730</u>	<u>47,822,185</u>	38.7%
Equity investments	54,580,485	52,689,816	42.6%
	<u>\$ 101,344,215</u>	<u>\$ 100,512,001</u>	<u>81.3%</u>

Pursuant to generally accepted accounting principles, the Foundation has disclosed the gross amount of purchases and sales of securities for the year ended December 31, 2002. These amounts are reported in the accompanying statement of cash flows as "proceeds from sales/redemption of investments – \$134,207,480" and "cost of investments purchased (\$242,338,830)". During 2002, all purchase and sale of investment decisions were made by the Foundation's various investment managers.

7. FIXED ASSETS

As of December 31, 2002, fixed assets consisted of:

Computer equipment and software	\$ 73,076
Furniture and equipment	58,575
Automobiles	36,444
Leasehold improvements	2,275
	<u>170,370</u>
Less – Accumulated depreciation	124,458
Net book value	<u>\$ 45,912</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 December 31, 2004. Lease commitments for the twelve months are approximately \$132,000 per annum for each of 2003 and 2004.

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.

Board of Directors

John P. Birkelund – Chairman

Chairman of the Board of Directors of the Polish-American Enterprise Fund, Senior Advisor UBS Warburg LLC

Marek Belka

Former Polish Deputy Prime Minister and Finance Minister, former Economic Advisor to the President of the Republic of Poland

Joseph C. Bell

Senior Partner at Hogan & Hartson

Michał Boni

Former Minister of Labour and Social Policy, former Advisor to Polish Deputy Prime Minister and Labour Minister

Zbigniew Brzeziński

Former National Security Advisor to the U.S. President, Counselor at the Washington Center for Strategic and International Studies, Member of the Board of Directors of the Polish-American Enterprise Fund

John H. D'Arms (till January 2002)

President of the American Council of Learned Societies

Robert G. Faris

President and Chief Executive Officer of the Polish-American Enterprise Fund

Anna Fornalczyk

Professor at the High School of Business-National Louis University in Nowy Sącz, former President of the Polish Office for Competition and Consumer Protection

Christopher R. Hill

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

Aleksander Koj

Professor at the Molecular Biology Institute at the Jagiellonian University, former Rector of the Jagiellonian University

Jerzy Koźmiński

President and Chief Executive Officer of the Polish-American Freedom Foundation, former Polish Ambassador to the United States

Krzysztof Pawłowski

Rector of the High School of Business-National Louis University in Nowy Sącz, former Polish Senator

Nicholas A. Rey

Former U.S. Ambassador to Poland, Member of the Board of Directors of the Polish-American Enterprise Fund

Management and Staff

Jerzy Koźmiński

President and Chief Executive Officer

Ryszard Kruk

Administrator of the Representative Office, former Vice President of the Polish-American Enterprise Fund

Norman E. Haslun III

Chief Financial Officer

C. Douglas Ades

Secretary to the Board of Directors

Jacek Michałowski

Program Director

Radosław Jasiński

Program Director

Anna Wojakowska-Skiba

Program Director

Małgorzata Rurewicz-Rzesoś

Chief Accountant

Mira Osiecka

Financial Analyst

Przemysław Zaroń

Information and Public Relations

REPRESENTATIVE OFFICE

72 Dobra St., 00-312 Warsaw, Poland
tel.: (22) 828-43-73
fax: (22) 828-43-72
e-mail: paff@pafw.pl, <http://www.pafw.pl>

POLISH-AMERICAN FREEDOM FOUNDATION

410 Park Avenue, 15th Floor
New York, NY 10022, USA
tel. (917) 210-8083