



Brussels, 19th February 2004

SPECIAL REPORT OF THE DEXIA S.A. BOARD OF DIRECTORS (UNDER FRENCH FINANCIAL SECURITY LAW)

I. REMINDER OF THE REGULATORY CONTEXT

The French financial security law of 1st August 2003 aims to strengthen the rights of savers and policyholders and particularly to improve the quality of financial information. Particular attention is paid to internal controls, notably in article 117.

This compels the Chairman of the Board of Directors to report to the Shareholders' Meeting on conditions for preparing and organizing the work of this Board as well as internal control procedures put in place by the company. This obligation applies to all issuers publicly calling for savings in France, whatever their nationality and therefore Dexia S.A. also.

II. CONDITIONS FOR PREPARING AND ORGANISING THE WORK OF THE BOARD OF DIRECTORS

II.1. Attributions of the Board of Directors

The Board of Directors of Dexia SA (hereinafter called the Board of Directors) sets out strategic objectives and general company and group policy. It controls and directs management. It appoints members of the Dexia SA Management Board (hereinafter the Management Board), approves the resources necessary to reach the strategic objectives that it defines, implements programs for the management and control of the company and reports to shareholders.

II.2. Preparation and schedule of Board of Directors meetings

Board of Directors' meetings are prepared by the CEO in cooperation with the Chairman. The Secretary General is responsible for the practical organization of these meetings.

Agenda

The agenda is determined by the CEO and the Chairman.

- The first point on the agenda covers the discussion and approval of the draft minutes of the previous board meeting.
- If one or several Board of Directors' committees (the Strategy Committee, the Audit Committee, the Appointments Committee and the Compensation Committee) have met since the last board meeting, the minutes of these committees will also be included in the Board of Directors meeting agenda. These reports are generally presented by the Chairman of the committee concerned.
- The last point on the agenda is the "miscellaneous" section enabling each member of the Board to raise any points not on the agenda.

Documentation

If necessary, each point of the agenda is supported by visual or paper documents. Wherever possible and as far as confidentiality obligations allow, these documents (notes, visuals, reports) are sent to Board members in advance.

Minutes

The Secretary General is responsible for writing the minutes of the Board of Directors meeting. These minutes should be a true and faithful reflection of the meeting and the contributions of each of the Board members.

Draft minutes are always sent to Board members in advance.

Once approved, the minutes are signed by the Chairman.

Participants

All Board members are invited to attend board meetings. This also includes an observer who participates in meetings without enjoying voting rights.

The Board of Directors comprises a certain number of independent Board members (8 out of 18 as of 31st December 2003) identified as such on the basis of very strict criteria that go beyond the stipulations of Belgian law and the recommendations of the Bouton report.

Except where the Board disagrees, the members of the Management Board attend the meeting for certain specific points of the agenda. Members of the Management Board do not in theory participate in discussions involving:

- the minutes of the last board meeting
- the reports of specialized committees created within the Board of Directors

Meeting calendar and place

Generally, the Board of Directors meets in February, March, May, July, September and November of each year.

Wherever possible, meetings are organized in Brussels and Paris alternatively.

Press conferences

At certain times, for example when the board has been informed of quarterly, half-yearly or annual company results, the meeting will be followed by a press conference.

II.3. Operation of the Board of Directors

Statutory regulations

The company's articles of association include the following rules for governing the Board of Directors:

- Any debate requires the presence of representation of at least half the members of the Board.
- Decisions are made by a majority of all members present or represented; if members votes are tied, the Chairman or member replacing him will have a casting vote.
- Decisions on important questions described below require the presence or representation of at least two-thirds of members and a decision made by a two-thirds majority of all members present or represented.
 - (i) *decisions to use authorized capital or to submit to the Ordinary Shareholders' Meeting a proposition to issue shares, bonds convertible or redeemable in shares, warrants or other financial instruments eventually giving rights to shares, when the amount of capital increase resulting from the issuing of these shares or the conversion or redemption of these bonds or the exercising of these warrants or other financial instruments exceeds 10% of the capital existing prior to these decisions being made.*
 - (ii) *decisions relating to the acquisition or sale of assets representing more than 10% of the company's equity.*
 - (iii) *decisions to submit to the Ordinary Shareholders' Meeting propositions to modify company's articles of association.*
 - (iv) *decisions to appoint or dismiss the Chairman of the Board of Directors or the CEO.*

Board of directors' internal rules of procedure

Since 1999, the Board of Directors has been governed by rules of procedure (hereinafter Rules). Amended several times, the Rules set out procedures enabling the board to fully exercise its functions and optimize the contribution of each member of the Board. The Rules determine rights and obligations of Board members in carrying out their mandate, operating and evaluation guidelines for, relationships with the Management Board and the organization and operation of specialized committees (see infra).

The rights of Directors set out in the Rules include the right to receive any information, specifically strategic information, necessary to carry out their duties. Directors' duties include a series of rules destined to ensure their independence. They must act in the company's interest, considered to be those of all shareholders and those of the company's and the Group's customers and staff. Directors must generally ensure that they show complete independence from interests outside the company itself. Directors also undertake to actively participate in the work of the Board and specialized committees of which they may be members. Regular attendance is the first condition of this membership and they are requested to effectively and attend at least three-quarters of meetings.

In application of regulations on insider trading, the Rules also set out a series of strict procedures designed to ensure complete transparency in the trading of Dexia shares. Directors are required to make occasional and periodic declarations to the Group Chief Compliance Officer and, also, to prohibit certain types of transaction or all transactions if necessary during specified periods, unless otherwise approved by the Group Chief Compliance Officer.

Finally, the Rules determine conditions of membership, operation and responsibility of specialized consultative committees created by the Board of Directors and acting under its responsibility.

Activities of the Board of Directors in 2003

- The Board met seven times in 2003. The attendance rate of directors was 84.8%.
- Beyond statutory appointments, the Board mainly focused on the following issues:
 - discussing and approving company and consolidated financial statements and following-up the Group's business activities in 2002.
 - discussing and approving interim company and consolidated statements at 31st March, 30th June and 30th September 2003 and following-up the Group's business activity at those same dates.
 - discussing and approving the Dexia Group's budget for 2003
 - discussing and approving the audit charter for 2003
 - discussing and approving the main elements of the Group's new structure implemented from 1st January 2004
 - discussing and making decisions following the Board of Directors' self assessment
 - discussing and approving the Compliance Charter and Action Plan
 - familiarization with and discussion of the internal control report and the 2002 risk assessment and management report
 - periodic reports of the audit committee

- a follow-up of the acquisition of Artesia, the merger between Dexia Bank and Artesia and a follow-up of the integration of these two entities
- a follow-up of the Dexia Bank Nederland case
- a follow-up of the Lernout & Hauspie case
- the Group employee shareholding plan and the stock option plan for 2003
- the reports of the Strategy Committee, Compensation Committee and Nominations Committee
- strategy and treatment of treasury shares
- the revision of the Board's internal rules of procedure, the internal rules of the Management Board and the protocol on the prudential structure of the Dexia Group, particularly in view of the consequences of the application of the Belgian corporate governance law of 2nd August 2002
- modification of the audit charter
- convening the Ordinary or Extraordinary General Assembly

Each quarter, the CEO provides a report to the members of the Board on the activities of the different entities and their subsidiaries. This report focuses on the Group's four main activities. It gives a detailed picture of Dexia's position in these areas.

Between two meetings of the Board of Directors, the CEO will send a letter of information covering any major events concerning the Group.

Self-assessment

The Board's internal rules of procedure have stipulated until now that it should carry out a self-assessment of its own activities at intervals not exceeding two years.

The Board carried out a new self-assessment in 2003.

Overall, the Board's satisfaction rate relative to the questions asked to may be considered to be very acceptable at 82%.

Several decisions were made following this self-assessment process and particularly:

- to strengthen the Strategy Committee
- to increase the number of meetings of the Audit Committee
- annual Board self-assessment
- the possibility for the Chairman of the Board of Directors of assigning a task to the Group Auditor on information from the Audit Committee.

THE COMPANY'S INTERNAL CONTROL OBJECTIVES

III.1 Internal control missions

Dexia S.A., a financial company in Belgian law, signed a protocol in March 2001¹ on the prudential structure with the Banking, Financial and Insurance Commission (hereinafter CBFA).

In this context, Dexia SA voluntarily complies with operating standards equivalent to those applied in Belgian credit institutions. This condition includes, firstly, the implementation of an appropriate collegiate management and control structure within the company and secondly, in addition to legislation arising from its status as a financial institution, Dexia SA is subject to certain prudential structure provisions inspired by those applied to credit institutions under Belgian law, particularly the law of 22nd March 1993 relative to the status and financial control of credit institutions and the CBFA circular 97/4 dated 30th June 1997 on internal control and internal audit.

The general aim of internal controls is to prevent and control major risks of error and fraud. As with any system of control, it has been designed to reduce this type of risk to levels compatible with the requirements of the company but cannot guarantee total immunity.

More specifically, the missions assigned to internal control within the Dexia Group may be set out in four main fields:

Ensure that risk management systems in place are effective

Risk management is the basis of any banking activity. Dexia SA, by the nature of the group's main activities as well as its desire to preserve its reliable risk profile and, consequently, emphasize rules of prudence, diversification and the quality of its outstanding loans, has made its approach to risk a key characteristic of its perception of financial markets. The system of internal control aims to guarantee to the Management Board that risks taken by the Group are in accordance with this characteristic and compatible with pre-determined performance objectives.

Ensure that accounting and financial information produced is reliable and pertinent

The main objective of financial information is to provide a reliable picture of the Dexia Group's situation in a regular, complete and transparent manner. The system of internal control is centered on achieving this objective.

Ensure respect for regulations and ethical rules, internally and externally

The enhanced performance of the Dexia Group implies strict compliance with legislation and regulations in each of those countries where it operates as well as with the standards that it fixes for itself in terms of corporate governance, compliance or sustainable development.

The internal control system must guarantee respect for these principles.

Improve the performance of the Group whilst ensuring efficient management of available resources

The decisions taken with this aim in mind by the Management Board must be able to be implemented quickly throughout the Group. Internal control procedures ensure the integrity of the flow of information, the conformity of action implemented and the monitoring of results.

¹ Protocol on the prudential structure dated 21st March 2001, modified 12th March 2003

III.2 General structure of the system

The Dexia Group internal control system rests on a clear separation of functions. It has been designed to maintain to distinction between operators and those responsible for their validation, monitoring or clearance.

Consequently, the Dexia Group's general internal control is based on a four level organization:

The first level of control is exercised by each employee, according to his or her own explicit responsibilities, the procedures applicable to the activity and instructions provided by their management.

The second level of control is exercised by management, as part of the normal supervision process and defined in applicable procedures. Managers of operating services are therefore heavily involved in operating the internal control system.

The third level of control is the responsibility of specialized functions, independent of the activities controlled and reporting directly to the Management Board. This third level may also be the responsibility of specialized committees, comprising employees from operating, support or control and functions and chaired by a member of the Management Board

The fourth level of control is the Dexia Group audit process that is permanently responsible for ensuring the performance and effective application of the three levels of control and defined above, in the parent company and all subsidiaries and offices.

Wherever possible, information systems are used to automate these controls.

Moreover, to ensure all players in the internal control system speak the same language, the Dexia Group has progressively compiled a common reference base of instructions from charters, codes, guidelines and procedures.

IV. THE MAIN PLAYERS IN THE INTERNAL CONTROL SYSTEM (ORGANISATION, ROLE, RESOURCES)

IV.1 The Management Board

The Management Board receives powers from the Board of Directors to manage the company and the Dexia Group of whom it steers and coordinates the different business lines.

To maintain the performance and development of the Dexia Group, the Management Board is ultimately responsible for implementing and maintaining an appropriate internal control system. It defines and coordinates the Group's financial control policy as part of the strategy defined by the Board of Directors. It allocates resources and deadlines for implementing action decided as part of this policy. It checks that the objectives given have been attained and the internal control system is adequate for all requirements. Finally, it adjusts these requirements according to internal and external developments.

IV.2. The organization of Dexia SA as a financial institution

To assist it in its overall role steering the Dexia Group, the Management Board is supported by four executive business line committees (two of which will only come into existence on 1st January 2005) and by 14 departments enabling it to carry out missions independent of control.

The executive business line committees (Public Finance, Personal Financial Services, Asset Management and Treasury & Financial Markets) propose the business line strategy, fix objectives, set budgets and monitor the results of the business line on a Group level. The business line executive committees comprise the main representatives within operating entities. They are chaired by Group business line managers who are also members of the Management Board. In consultation with entity managers, business line managers are given certain competences for managing their leading executives.

The fourteen Dexia SA departments are particularly responsible, within their field of competence, for defining and coordinating the implementation of policies decided by the Management Board and searching for synergies within the Group. They work in cooperation with teams in the different entities within the Group.

The teams more specifically concerned by internal control are:

- Group Audit, reporting directly to the CEO, chairman of the Management Board, defines the methods used within the Group, coordinates and participates in auditing cross-division functions covering several entities, audits Group divisions and the audit functions of the different entities.
- the Risk Management team, reporting to the Group Chief Financial Officer, supervises risk management policy. It establishes guidelines on limits and delegations, controls and measures risks for the Group and implements harmonized methods in the different entities.
- the Chief Compliance Officer, reporting directly to the CEO, chairman of the Management Board, manages the network of Compliance Officers in the different entities and ensures respect for the policy of integrity and the development of the culture of ethics that has been preponderant in the Dexia group since its creation.

Moreover, divisions have been set up with the main subsidiaries (Dexia Bank Belgium, Dexia BIL and Dexia Crédit Local) for human resources (under the supervision of the Group Human Resources Department), finance, planning and budget (under the supervision of the Group Chief Financial Officer) and operations and technology (under the supervision of the Group Chief Operating & Technology Officer) functions. Within these divisions, the manager of the subsidiary reports to the manager of the same function within Dexia SA. The manager of the Group function, in cooperation with the supervisor of the divisions concerned, may propose recruitment, promotion, compensation and objectives for the said subsidiary.

In any case, monitoring is based on a system of delegations, regular reports to Dexia SA departments concerned as well as to the Management Board and on the participation of the members of the said Management Board in the different administrative and management bodies. When their size and activity justify it, subsidiaries themselves have the same corporate governance bodies as Dexia S.A.

IV.3. Dexia S.A. operating departments and divisions

In agreement with Dexia Group principles, the managers and employees of Dexia SA operating departments and divisions guarantee the adaptation and performance of internal control within their field of activity. They are particularly responsible for analyzing the risk of each transaction they initiate and checking it is compatible with their department's system of internal control. Where changes in the internal or external environment occur that impact the system, they should propose or set up, depending on their level of responsibility, the adaptations necessary to properly control the risks taken.

IV.4 Specialist committees

A certain number of committees are a key part of the Dexia Group internal control system and contribute particularly to the definition and performance of it. The purpose of these committees is to enable simultaneous consultation between different departments or divisions in managing the different activities with the aim of taking into account the constraints of all, provide shared experiences and encourage good practice. Decisions are taken on a collegial basis. In case of persistent disagreement, the Chairman, a member of the Management Board, will be the final arbitrator.

Their responsibilities cover several areas of internal control. Among the most important:

Credit risk management

Within Dexia SA, the quarterly Credit Risk Policy Committee defines the Group's risk profile and risk guidelines and the Credit Committee rules on issues that are beyond the scope of the delegations granted to operating entities.

Credit Committees also exist in Dexia SA subsidiaries or for certain specific activities. They make commitment decisions on issues under their competence or monitor doubtful or contested debts and decide on provisions to be made.

Market risk management

Within Dexia SA, the ALM Committee fixes particularly risk limits (VAN ALM and sensitiveness) and pilots cash flow gap and rate structural exchange position gap coverage.

A quarterly Market Risks Committee is being constituted within Dexia SA; it will be responsible for defining limits for the Group and the entities by business line, defining market risk management methods and will monitor respect for limits fixed for the Group and its entities;

ALM and Market Committees also exist in Dexia SA subsidiaries. They meet either monthly or fortnightly.

IV.5 Risk Control Department

The Risk Control Department guarantees the Management Board a low risk profile for the Group, leading to a high rating. This is essential for raising resources in the best possible conditions and reaching objectives of profitability expected by investors.

The Risk Control Department has wide-ranging competence as it covers all the Group's credit, market, cash flow and operating risks in its banking and non banking activities.

The department manager reports to the Group Chief Financial Officer, a member of the Management Board, responsible for mergers & acquisitions, risks, compatibility and financial control. The positioning of the Risk Control Department ensures complete independence from operations.

IV.6 Compliance

Operating in highly regulated sectors, the Dexia Group attaches great importance to complying with legal, regulatory and prudential requirements. Beyond strictly regulatory requirements, the Group has an approach that emphasizes ethics and compliance with regulations. Harmonized guidelines have been defined in the integrated policy, and Compliance Charter and ethical codes.

The Dexia Group uses international standards in the fight against money laundering and the financing of terrorism. More specifically, the company adheres to recommendations published by FATF, as it does the Wolfsburg principles for Private Banking and Correspondent Banking. These principles constitute standards, applicable to all Group entities. They are strengthened in practice by automatic prevention, monitoring and surveillance tools.

The Dexia Group has an independent Compliance function for piloting its policy across the Group and defending them within Dexia SA, particularly with the members of the Board of Directors and the Management Board. The Chief Compliance Officer reports directly to the CEO and manages a network of Compliance Officers who are active in each of the Group's operating entities and subsidiaries. Compliance Officers are appointed in all the Group's important subsidiaries and in all other entities where the local situation demands it. They functionally report to the Group Chief Compliance Officer and in theory report to the Chairman of the Management Board. Correspondents are in place in the Group's other subsidiaries, offices or representatives.

Together with his opposite numbers, the Group Chief Compliance Officer is responsible for keeping the internal ethics and regulatory rules up-to-date based on external developments in regulations. They also inform and educate management and staff in regulations while ensuring compliance with policy in each entity. Coordination enables methods and procedures to be harmonized in the different, often international, domains of ethics and the fight against money laundering and terrorism.

IV.7 Internal Audit

Internal audit promotes internal controls within the Group and permanently monitors the performance and the effective application of the applicable internal control system. Internal audit therefore assists the Group Board of Directors in their monitoring role as well as the Group and Entity Management Boards in attaining their objectives.

Internal audit evaluates whether the risks run by the Group in its various activities and in all entities comprising it are adequately perceived and covered. Internal audit is also attentive to constant improvement in operating and the brand image of all group entities whilst ensuring efficient management of available resources.

A common audit charter sets out the fundamental principles governing internal audit within the Dexia Group describing the objectives, role, responsibilities and methods of operation.

The strategy, level of requirement and operating rules of group internal audit are fixed by the Management Board within a framework approved by the Dexia SA Management Board Audit Committee that takes into account the requirements of local legislation and regulations or instructions from prudential control authorities.

As part of its operations, internal audit has access to all information, documents, premises or people in the group or the entity for which it is responsible.

All Group activities and entities come under the internal audit field of action, without reservation or exception. Therefore, the Group internal audit function covers the activities of Dexia SA, operating entities and their subsidiaries and branches. It does not in theory cover activities of companies in which the Dexia Group only has a minority shareholding except where specifically requested by prudential control authorities. However, the Dexia representative on the Board Of Directors should be aware of the status of the internal control system and alert if necessary in the Management Board and audit department of the entity that holds this shareholding.

Group Audit managers, under the leadership of the Group General Auditor, report to the Chairman of the Group Management Board and the Dexia SA Board of Directors assisted by its Audit Committee.

Managers in subsidiary audit departments report hierarchically either to the Chairman of the local board, the Board of Directors, the Supervisory Board or the Audit Committee and functionally Dexia General Auditor. The procedures for implementing these operations were approved by subsidiary administration and surveillance bodies in 2002.

Subsidiary audit managers report to general auditors in their respective entities.

The methods used are standardized, both in risk analysis and performing tasks. They were developed at the initiative of Group Audit and are common to all group entities.

Risk analysis for each activity to be audited determines the frequency of audits (annual, twice a year or four times a year). These frequencies are used to determine the audit plan for the year in progress. Audit plans are presented to Management Boards in the entities concerned, and then submitted for approval to their audit committees.

Recommendations are drawn up and action plans established for each mission. Their purpose is to remedy weaknesses shown by audit missions in order to consolidate the system of internal control. Each action plan is approved by the Management Board and is regularly monitored.

V. PRODUCTION AND TREATMENT OF ACCOUNTING AND FINANCIAL INFORMATION

V.1. Financial reports

The main purpose of annual accounts is to provide a true and faithful picture of the assets, financial situation and results of a company.

Accounting and Consolidation Department missions and organization

The Accounting and Consolidation Department reports to the Chief Financial Officer, a member of the Management Board.

The accounting and consolidation department produces Dexia SA company financial statements and consolidated financial statements for the Dexia Group.

It also has a role monitoring and controlling accounting data in its permanent establishment in France and direct subsidiaries Dexia Crédit Local, Dexia BIL and Dexia Bank as part of the consolidation process. It checks that the information provided is uniform and complies with Group rules.

This Department was created on 1st February 2003. Its purpose is to coordinate Group accounting projects as well as accounting standards. It uses competences existing in the three entities and only therefore has a small team of specialists. More generally, it has a variety of information resources to carry out its mission monitoring accounting in its widest sense. It ensures that accounting and consolidated data corresponds with the information existing in other departments (Legal, Fiscal, Risk Management; Financial Control...). It is involved in the Committees that may cover its mission or receives minutes of their meetings. It participates in making changes to computer systems with the aim of ensuring that specific requirements are taken into account and is responsible for piloting the project enabling the Group to adopt international accounting standards (IFRS) by 2005.

Producing company accounts

Dexia SA's Belgian accounting information is held in Brussels and French accounting information is held in Paris. Accounting information for the permanent establishment is held by a person in charge in the Dexia Crédit Local accounting department.

Each quarter, accounts for the permanent establishment are integrated into those of Dexia S.A. – Brussels, as part of quarterly end-of-period account closures.

Further checks are carried out by general accounting teams during quarterly or annual closing of accounts. Major changes have to be explained.

Producing consolidated accounts

Dexia SA main has shareholdings in three entities: Dexia Crédit Local, Dexia BIL and Dexia Bank (Belgium). Each of the entities prepares consolidated accounts that are in turn consolidated with those of the parent company Dexia SA.

The main adjustments made in consolidating the Dexia Group cover the elimination of reciprocal accounts and intra-group transactions (acquisitions/sales of assets, dividends...). They also cover the reprocessing of accounts of companies held by different entities in the Group. Accounts sent by the entities have already been reprocessed according to Dexia standards, the number of adjustments to be made other than those set out above is therefore limited.

Where difficulties arise interpreting accounting principles, all entities may call on the Dexia SA Consolidation Department. In cooperation with the entity accounting standards department, it will supply an appropriate answer. A working group including managers from standards departments in each entity meets regularly to discuss accounting interpretations of Dexia and IFRS standards and, if necessary, to propose modifications to Group CFO committees.

Accounts closure process

When company and consolidated accounts have been finalized, the Consolidation And Accounting Director presents therefore reviewed by the Dexia Chief Financial Officer and has them approved by the Management Board. They are then presented to the Audit Committee and to the Dexia SA Board of Directors.

Role of the Statutory Auditors

Auditing is the responsibility of a college of two auditors who carry out a peer review of the other's information.

The Auditors are involved in the entire process of controlling financial and accounting information in order to preserve efficiency and transparency. They analyze accounting procedures and evaluate internal control systems in place with the aim of determining the type, period and extent of their controls.

They issue instructions for auditors in entities and centralize their work. They organize review meetings about the results of their audits and evaluate the interpretation of standards. Finally, they check coherence between the management report and financial statements as well as coherence with all elements audited.

Carrying out these tasks allows them to be assured beyond reasonable doubt that the accounts they are checking do not contain significant anomalies.

V. 2 Management information

Financial statements (balance sheet, off-balance sheet, income statements and appendices) are not the only documents issued by the Dexia Group to its shareholders and the general public. They are mainly supplemented by activity reports and business line results, included in the Activity Report or provided during presentations to financial analysts.

Most of the information requires crossing or aggregating data from different sources, breaking down figures available globally or reprocessing accounting data according to financial control parameters. It is checked and supplied to the writers of the Activity Report by the Planning and Financial Control department, report into the Dexia SA Chief Financial Officer, a member of the Management Board

Producing the activity report

This quarterly activity report uses a series of key indicators (production & long and short-term financial commitments, commissions, volumes of deposits and managed outstanding credits, updated premiums and principal sums in the credit enhancement activity...). It is produced using information supplied by commercial departments based on templates specific to each business line and uniform across the Group. These templates have been produced by Group and entity financial control departments (Group Financial Control). The information supplied is accompanied by comments directly made by commercial departments.

Group Financial Control checks the coherence of information supplied and the conformity of the presentation with the standards established for all Dexia Group entities.

This activity report is presented to the Management Board before being sent to the Department of Financial Communication and Investor Relations for inclusion in the annual report and quarterly Activity Report.

Determining results by business line

The Dexia Group is divided into four business lines (Public/Project Finance and Credit Enhancement, Retail Financial Services, Investment Management Services, Capital Markets and Treasury activities) to which Central Assets is added.

Revenue per business line is calculated based on two types of analytical information, sales margins and other information from the income statement (commission, overheads, and value corrections).

Aggregating intermediate balances for all business lines leads to a reconciliation of the accounting income statement.

In summary, all these processes contribute to the production of a complete income statement for each business line enabling the profitability and contribution to overall results to be evaluated.

The process of consolidation

In entities with their own financial control team, these two processes are steered locally according to the same standards and principles described in an instruction reference called the Financial Control Procedures and Standards Manual that is common to the entire Dexia Group.

It is organized, monitored and supervised by Group Financial Control who provides all entities with standardized and secure information collection tools for a more reliable and optimized feedback mechanism. Finally, it also consolidates all information.

The process of aggregating information by business line is in parallel to consolidation carried out by the Accounting Department. To maintain the coherence of analytical and accounting information, coherence checks have been put in place.

VI. THE KEY RISKS AND SPECIFIC SYSTEMS OF INTERNAL CONTROL

Banking generates four major types of risk, credit risk, market risk, structural risk (interest rate, exchange rate and cash flow) and operating risk.

If the Dexia SA Risk Control Department oversees and the Group risk management policy under the guidance of the Management Board or specialized risk committees. It sets Group guidelines on limits and delegations, sets and manages the risk surveillance function and it implements risk assessment methods for each of the bank's activities and operational entities.

All these risks are monitored jointly by specialized committees and the Risk control departments using tools developed, in compliance with regulatory and prudential constraints and under limits fixed by the Management Board or by specialized committees.

Subsidiaries and branches are supervised by a local risk management structure. These structures are strictly independent of Front Offices and have a hierarchical (subsidiary) or functional (branch) with the Risk Management Department.

Each local risk management function has one (or several) correspondent(s) for managing operating risks and for implementing the Basel reform. Generally, all risk management systems existing in Dexia SA also exist in each entity, subsidiary or branch.

Beyond the general principles presented above, the resources put in place by Dexia SA to manage risks on a practical, daily level as well as in exceptional circumstances are detailed here.

VI.1 Credit risk

Credit risk is the risk of loss due to the incapacity of customers or other bank counterparties to manage their financial obligations.

The approval process

Any commitment that may lead to a credit risk must be approved under a decision-making system organized according to volume, type of counterparty and the complexity of the commitment.

The system rests on decision-making delegations granted to entities, subsidiaries and branches under very strict rules set out in notation procedures specific to each market and updated annually under the supervision of the Risk Management Department.

This decision-making process is part of limits fixed by the risk management team covering loans to banks and credit extended to sovereign states.

Determining limits

Limits apply to all types of counterparty under technical procedures specific to each type. The system is determined by guidelines fixed by the Group and the Risk Management Team, approved by the Group Credit Risk Policy Committee and implemented in entities and subsidiaries.

Generally, determining limits takes account of Tier One equity to arrive at variable percentages according to internal notation and the size of the counterparties.

Counterparty limits on the banks and sovereign debtors are distributed each year by the Group Risk Management Team between 3 entities, Dexia Bank, Dexia Bil and Dexia Crédit Local who can make transfers between themselves.

Specific rules have been fixed by the Dexia Group for private companies that take into account internal notation and the duration of operations in order to limit equity exposure in case of default.

There are finally, depending on circumstances, "sector" limits such as for example those on telecommunications or German mortgage banks.

Surveillance and feedback

Entity, branch and subsidiary sales teams are the first level of surveillance in a permanent system of monitoring the financial health of their counterparties. Respect for limits is checked on each new commitment decision by the Credit Committee or by delegation.

The second level is the Risk Control Department that receives and consolidates quarterly any exposure, consolidates doubtful debts and consolidates provisions.

Changes to the quality of commitments and respect for limits are examined quarterly (monthly for banking limits) and are reported by the Risk Management Department to the Management Board.

Debt Monitoring Committees meet quarterly to examine changes to sensitive dossiers, their provisioning and possible transfer.

Finally, since the beginning of 2004, Default Committees meetings are held by entity and presided by the Risk Control Department that examine each dossier satisfying criteria fixed by regulators to re-absorb real defaults and reclassification as healthy debt. A Group Default Committee examines counterparties common to several entities.

Consolidated risk management in the entities, subsidiaries and branches is based on the risk procedures already described.

The internal notation system

In agreement with rules applicable throughout the Dexia Group, each counterparty has an internal risk notation. This notation is determined at the beginning of a relationship and is regularly and formally reviewed, in theory annually.

Based, for the local public sector, on expert methods or scoring updated annually, this notation means a decision-making powers for the best categories of risk can be delegated to sales teams on the ground and less well-noted categories of risk can be submitted either to the Risk Control Department, the Dexia Credit Committee or Dexia SA.

The group has central analysis units designated by type of counterparty for local public sector, project financing and local sector private company segments who give internal notations applicable to the entire Dexia Group.

Internal notation for loans to private business, project financing and other specialized finance is subject to detailed individual analysis carried out by specialized central analysis units that take into account the counterparty risk and transaction risk.

The scale of counterparty marks, defined by the Dexia Group has 18 levels including 2 for counterparties in default. This scale can be compared to external notation agencies and gateways have been established to enable each counterparty to find its place in it.

This system, under the responsibility of the Risk Management Department, is essential for Dexia SA which has chosen the most advanced method recommended by regulators and for the reform of the solvability ratio and adequacy of equity. Developments leading from the Basel Reform are being tested on two essential elements, two for probability and loss in case of default.

Funding policy

A Funding Committee, chaired by the Risk Management Department, examines changes to doubtful debts and provisions made and monitors the cost of the risk quarterly.

It decides on levels of funding by country in agreement with levels determined by the Dexia Group Risk Management team.

Dexia SA has this year also started constituting general provisions on a statistical basis. This practice aims to reflect losses inherent in any portfolio but that will be revealed only during its life cycle in the accounts.

VI.2 Market risks

Scope

These are risks from variations in market prices and rates, their interaction and level of volatility. By the very nature of its activity, Dexia SA is not exposed to high levels of market risk.

Monitoring

Risk management in the financial markets is organized around two committees:

The Dexia Group Treasury and Financial Market Risks Committee (TFM) is responsible for defining risk policy (standards, methods of risk calculation and management), allocating equity and fixing limits.

Market committees by entity for locally monitoring the implementation of standards and decisions of the Treasury and Financial Market Risks Committee (TFM) and Correctly Distribute Information to Local Management.

Risks are measured regularly by the Market Risk Management Department that produces a quarterly report on market risks presented to the Management Board.

This report is based on different indicators for monitoring the limits allocated to different risks.

Dexia's main risk indicator is the *Value at Risk* (VaR). Beyond this, risks are measured and limited by other indicators (nominal volumes, sensitivity to rates and spreads, sensitivity of options related to underlying factors and time), calculated by currency.

Counterparty risks associated with these operations are monitored separately.

VI.3 Structural interest rate, exchange rate and cash flow risks

These risks are grouped together under the title Assets/Liabilities Management.

The different elements making up Dexia assets (loans, securities...), liabilities (customer deposits, bond debt...) and off-balance-sheet (financial measurements...) do not have the same characteristics in terms of rates, currency, depreciation or maturity. Residual surpluses or deficits remain on all part of future debts coming to maturity. These differences constitute

interest rate or exchange rate positions that generate market risk. They also represent an imbalance between the application of funds and future resources, generating the cash flow risk.

The purpose of the ALM is to partially or totally cover risks connected with this balance-sheet structure. Except interest rate and exchange rate risks connected to financial markets, all significant Dexia risk from interest rates, exchange rates and cash flow comes under the scope of the ALM committee.

Monitoring

ALM risk management is organized around two committees:

The Dexia ALM committee meets quarterly to check the overall coherence of the group's Asset and Liability Management. This committee also decides on risk measurement procedures and conventions. However, it is not involved, except in exceptional cases, in management decisions that are the responsibility of each entity in the light of the specific nature of their balance-sheet structure.

The entity ALM committees, who meet generally at least monthly, operate within constraints fixed by the group. Residual risks may be kept and managed following decisions made by the ALM committee and in the perspective of long-term management.

They monitor monthly changes to the risk and control limits fixed according to indicators standardized by the Dexia Group.

The main indicator is based on the sensitivity of the Net Current Value of assets and liabilities within the scope of ALM (VAN ALM) at a given variation (100 basis points) of market interest rates.

Interest rates on revenue during the year in progress and the following year as well as the VaR, determined by the same method as that described for market risks, are also taken into account.

VI.4 Operating risks

Operating risks are defined as risks of loss resulting from the inadequacy or failure of procedures, people or internal systems or even external events (catastrophe, fire...). They include risks involving the security of information systems, legal risks and reputation.

Operating risks are closely and constantly examined under internal control procedures and particularly through internal auditing. Action plans are instigated to improve on weak points.

The process of evaluating operating risks

As part of the process launched by the Basel Committee during work reforming the solvability ratio, the Management Board adopted a General Operating Risk Management policy in 2002. The main Group entities appointed an operating risk manager associated with a network of correspondents appointed in each department or entity to properly imbed management principles in the company.

Preliminary work was based around three major strategies:

Collecting, analyzing, recording and processing incidents

Good knowledge of recent operating problems leading to financial loss is key to perfecting understanding of the Dexia risk profile.

A computer facility common to the entire group and dedicated to collecting data relative to operating incidents and losses was therefore developed in 2003. This facility is also a response to reforms proposed by the Basel Committee enabling the Group to constitute a historical record of losses. Operating risk correspondents listed and analyzed incidents. If analyzing incidents leads to the implementation of corrective action, monitoring them will also be the responsibility of these correspondents.

Risk mapping

Beyond listing and analyzing past events, it is essential to supplement this historical data by an analysis of potential events that may have significant impact on the Group.

The same principles as those used as a basis for losses and incidents will be used and a unique procedure will be defined and a common tool will be chosen for the entire Group.

Extensive preliminary work and tests on pilot sites were carried out in 2003. The choice of computer facility to be used for deployment across all activities will be made in the first half of 2004.

Risk mapping will be started in 2004 and completed in 2005.

Sustainable development

Problems arising from this commitment are integrated into the process of evaluating operating risks. In April 1998, Dexia signed the United Nations Declaration of Financial Institutions on the Environment and Sustainable Development, an initiative of the United Nations Environmental Programme. An initial commitment was made in December 2002, when Dexia signed the Global Compact launched by the United Nations.

In September 2003, Dexia adopted the Equator Principles, a set of guidelines developed by a group of international banks for managing social and environmental issues related to the financing of development projects. The Dexia group will apply the principles globally to project finance in all industrial sectors.

IT security:

This covers all systems for protecting information against any threat to its confidentiality, integrity of or availability.

Dexia's policy is based on a set of directives, specific security policies, operating rules and procedures dealing particularly with essential themes like physical security, access controls to systems, databases and applications, respect for regulations and ethical rules or the continuity of activities.

On this last point, a continuity plan has been drawn up cooperation with all operating services under the supervision of a dedicated steering committee. The consequences of an incident

with an effect on premises or information systems, of a failure of safety systems or a loss of service are analyzed under a "business line" angle. Preventive controls are in place to reduce risk of interruption of business to an acceptable level. Procedures for maintaining continuity have been defined to ensure that essential activities may be restored within deadlines that satisfy company requirements. This plan and procedures are maintained and tested regularly.

Operating risk insurance

The Dexia group has taken out insurance contracts covering very extensive areas, such as:

- the risk of damage to movable and immovable assets (fire, explosion, etc)
- fraud or malice (misappropriation, fraud, breach of trust, etc)
- professional liability (in case of errors, omissions or professional misconduct, etc)
- operating liability (in case of physical, material or immaterial damage caused by third parties, etc)
- operating losses (loss of revenue or turnover, extra operating costs and additional, etc...)
- theft of valuables on premises and in safes.
- civil liability of corporate officers (in case of errors or omissions, etc..)

VII. METHOD OF EVALUATING INTERNAL CONTROL

VII.1 The Management Board

The Management Board plays an essential role in evaluating internal control. It has several sources of information enabling it to carry out all its tasks in this field.

The members of the Management Board all have business line or function operating responsibilities. They are therefore highly aware of the constraints and opportunities of their field of activity and are able to define and then judge the effectiveness of internal control.

Specialized committees within Dexia SA are chaired by at least one member of the Management Board and in most cases they comprise most of its members.

The Management Board has also put in place a system of delegations and reporting that imposes on operating departments the presentation and approval of key indicators enabling it, among others, to judge the quality and performance of the internal control system.

Group Audit is also a leading source of information for the Management Board. It is supplied with all audit reports that are debated and commented on during meetings. Moreover, the Management Board may also request internal audit carries out tasks not provided for in the annual audit plan on subjects that seem to require immediate attention. Finally, the Management Board relies on the expertise of internal audit for preparing the report on the state of internal control that, at the request of the prudential authorities, must be produced at least one per year and presented to the audit committee and then the Board of Directors.

Auditors, as part of their role revising accounts and regulators, as part of their inspection role, occasionally make improvement recommendations on specific points of internal control. The Management Board will then take action to implement these recommendations as soon as possible.

VII.2 The Audit Committee

In compliance with principles set out in the Audit Charter, the Dexia SA Board of Directors Audit Committee assists it in its role monitoring the business and management of the Group in application of corporate governance principles.

The role of the Audit Committee is very wide-ranging. It ensures the exactitude and sincerity of Dexia Group company and consolidated accounts as well as the quality of procedures used producing them.

It ensures that risks of any kind to which the Dexia Group is exposed during its activities are properly monitored by reliable and applied procedures.

The Audit Committee reports on its work and observations to the Board Of Directors.

To carry out its tasks, the audit committee has free access to the Auditors, the General Auditor and to the Dexia SA Group Chief Compliance Officer.

It is aware of the conclusions of prudential authority missions and internal audit missions and may request the audit reports. It may suggest further work.

It may call for any information it deems necessary.

Audit Committees, with the same roles and prerogatives, exist in Group operating entities and subsidiaries:

- ◆ whenever required by local legislation or regulation or at the request of prudential control authorities.
- ◆ in the presence of minority interests

Audit Committees therefore exist within Dexia Crédit Local, Dexia Bank and Dexia BIL and in the main subsidiaries of these entities.

VII.3 Preparing the Report

The present report was prepared by the Chairman of the Board of Directors of Dexia SA.

All analyses and descriptions presented are based on information obtained during:

- interviews with the Chairman of the Dexia SA Audit Committee
- interviews with the directors of Dexia SA operating departments
- audit reports carried out by Group Audit and Internal Audit Departments in operating entities.

François Narmon
Chairman of the Dexia SA Board Of Directors