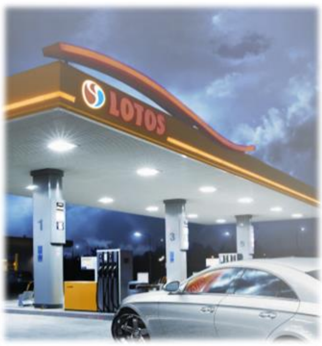
Directors’ Report on the Operations of

Grupa LOTOS S.A.

for 2012

This is a translation of a document originally issued in Polish.





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1. INFORMATION ON GRUPA LOTOS S.A.

Grupa LOTOS S.A. is a vertically-integrated oil company whose business consists in the production and processing of crude oil as well as wholesale and retail sale of petroleum products. It is a producer and supplier of such products as unleaded petrol, diesel oil, light fuel oil, aviation fuel and heavy fuel oil. The Company also specialises in the production and sale of lubricating oils and bitumens.

Grupa LOTOS S.A.'s key market is Poland. In 2012, domestic sales represented 74.8% of the total revenue.

The current business strategy for the years 2011-2015 provides for consolidation of the LOTOS Group's position as a strong, innovative and successfully developing organisation, which plays a crucial role in ensuring Poland's energy security and operates in compliance with the principles of social responsibility and sustainable growth.

Grupa LOTOS S.A. is a joint-stock company, whose shares have been listed on the Warsaw Stock Exchange (WSE) since June 2005.

Through LOTOS Petrobaltic S.A. and LOTOS Exploration and Production Norge AS (LOTOS Norge), the Group is engaged in the exploration for and production of crude oil from the Baltic Sea and the Norwegian Continental Shelf. The Group also has access to onshore hydrocarbon deposits in Lithuania through its subsidiary AB Geonafta. Further development of the exploration and production segment is the priority of the 2011-2015 strategy. One of the objective of the strategy is that the Group's annual production of crude oil is to reach 1.2 million tonnes by in 2015.

Following the completion of the 10+ Programme, the volume of crude oil processed in 2012 reached 9.7 million tonnes, the record high level in the Gdańsk refinery's history.

A country-wide network of about 405 service stations (the fourth largest in Poland) operates under the LOTOS brand. Through the network, the Group markets products and services in the Premium segment. Since 2011, the Group has also offered products and services in the economy segment, where the Group is present through its rapidly developing LOTOS Optima network. By 2015, the Group plans to gain a 10% share in the retail market and maintain its share in the Polish fuel market at 30%. As at the end of 2012, the LOTOS Group's share in retail fuel sales in Poland was 8%, while its share in the domestic fuel market stood at 34.3%.

The workforce at Grupa LOTOS S.A. at the end of 2012 was 1,349 staff. Revenue came in at PLN 31,071.9m, up 14% on 2011. Operating profit in 2012 amounted to PLN 556.3m, while net profit reached PLN 836.4m.

1.1. ORGANISATION AND MANAGEMENT AT GRUPA LOTOS S.A.

In 2012, there were significant changes to the organizational structure of Grupa LOTOS S.A. The changes were effected as a result of changes in the composition of the Grupa LOTOS Management Board S.A., and their objectives included:

- ensuring the proper implementation of the business strategy until 2015,
- raising the standing, decision-making powers, responsibility and effectiveness of the segments,
- enhancing the management model,
- minimising management costs,
- improving segmental reporting,
- enhancing the communication process,
- optimising areas related to financial and accounting support, corporate social responsibility (CSR) and sponsorship, IT management, financial risk management and asset management.

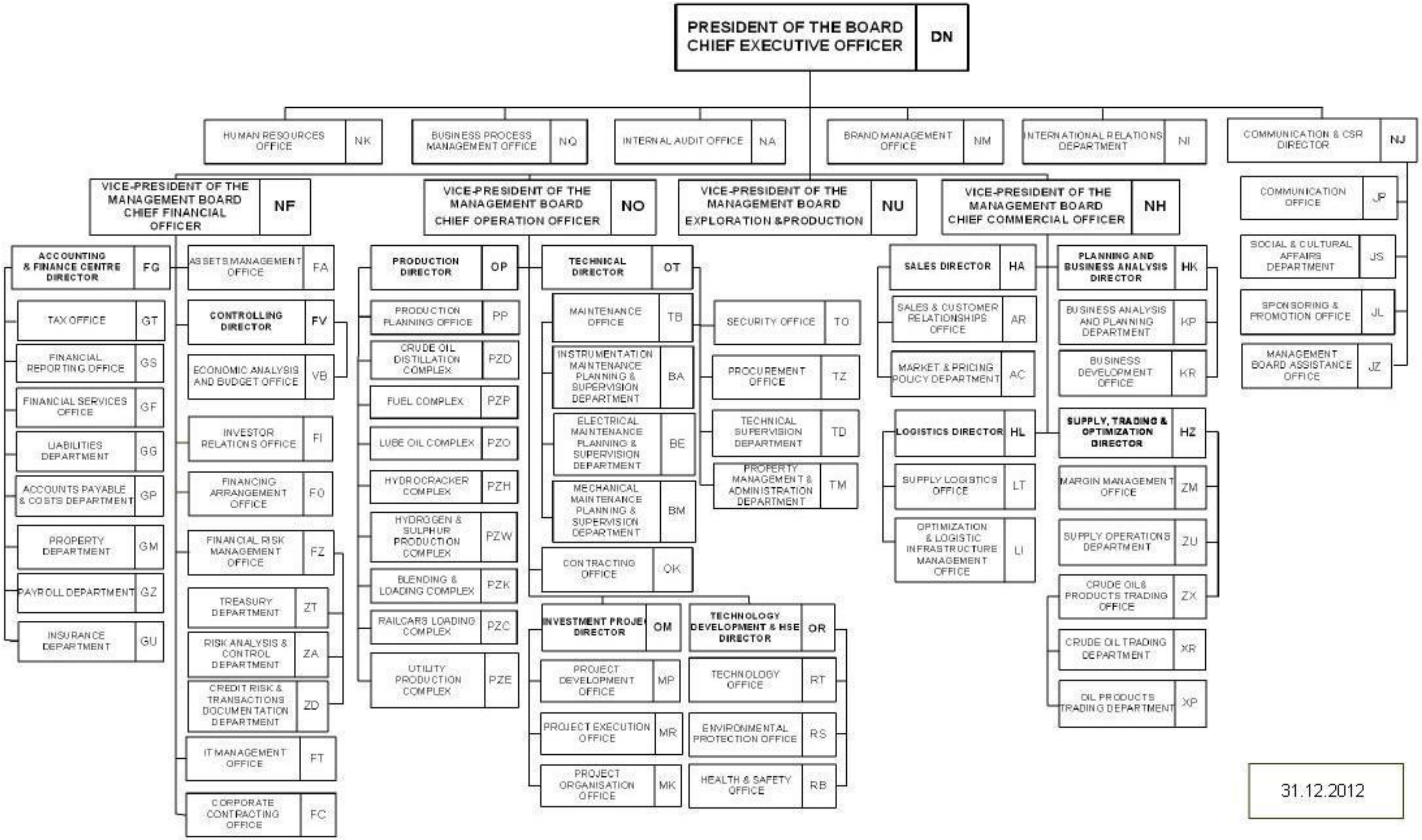
1.1.1. ORGANISATIONAL STRUCTURE OF THE LOTOS GROUP AND GRUPA LOTOS S.A. BRANCHES (PLANTS)

The corporate structure of Grupa LOTOS S.A. reflects the division of competences and relations between various functions and tasks performed at the Company, the hierarchy of organisational units and management. As at December 31st 2012, the corporate structure of Grupa LOTOS S.A. comprised the following units:

- 15 divisions, including 5 divisions reporting directly to the Chief Executive Officer,
- 35 offices,
- 19 departments,
- 8 complexes.

A division is a group of organisational units reporting to specific executive officers who hold decision-making powers within a certain area of the business. Organisational units are separated mainly based on the criterion of the function performed. The basic responsibility of an office is to support the Chief Executive Officer’s or the division directors’ decision-making process. A department is responsible for performing a specific function assigned to it, and ranks one level below an office in the organisational hierarchy. A complex is an operating component of the enterprise, directly performing operating and executory functions.

Grupa LOTOS S.A. has no divisions within the meaning of the Polish Accountancy Act.


PRESIDENT OF THE BOARD CHIEF EXECUTIVE OFFICER DN
HUMAN RESOURCES OFFICE NK
BUSINESS PROCESS MANAGEMENT OFFICE NQ
INTERNAL AUDIT OFFICE NA
BRAND MANAGEMENT OFFICE NM
INTERNATIONAL RELATIONS DEPARTMENT NI
COMMUNICATION & CSR DIRECTOR NJ
COMMUNICATION OFFICE JP
SOCIAL & CULTURAL AFFAIRS DEPARTMENT JS
SPONSORING & PROMOTION OFFICE JL
MANAGEMENT BOARD ASSISTANCE OFFICE JZ
VICE-PRESIDENT OF THE MANAGEMENT BOARD CHIEF FINANCIAL OFFICER NF
ACCOUNTING & FINANCE CENTRE DIRECTOR FG
TAX OFFICE GT
FINANCIAL REPORTING OFFICE GS
FINANCIAL SERVICES OFFICE GF
LIABILITIES DEPARTMENT GG
ACCOUNTS PAYABLE & COSTS DEPARTMENT GP
PROPERTY DEPARTMENT GM
PAYROLL DEPARTMENT GZ
INSURANCE DEPARTMENT GU
ASSETS MANAGEMENT OFFICE FA
CONTROLLING DIRECTOR FV
ECONOMIC ANALYSIS AND BUDGET OFFICE VB
INVESTOR RELATIONS OFFICE FI
FINANCING ARRANGEMENT OFFICE FO
FINANCIAL RISK MANAGEMENT OFFICE FZ
TREASURY DEPARTMENT ZT
RISK ANALYSIS & CONTROL DEPARTMENT ZA
CREDIT RISK & TRANSACTIONS DOCUMENTATION DEPARTMENT ZD
IT MANAGEMENT OFFICE FT
CORPORATE CONTRACTING OFFICE FC
VICE-PRESIDENT OF THE MANAGEMENT BOARD CHIEF OPERATION OFFICER NO
PRODUCTION DIRECTOR OP
PRODUCTION PLANNING OFFICE PP
CRUDE OIL DISTILLATION COMPLEX PZD
FUEL COMPLEX PZP
LUBE OIL COMPLEX PZO
HYDROCRACKER COMPLEX PZH
HYDROGEN & SULPHUR PRODUCTION COMPLEX PZW
BLENDING & LOADING COMPLEX PZK
RAILCARS LOADING COMPLEX PZC
UTILITY PRODUCTION COMPLEX PZE
TECHNICAL DIRECTOR OT
MAINTENANCE OFFICE TB
INSTRUMENTATION MAINTENANCE PLANNING & SUPERVISION DEPARTMENT BA
ELECTRICAL MAINTENANCE PLANNING & SUPERVISION DEPARTMENT BE
MECHANICAL MAINTENANCE PLANNING & SUPERVISION DEPARTMENT BM
SECURITY OFFICE TO
PROCUREMENT OFFICE TZ
TECHNICAL SUPERVISION DEPARTMENT TD
PROPERTY MANAGEMENT & ADMINISTRATION DEPARTMENT TM
CONTRACTING OFFICE OK
INVESTMENT PROJECTS DIRECTOR OM
PROJECT DEVELOPMENT OFFICE MP
PROJECT EXECUTION OFFICE MR
PROJECT ORGANISATION OFFICE MK
TECHNOLOGY DEVELOPMENT & HSE DIRECTOR OR
TECHNOLOGY OFFICE RT
ENVIRONMENTAL PROTECTION OFFICE RS
HEALTH & SAFETY OFFICE RB
VICE-PRESIDENT OF THE MANAGEMENT BOARD EXPLORATION &PRODUCTION NU
VICE-PRESIDENT OF THE MANAGEMENT BOARD CHIEF COMMERCIAL OFFICER NH
SALES DIRECTOR HA
SALES & CUSTOMER RELATIONSHIPS OFFICE AR
MARKET & PRICING POLICY DEPARTMENT AC
LOGISTICS DIRECTOR HL
SUPPLY LOGISTICS OFFICE LT
OPTIMIZATION & LOGISTIC INFRASTRUCTURE MANAGEMENT OFFICE LI
PLANNING AND BUSINESS ANALYSIS DIRECTOR HK
BUSINESS ANALYSIS AND PLANNING DEPARTMENT KP
BUSINESS DEVELOPMENT OFFICE KR
SUPPLY, TRADING & OPTIMIZATION DIRECTOR HZ
MARGIN MANAGEMENT OFFICE ZM
SUPPLY OPERATIONS DEPARTMENT ZU
CRUDE OIL & PRODUCTS TRADING OFFICE ZX
CRUDE OIL TRADING DEPARTMENT XR
OIL PRODUCTS TRADING DEPARTMENT XP
31.12.2012

1.1.2. CHANGES IN ORGANISATION AND MANAGEMENT AT GRUPA LOTOS S.A.

The changes in the organisational structure of Grupa LOTOS S.A. implemented in 2012 by virtue of a resolution of the Grupa LOTOS Management Board were as follows:

In connection with the reorganisation of the Accounting and Finance Centre (FG) and appointment of Accounting & Finance Service Teams delegated to perform tasks for individual subsidiaries of Grupa LOTOS S.A., on July 10th 2012 the following two organisational units were liquidated in the division headed by the Accounting and Finance Centre Director:

a) Trade Accounting Department (GH),
b) Wholesale and Retail Settlements Department (GD).

As of November 1st 2012, the following changes were introduced:

1. <u>within the division headed by the Chief Executive Officer (DN):</u>

   c) liquidation of the Deputy CEO's Division (NW),
   d) within the division headed by the Communication and CSR Director (NJ), the liquidation of:
      - Information Office (JP),
      - Sponsoring, Public Matters and CSR Office (JS),
      - Event Organisation Department (JW),
   e) within the division headed by the Communication and CSR Director, the establishment of:
      - Communication Office (JP),
      - Social and Cultural Affairs Department (JD),
      - Sponsoring and Promotion Office (JL),
      - Management Board Assistance Office (JZ),

2. <u>within the division headed by the Chief Financial Officer (NF):</u>

   a) establishment of the IT Management Office (FT),
   b) establishment of the Corporate Contracting Office (FC),
   c) within the division headed by the Accounting and Finance Centre Director (FG), the establishment of:
      - Insurance Department (GU),
   d) the establishment of the following units directly reporting to the Head of the Financial Risk Management Office (FZ):
      - Treasury Department (ZT),
      - Risk Analysis and Control Department (ZA),
      - Credit Risk and Transactions Documentation Department (ZD).

3. <u>within the division headed by the Chief Operation Officer (NO):</u>

   a) within the Technical Director's Division (OT), the establishment of:
      - Security Office (TO),
      - Property Management and Administration Department (TM).

Also, a new organisational unit was established: Vice-President of the Management Board, Exploration & Production (NU).

1.1.3. OWNERSHIP CHANGES AT THE LOTOS GROUP IN 2012

Changes in share capital of the LOTOS Group companies in 2012

Company	Registration date	Before	Increase / Reduction	After	Currency	Comments
LOTOS Petrobaltic S.A.	Feb 2 2012	96,600,000	2,800,000	**99,400,000**	PLN	issue of 280,000 Series C registered shares with a par value of PLN 10 per share
LOTOS E&P Norge AS*	Jan 14 2012	572,733,964	91,984,477	**664,718,441**	NOK	issue of Series B shares (with a par value of NOK 1 per share)
	Dec 20 2012	664,718,441	115,000,000	**779,718,441**	NOK	issue of Series B shares (with a par value of NOK 1 per share)
	Dec 24 2012	779,718,441	171,000,000	**950,718,441**	NOK	issue of Series B shares (with a par value of NOK 1 per share)
AB LOTOS Geonafta	May 14th 2012	168,256	337,322	**505,578**	LTL	increase in the par value per share from LTL 1 to LTL 3
	Aug 20 2012	505,578	(287,175)	**218,403**	LTL	cancellation of 95,725 own shares with a par value of LTL 3 per share
UAB Genciu Nafta	Jul 13 2012	16,900,000	(16,890,000)	**10,000**	LTL	cancellation of 1,689,000 ordinary shares with a par value of LTL 10 per share

**On January 30th 2013, a resolution on a NOK 53m share capital increase at LOTOS EPN was adopted; the subscription period ends on April 30th 2013.*

Buy-back of shares from the shareholders of LOTOS Petrobaltic S.A.

Event	Date of registration in the share book	Number of shares	Comments
Buy-back of shares from the shareholders of LOTOS Petrobaltic S.A.	Mar 20 2012	26 shares	This transaction completed the voluntary share buyback
Decision on minority squeeze-out	May 24th 2012	-	Excluding shares owned by the State Treasury (i.e. Grupa LOTOS S.A.) which holds 9,934,851 shares, representing 99.95% of the share capital of LOTOS Petrobaltic S.A.
Entry in the share book on mandatory transfer	Dec 20 2012	218 shares	First tranche of shares subject to squeeze-out (transfer of ownership to Grupa LOTOS S.A.)
Entry in the share book on mandatory transfer	Feb 18 2013	470 shares	Second tranche of shares subject to squeeze-out (transfer of ownership to Grupa LOTOS S.A.)

Full control taken of UAB Manifoldas, a subsidiary of AB LOTOS Geonafta

On November 28th 2012, after clearance from the Lithuanian anti-trust authority was obtained and a number of other material contractual conditions were fulfilled, AB LOTOS Geonafta (a subsidiary of LOTOS Petrobaltic S.A.) acquired a 50% interest in UAB Manifoldas. The transaction was executed in performance of the provisions of the conditional share purchase agreement concluded in Vilnius on September 27th 2012 between AB LOTOS

Geonafta and a natural person, concerning sale of 50% of shares in UAB Manifoldas. The transaction enabled AB LOTOS Geonafta to take full control of UAB Manifoldas.

Sale of shares in LOTOS Parafiny Sp. z o.o.

As part of its strategy to focus on the core business, the LOTOS Group sold its shares in LOTOS Parafiny Sp. z o.o. The transaction was completed on January 10th 2012 and involved disposal of 100% of the shares by Grupa LOTOS S.A. to Krokus Chem Sp. z o.o., in which Fundusz Nova Polonia Natexis II and the management staff of LOTOS Parafiny hold shares. As part of the transaction, on November 29th 2011 the parties signed a seven-year agreement on supply of slack waxes by Grupa LOTOS S.A. to LOTOS Parafiny Sp. z o.o. (reported by Grupa LOTOS S.A. in Current Report No. 37/2011 of November 30th 2011).

1.1.4. CHANGES IN ORGANISATIONAL OR CAPITAL LINKS BETWEEN GRUPA LOTOS S.A. AND OTHER ENTITIES

The only significant change in organisational or capital links in 2012 was the acquisition by LOTOS Petrobaltic S.A.'s subsidiary, AB LOTOS Geonafta, of a 50% interest in UAB Manifoldas.

Entities in which the Company directly holds interests in the share capital or in the total vote

Name	Registered office	Business profile	Ownership interest (%)	
			Dec 31 2012	Dec 31 2011
LOTOS Paliwa Sp. z o.o.	Gdańsk	Wholesale and retail sale of fuels and light fuel oil, management of the LOTOS service station network	**100.00%**	100.00%
LOTOS Gaz S.A. w likwidacji (in liquidation)	Kraków	The company does not conduct operations	**100.00%**	100.00%
LOTOS Oil S.A.	Gdańsk	Production and sale of lubricating oils and lubricants, and sale of base oils	**100.00%**	100.00%
LOTOS Asfalt Sp. z o.o.	Gdańsk	Production and sale of bitumens	**100.00%**	100.00%
Technical Ship Management Sp. z o.o.	Gdańsk	On October 1st 2012, the company launched sea transport support activities involving advisory on the operation of ships.	**- (1)**	100.00%
LOTOS Kolej Sp. z o.o.	Gdańsk	Railway transport	**100.00%**	100.00%
LOTOS Serwis Sp. z o.o.	Gdańsk	Maintenance of mechanical and electric operations and controlling devices, overhaul and repair services	**100.00%**	100.00%
LOTOS LAB Sp. z o.o.	Gdańsk	Laboratory analyses	**100.00%**	100.00%
LOTOS Straż Sp. z o.o.	Gdańsk	Fire safety	**100.00%**	100.00%
LOTOS Ochrona Sp. z o.o.	Gdańsk	Personal and property protection	**100.00%**	100.00%
LOTOS Parafiny Sp. z o.o.	Jasło	Production and sale of paraffin	**- (2)**	100.00%
LOTOS Tank Sp. z o.o.	Gdańsk	Until October 16th 2011 – trading in aviation fuel and, as of January 1st 2013 – logistics services	**100.00%**	100.00%
LOTOS Czechowice S.A. (parent company of another group)	Czechowice-Dziedzice	Storage and distribution of fuels	**100.00%**	100.00%
LOTOS Jasło S.A.	Jasło	Storage and distribution of fuels; renting and management of own or leased real estate	**100.00%**	100.00%
LOTOS Petrobaltic S.A. (parent of another group)	Gdańsk	Acquisition of crude oil and natural gas deposits and their exploitation	**99.96% (3)**	99.95% (3)

Name	Registered office	Business profile	Ownership interest (%)	
			Dec 31 2012	Dec 31 2011
LOTOS Park Technologiczny Sp. z o.o.	Jasło	Dormant	**100.00%**	100.00%
AB LOTOS Geonafta (parent of another group)	Gargždai, Lithuania	Crude oil exploration and production, drilling services, and purchase and sale of crude oil	**0.00137%**	0.00137%
LOTOS Biopaliwa Sp. z o.o.	Czechowice-Dziedzice	Production of fatty acid methyl esters (FAME)	**0.005%**	0.005%
RCEkoenergia Sp. z o.o.	Czechowice-Dziedzice	Production and distribution of electricity, heat and gas	**0.005%**	0.005%
LOTOS Exploration & Production Norge AS	Stavanger, Norway	Oil exploration and production at the Norwegian Continental Shelf, provision of services related to oil exploration and production	**0.00000013%**	0.0000002%

(1) On July 31st 2012, Grupa LOTOS S.A. sold 100% of shares in Technical Ship Management Sp. z o.o. (formerly LOTOS Ekoenergia Sp. z o.o.) to Miliana Shipholding Company Ltd.

(2) On November 30th 2011, Grupa LOTOS S.A. and Krokus Chem Sp. z o.o. signed a preliminary agreement to sell 100% of shares in LOTOS Parafiny Sp. z o.o. As at December 31st 2011, the Company disclosed the shares in LOTOS Parafiny Sp. z o.o. under assets held for sale. On January 10th 2012, the Company sold its entire shareholding in LOTOS Parafiny Sp. z o.o.

(3) In exercise of its pre-emptive rights, on December 15th 2011 Grupa LOTOS S.A. subscribed for newly issued Series C shares of LOTOS Petrobaltic S.A. Grupa LOTOS S.A. subscribed for 279,996 shares in the increased share capital of LOTOS Petrobaltic S.A., with a total value of PLN 53,980 thousand, which are disclosed under "Receivables from acquisition of shares in related entities" (see Note 15). On February 2nd 2012, the increase in the share capital of LOTOS Petrobaltic S.A. was registered.

Grupa LOTOS S.A. also continued purchasing shares from non-controlling shareholders as part of the voluntary share purchase process, which was completed at the end of March 2012. In the period from January 1st 2012 to the completion of the voluntary share purchase process, Grupa LOTOS S.A. acquired 26 shares in LOTOS Petrobaltic S.A. with an aggregate value of PLN 3 thousand, representing 0.0003% of the company's share capital.

With respect to the remaining shares held by non-controlling shareholders, excluding the shares held by the State Treasury, on May 8th 2012 the Extraordinary General Meeting of LOTOS Petrobaltic S.A. adopted a resolution regarding minority squeeze-out by the majority shareholder, that is Grupa LOTOS S.A.

As part of the squeeze-out process, by December 31st 2012 Grupa LOTOS S.A. acquired 1,421 shares in LOTOS Petrobaltic S.A. with the aggregate value of PLN 179 thousand, representing 0.0146% of the company's share capital, of which 218 shares with the aggregate value of PLN 28 thousand, representing 0.0022% of the company's share capital, were recorded in the share register.

Following acquisition of shares in LOTOS Petrobaltic S.A. from non-controlling shareholders as part of the voluntary share purchase process and the minority squeeze-out, executed in 2011 and 2012, and the increase in the share capital of LOTOS Petrobaltic S.A., as at December 31st 2012 Grupa LOTOS S.A. held a 99.96% interest in the share capital of LOTOS Petrobaltic S.A., including 9,935,069 shares entered in the share register and representing 99.95% of the share capital of LOTOS Petrobaltic S.A.

1.2. WORKFORCE OF GRUPA LOTOS S.A.

1.2.1. WORKFORCE STRUCTURE OF GRUPA LOTOS S.A.

Grupa LOTOS S.A. workforce structure by type of position (as at December 31st 2012)

Item	Men	Women	Total	FTEs
Blue-collar jobs	512	5	517	521
White-collar jobs	420	412	832	802
Total	**932**	**417**	**1,349**	**1,323**

Grupa LOTOS S.A. workforce structure by education (as at December 31st 2012)

Education	White-collar jobs	Blue-collar jobs	Total	
			Number of positions	%
university-level	655	88	743	**55.00%**
secondary vocational	99	280	379	**28.00%**
secondary general	71	71	142	**11.00%**
basic vocational	6	65	71	**5.00%**
primary	1	13	14	**1.00%**
Total	**832**	**517**	**1,349**	**100.00%**

1.2.2. AGREEMENTS BETWEEN THE COMPANY AND THE MANAGEMENT STAFF AND REMUNERATION, AWARDS OR BENEFITS PAID TO THE MANAGEMENT AND SUPERVISORY STAFF OF GRUPA LOTOS S.A.

Compensation agreements

Apart from standard employment contracts concluded by Grupa LOTOS S.A. with the management staff in 2012, no agreements were executed that would provide for compensation to the management staff in the event they resign or are dismissed without good reason or in the event they resign or are dismissed as a result of the Company's takeover by another entity.

Remuneration paid or payable to members of the Management Board of Grupa LOTOS S.A. for 2012 (PLN '000)

Management Board Members	Short-term employee benefits (salaries and wages)	Length-of-service awards	Share-based employee benefits	Management Board – subsidiaries *	Total remuneration paid
Paweł Olechnowicz	319	-	-	1,081	**1,400**
Marek Sokołowski	315	-	-	641	**956**
Mariusz Machajewski	319	-	-	641	**960**
Maciej Szozda	322	-	-	641	**963**
Zbigniew Paszkowicz	129	-	-	100	**229**
Total	**1,404**	**-**	**-**	**3,104**	**4,508**

** Short-term employee benefits – remuneration paid to the members of the Management Board of Grupa LOTOS S.A. for serving on Supervisory Boards and the Board of Directors of direct and indirect subsidiaries*

Remuneration paid or payable to members of the Supervisory Board of Grupa LOTOS S.A. for 2012 (PLN '000)

Supervisory Board Members	Term of office	Total remuneration paid
Wiesław Skwarko	Jan 1 – Dec 31 2012	41
Leszek Starosta	Jan 1 – Feb 29 2012	10
Małgorzata Hirszel	Jan 1 – Dec 31 2012	41
Oskar Pawłowski	Jan 1 – Dec 31 2012	41
Michał Rumiński	Jan 1 – Dec 31 2012	41
Rafał Wardziński	Jan 1 – Jan 27 2012	6
Marcin Majeranowski	Feb 29 – Dec 31 2012	31
Agnieszka Trzaskalska	Feb 29 – Dec 31 2012	31
Total		**242**

As at December 31st 2012, the Company did not grant any loans or similar benefits to members of its management and supervisory staff.

As at December 31st 2012 and as at the date of release of this Directors' Report, i.e. March 21st 2013, members of the Grupa LOTOS Supervisory Board did not serve on management or supervisory boards of Grupa LOTOS S.A.'s subsidiaries.

1.2.3. CONTROL SYSTEMS FOR EMPLOYEE STOCK OPTION PLANS

In 2012, no control system for employee stock option plans was operated at Grupa LOTOS S.A.

2. OPERATIONS OF GRUPA LOTOS S.A. AND KEY BUSINESS DRIVERS

2.1. LOTOS GROUP'S STRATEGY FOR 2011–2015

The operations of Grupa LOTOS S.A. focus on efficient utilisation of its expanded refining capacities following completion of the 10+ Programme, further increase of the conversion ratio and optimum use of synergies between the refining and the power sectors.

Strategic operating goals:

- - Achieving the world-class standards of production and maintaining a strong competitive position among European refineries;
- - Making optimum use of assets held and acquired as part of the growth strategy;
- - Ensuring safe and stable operation of the production and ancillary facilities, as measured by the minimum annual availability of 98%;
- - Further increasing the conversion ratio and intensifying feedstock processing.

Development of petrochemical business

In 2012, work begun on a new development project – diversification into petrochemical operations. In November 2012, Grupa LOTOS S.A. signed an agreement with Zakłady Azotowe w Tarnowie-Mościcach (Grupa Azoty S.A.) concerning a preliminary feasibility study for a project involving construction of a petrochemical production complex, with two alternatives examined – a pyrolysis (steam cracker) complex with polyolefin production, or an aromatics complex. Once results of the feasibility study are known, design work on the selected alternative can start.

The new project and the alliance with Grupa Azoty S.A. will produce synergies as the process chain will be extended and production of highly-refined products and petrochemical intermediate feedstock will be possible, ensuring efficient utilisation of the existing industrial infrastructure and a close proximity of the Gdańsk port.

The objective behind the Group's marketing activities is to further develop its retail chain and marketing structures based on the extended distribution network and efficient product logistics.

Strategic marketing goals:

- - Maintaining a 30% share in the domestic fuel market;
- - Achieving fuel sales exceeding the fuel production capacities of the Company's refinery by 15%;
- - Securing a 10% share in the domestic retail market by the end of the period covered by the forecast;
- - Developing a network of service stations and intensifying sales through the existing network;
- - Maintaining the leading position on the Polish market for lubricating oils.

Key directions of development until 2020:

- Further optimisation of the management model to achieve the highest available efficiency,
- Access to proved recoverable reserves of hydrocarbons of approximately 330m boe in 2020,
- Output growth to approximately 110 thousand boe/day (equal to 5m tonnes of crude a year),
- Taking steps to optimise the power management processes at the LOTOS Group's refinery through extension of its connections with other power systems.

2.2. OVERVIEW OF INTERNAL AND EXTERNAL DEVELOPMENT FACTORS

External factors

- **Prices of crude oil and petroleum products** – they are material for the Company's financial performance.
- **PLN/USD exchange rate** – the performance of the Company is also affected by foreign exchange rates, as prices of crude oil and of certain products are quoted in the US dollars, and Grupa LOTOS S.A. has debt in that currency.
- **Demand of and supply for petroleum products** – market demand and supply trends have a material impact on the Company's financial performance. The demand for diesel oil is expected to continue to grow in the long run, while the demand for motor gasolines is expected to decline. These trends are reflected in the strategy pursued by the Company.

Internal factors

- **Development of the upstream segment** with a view to strengthening the Company's independence from external sources of feedstock, improvement of financial performance and enhancement of Grupa LOTOS S.A.'s shareholder value;
- **Strengthening of the market position** of the LOTOS brand, with special emphasis on the development and improved profitability of retail sales;
- **Optimisation of operations in the production and sales segment**, through effective use of the assets which have been modernised or delivered under the 10+ Programme;
- **Efficiency enhancing measures** taken up in line with the Optimum Expansion Programme adopted by the Management Board. As at the end of 2012, the total effect of the efficiency enhancing, cost saving measures and planned investment cuts at the LOTOS Group was PLN 446m.

2.3. LOTOS GROUP'S BUSINESS RISKS

The Company and its Group strive to improve their tools and methods used to identify and assess risks and implement adequate risk hedging/mitigating strategies. The measures taken helped reduce exposure to risks in 2012. Some risks materialised, which triggered procedures to reduce their impact. New risks were identified, including those related to changes in the technologies used at the Gdańsk refinery.

Risk management system at the LOTOS Group

The LOTOS Group implemented an enterprise risk management (ERM) system based on the COSO II integrated framework released in 2004, which is compliant with ISO 31 000 guidelines and requirements.

Relevant internal standards have been developed and implemented, including:

- **LOTOS Group Enterprise Risk Management Policy**, which defines the general scope of responsibility within the system and key risk management policies operated by the organisation,
- **procedure: LOTOS Group Enterprise Risk Management**, which specifies detailed rules for risk identification and assessment, monitoring and reporting methods, and reviews aimed to check if the mitigation measures taken have brought the expected results.

Key risk management instruments

The LOTOS Group identifies risks which may affect the achievement of its strategic, process and operational objectives. Risk is evaluated based on the Risk Assessment Matrix approved by the Company's Management Board. Based on the criteria defined in the Matrix, major, moderate and minor risks are identified. The strategy for addressing a given risk depends on its detailed analysis and impact on the Company and its environment.

Risk assessment is undertaken from two different time perspectives – the following year and until the end of the period covered by the LOTOS Group's strategy (until the end of 2015). For each risk, the probability of its occurrence is estimated, followed by an assessment of its possible impact on the Group's financial standing and reputation The assessment takes into account the expected impact on safety of people, environmental impact and reception by key stakeholders.

Relevant controls and security measures are indicated for registered risks. Each risk has its owner, who is responsible for overseeing the risk, monitoring it in line with adopted criteria and implementing agreed mitigation plans.

The existing rules of risk identification and assessment allow us to promptly respond to threats, so as to mitigate or altogether eliminate them. Thanks to response plans, it possible to adequately prepare for the occurrence of a given risk. The LOTOS Group also identifies newly emerging opportunities and possibilities, and strives to exploit them. The enterprise risk management enables the Company to undertake activities optimal for its business (within the acceptable risk limits).

Risks and opportunities in the context of strategy for the petroleum sector prepared by the Polish government and the European Commission

In 2012, the LOTOS Group undertook a number of initiatives to predict and minimise risks related to Polish and EU legislation. The Company monitored European Union's petroleum sector policy by cooperating with international organisations, such as CEEP (Central Europe Energy Partners), CONCAWE and the Polish Organisation of Oil Industry and Trade (POPiHN), and participated in public consultations on draft legislation.

- **Polish legislation on biofuels and NIT -** in January 2012, the notification procedure was completed for domestic regulations allowing a higher biocomponent content in diesel oil. The long-expected rule approving the use of diesel oil with a 7% ester content (B7) was finally adopted in 2012. In the same year, the Group took advantage of the statutory regulations of May 2011, which provided for a reduction of the NIT target level by a ratio of 0.85 upon fulfilment of certain statutory requirements concerning the origin of biocomponents. As the same regulation can be used in 2013, the application of the reduction ratio may contribute to lower costs of meeting the NIT.

2008	2009	2010	2011	2012	2013
3.45%	4.60%	5.75%	6.20%	6.65%	7.10%

Grupa LOTOS S.A. implements the reduced NIT by taking advantage of the regulations pursuant to which companies purchasing at least 70% of biocomponents (in terms of mass) from producers registered with the Agricultural Market Agency may lower their NIT by a ratio of 0.85. The Company applies the regulation to liquid fuels and liquid biofuels for which quality requirements are stipulated in the Act Amending the Act on Monitoring and Control of Fuel Quality and certain other acts, that is for:

BB gasolines, known as E95/E98 gasolines, containing up to 5% v/v of pure bioethanol or bioethanol in ETBE,

diesel oils known as B-7 oils, containing up to 7% v/v of FAME (Fatty Acid Methyl Esters),

B100 – 100% higher fatty acid esters, which are intrinsic fuels.

- **risk of failure to meet the NIT-** in Poland, the National Indicative Target is attained exclusively through the use of biocomponents and biofuels. Achieving the target level has a tangible effect on transport energy costs. Although the amendment is a good solution, the LOTOS Group is convinced that the maximum level of NIT should be determined on the basis of fuel quality standards, so that the legally required content of biocomponents and biofuels in transport fuels in the coming years does not exceed the biocomponent content in standard fuels. A level of the NIT higher than provided for in the fuel quality standards necessitates the introduction of 100 per cent biodiesel (B100) to the market. Given the current fuel prices, the use of B100 must be minimised, as its market launch will have adverse financial effects. In 2012, the application of the NIT reduction ratio and approval of the B7 use contributed to minimising the sale of B100. At present, fuel companies expect that the next step aimed at minimising the role of B100 in meeting the NIT in 2013 will involve launch of gasoline with a 10% bioethanol content (E10), approval of the oil co-hydrogenation technology in the production of diesel oil in Poland and introduction of a double settlement standard for biofuels/biocomponents from waste materials, e.g. used frying oil. It is also expected that the possibilities of achieving the NIT will be expanded to include the use of other renewable energy sources, such as biogas or green power.
- **risk related to the draft Energy Law -** the draft Energy Law prepared by the Ministry of Economy as part of the planned set of three energy acts was particularly important for the petroleum sector in 2012. In the section on liquid fuels, the draft Energy Law provides for withdrawal of licences for liquid fuel production, storage, transmission and trading in Poland. Instead, these services would become regulated activities, requiring only entry into the petroleum operations register maintained by the President of the Energy Regulatory Office. In the opinion of sector players who are members of the POPiHN, this solution could facilitate circumvention of the mandatory stocks system, the NIT system, the excise duty act or other relevant regulations. In consequence, it may lead to the expansion of the black market, thus threatening the business of fuel companies operating legally.
- **risk related to regulations concerning mandatory stocks -** given the need to implement the Directive 2009/119/EC, the work on the amendment to the act on mandatory stocks of oil and fuels will be continued. The act is expected to be adopted in near future. At first its implementation may entail higher costs for the petroleum sector, but ultimately the companies will be released from the obligation to maintain mandatory stocks.

Risks related to changes and interpretations of the tax law

The LOTOS Group operates in an unstable tax and legal environment. Furthermore, Grupa LOTOS S.A., as a member of domestic organisations of employers and entrepreneurs, takes a role in issuing opinions on draft legislation. This is primarily aimed at improving the quality of tax legislation, but also allows to adequately respond to any changes in the legal environment. The Group updates its internal procedures to ensure compliance with legal requirements and to identify and mitigate any tax risks, and in particular their effect on the Group's financial statements.

- **tax risk related to transactions** may arise following a change in tax law interpretation. The differing interpretations of tax rules increase business uncertainty and, as regards international trading, may tarnish our reputation as a reliable partner and force the LOTOS Group to give up on valuable projects or transactions. In situations where a tax risk related to a possibility of disparate interpretations is identified, the LOTOS Group avails itself of the right to request a binding interpretation of tax law by the Minister of Finance.
- **risk related to non-observance by the legislator of the vacatio legis principle** while enacting amendments to tax laws. This prevents businesses from adjusting to the new requirements on time and increases the likelihood of incurring additional costs or sanctions.
- **risk related to the planned introduction of tax on extraction of minerals in Poland -** the planned introduction of new tax solutions concerning the extraction of minerals creates the need to re-evaluate the E&P segment's performance. According to the "target" proposals of the Ministry of Finance presented in 2012, the tax will apply to all hydrocarbons, all types of deposits and all entities involved in production of those minerals. Therefore, an increase in tax burden is expected. At present, the tax burden (the government take, or the state's share in pre-tax profit) is approximately 27%. The total amount of tax and charges payable by the upstream industry following the planned change will be approximately 40% of the pre-tax profit. The tax on natural gas and oil produced will be 5% and 10%, respectively. In addition, a special hydrocarbon tax was proposed, in the amount of 25% of the surplus of revenue over expenses. Mineral production royalty is also expected to rise. Pursuant to the draft, the charge, currently at PLN 5.89 or PLN 4.90 for 1,000 cubic metres of gas, will reach PLN 24 for 1000 cubic metres. The corporate income tax rate and the real estate tax payable by upstream companies to municipalities or communes are to remain flat at 19% and 2%, respectively. Given the taxation of gas and oil, the planned changes will affect the Group's performance.
- **risk related to introduction of tax on energy in the European Union -** the European Commission's proposals aimed at changing the energy taxation system, including transport energy, are designed to make tax rates depend on fuel's calorific value and CO2 emissions. Such modifications may entail the risk of altering the structure of transport fuel demand by 2020.

Financial risks

The financial risk management policies and instruments and the impact of the key risk factors on the individual items of financial results are described in Section 33 of the consolidated financial statements.

- **Risk related to prices of raw materials and petroleum products** - work is currently in progress on the development of a new policy for managing the risk based on the Energy Trading and Risk Management (ETRM) system. In 2012, work commenced on the implementation of the Allegro 8.0 system. The project is scheduled to be completed in 2014.
- **Currency risk** is managed in line with the Strategy of Currency Risk Management at Grupa LOTOS S.A. The US dollar (USD) is the currency of the market we operate in. Consequently, as regards its operating activities,

the Company has a structurally long position in the US dollar. The US dollar was chosen as the currency for contracting and repaying long-term loans.

- **Interest rate risk** is connected with the expected schedule of payments under the loans taken out to finance inventories and the implementation of the 10+ Programme, and the resulting interest accruing at floating rates (LIBOR USD).
- **Liquidity risk -** in 2012, real cash pooling and IT tools enhancing the efficiency of liquidity management were implemented at the LOTOS Group.
- **Counterparty credit risk in financial transactions –** the LOTOS Group concludes transactions exclusively with financial institutions or companies holding the minimum acceptable credit rating assigned by rating agencies or an appropriate guarantee, if they do not hold their own credit ratings at the required levels, issued by a financial institution or company holding the minimum acceptable credit rating assigned by credit agencies and meeting the requirements adopted by LOTOS Group and resulting from contractual obligations. Credit limits for counterparties in financial transactions are determined in reference to the Company's equity and a ratio calculated based on credit ratings updated on an ongoing basis. The utilisation of credit limits is monitored on a regular basis
- **Counterparty credit risk in trade transactions** is managed in line with an internal procedure whereby the creditworthiness of a counterparty applying for an open credit limit is verified. The LOTOS Group companies award such a credit limit in reference to the result of an assessment of trade counterparties' creditworthiness, which is performed by analysing available data and information concerning the company being assessed. The final decision on the credit limit amount is made by the person responsible for credit risk in line with the assigned profile of responsibilities. The utilisation of credit limits is monitored on a regular basis

Risks related to upstream activities

Upstream operations involve risks at each stage of work performed, i.e. during exploration, development of and production from fields. All risks at each work stage are identified and a risk mitigation strategy is developed.

- **Exploration risk -**a risk of incorrect estimation of in-place resources. To mitigate that risk, such resources are estimated for three scenarios P10/P50/P90 (in accordance with the SPE 2007 resources classification system), which means that quantities are given that can be potentially recovered with the 10%, 50% and 90% probability. Necessary geological work and analyses are performed to document the potential prospects and provide a sufficient basis for a decision whether to drill exploration wells. These steps are taken to increase the Chance of Success (CoS) rate and provide a real-term estimation of potential hydrocarbon resources in the analysed prospects.
- **Production risks -** risks related to the process of production of hydrocarbons. These include risks of oil spills, marine collisions, fires, gas eruptions or other failures, which can have major consequences for the Company and the natural environment. Therefore, a number of measures have been implemented to mitigate that risk, such as leakage testing, blow-out risk prevention by securing boreholes, and monitoring of fire risks. A key element helping to reduce the risk is the appropriate awareness and competences of the personnel. Procedures applicable in day-to-day work and when a threat of failure occurs have been put in place and are being reviewed.
- **Technical risk** is mitigated through monitoring of the condition and performance of the equipment, as well as technical supervision and performance of necessary tests. The production and process systems are subject to technical inspections and reliability tests. The specific nature of upstream operations requires that the Company constantly develop its precautionary approach and operation maintenance system and monitor the best technologies available in this area.

Operating risks

In 2012, a technological change was made at the Gdańsk refinery, involving the introduction of high-pressure gas as the main energy carrier. Gas from a new pressure reduction station now flows to the refinery's fuel gas network, through which it fuels process furnaces and, separately, the CHP plant, as well as to two hydrogen production plants, where it is used as production feedstock. Switching to natural gas as the main fuel entails a number of benefits for the Company, including ecological (emissions of sulphur dioxide, nitric oxides, dust and carbon dioxide are lower than when heavy fuel oil or LPG were used), financial (natural gas is a cheaper fuel and generally a cheaper commodity than the ones it has replaced) and commercial ones (additional petroleum products are available to be placed on the market). However, these changes carry new risks for Grupa LOTOS S.A.

- **risk of sudden stoppage in gas supply** (e.g. due to failure of a gas reduction station),
- **risk of limited availability of gas** in the case of a severe winter – this could lead to lower sales of products (mainly LPG) and higher operating costs to the Company. Grupa LOTOS S.A. maintains the infrastructure enabling it to switch back to the fuels which were used before natural gas was introduced.
- **Risks related to the supply of raw materials** - feedstock for production is supplied mainly via a system of pipelines and by sea transport. The Company strives to diversify the directions and sources of oil supply. Security of crude supplies is enhanced through progressive expansion of our presence on the international oil market, regular contracting of various types of crude transported by sea, creating conditions to radically increase their share in total supplies to the refinery, and increasing the role of own production. Our competitive position is improved by fully capitalising on the coastal location of the Gdańsk refinery and the possibility to source crude supplies through two independent channels: Russian oil through the Druzhba Pipeline and various types of oil available through Naftoport (offshore oil terminal). An appropriate selection of types of crude and directions of supplies is the result of efforts to maximise the integrated margin. Diversification-related risks, including risks related to potential disruptions at multiple sources of oil supply, are identified and mitigated.
- **technical risk** - ongoing activity carried out by Grupa LOTOS S.A. to ensure continuous operation and control of production infrastructure guarantees safe operation and undisturbed functioning of the refinery. The refinery also uses technologies and equipment meeting the BAT (*Best Available Techniques*) criteria. Process units are equipped with safety and protection solutions, including multi-layered security systems (prevention, protection and counteraction layers). Alarm, emergency stop and shutdown systems are deployed in order to prevent uncontrolled development of an emergency situation and serious damage to the plant and equipment.
- **risks related to the preparation and carrying out of the Spring 2013 Maintenance Shutdown** at the Gdańsk refinery - the Company is involved in planning and scheduling work with a view to limiting the downtime. Given the current unstable situation on the construction market, the risk of deterioration of the financial condition of contractors to be potentially engaged to perform overhaul work is taken into account. Such worsening of contractors' financial situation could result in delays or non-performance of some of the planned work. The Company applies relevant controls and prevention measures with a view to limiting this risk to the minimum.
- **risk relating to safety at work** - each work post is assessed from the point of view of occupational risk, including with respect to the presence of any explosive materials, noise or exposure to hazardous biological or chemical substances. Based on such assessment, individual and collective security systems are deployed and continuously improved.
- **risks related to CO_2** emission limits - having implemented during the period of National Allocation Plan II (2008–2012) its development programme as a result of which over a two-year time span new installations were launched and the manner of operation of existing installations changed, entailing a significant increase in carbon dioxide emissions, Grupa LOTOS S.A. faced a considerable challenge of having to acquire a large volume of

additional allowances from the national reserve to cover the emissions from its new installations. For the entire five-year trading period under the ETS (Emissions Trading Scheme), there was no need for the Company to purchase additional allowances to cater for its increased needs. For 2013-2020, crude oil refineries will obtain allowances calculated on the basis of the a CWT ("Complexity Weighted Tonne") benchmark.

- **risks** related to the European Commission's actions taken to **reduce the emission allowances under the ETS**. So far there are no transparent regulations, whether at the European Commissioner at the national level, concerning the National Reduction Target provided for in Art. 7a of Directive 2009/28/EC. This will therefore require greater involvement of the industry representatives in providing support to the state administration in the process of implementation of this directive into the Polish law. Currently, thanks to the introduction of new solutions, Grupa LOTOS S.A. is not exposed to the risk of changing prices of CO2 emission units, however the EU's policy aimed at introducing the so-called backloading or at further limitation of CO2 emissions may have an adverse effect on the LOTOS Group. In this situation, working on the CEEP platform, Grupa LOTOS S.A. is trying to prevent the backloading concept from being actually put in place.
- **risk of stricter quality requirements for petroleum products -** the LOTOS Group has been monitoring proposed standards and regulations affecting its production and technical activities, through Technical Committee 222 at the Polish Committee for Standardisation, responsible for petroleum products and process liquids. The LOTOS Group may also have a say on quality requirements, in particular requirements applicable to engine fuels, through participation in the works of an industry association, the Polish Organisation of Oil Industry and Trade (POPiHN). The participation substantially reduces the risks of delayed compliance with future quality standards for petroleum products.

Marketing risks

The background for our marketing activities is the ever-present price competition and the fast-changing global macroeconomic environment. Therefore, the LOTOS Group continuously improves the tools it uses for monitoring parameters related to such areas as prices and margins.

- **risk of smaller internal demand** for products due to growing pricing pressures or macroeconomic conditions. Growing unemployment may mean reduced consumption of products and services. The Company uses various distribution channels to sell its products, pursues a pricing policy guaranteeing competitiveness of its products and optimises its operating expenses.
- Risk management in the marketing area is also focused on ensuring an uninterrupted supply of products to the market. The process is coordinated through the cooperation of the sales, logistics, production, and trading and optimisation areas. The purpose of all the actions that are taken is to set coherent and optimised development directions for the entire supply chain.

Environmental risks

The activities conducted by the LOTOS Group, starting from oil and gas exploration and production, to end with oil refining, have or may have an impact on the natural environment.

- **risk of non-compliance with the legal requirements concerning environmental impact** is minimised through ongoing monitoring of the Polish and EU laws, their efficient implementation and participation in legislative processes.
- **The risk of environmental disaster** caused by a tanker leaking oil or petroleum products is mitigated by ensuring compliance with standards of safety in sea transport and maintaining cooperation with shipowners who observe maritime conventions and meet strict safety requirements.

Reputational risk

Materialisation of the reputational risk could have an adverse effect on the value of the LOTOS brand. All risks identified within the LOTOS Group are evaluated in the financial and reputational aspect; they are analysed and relevant mitigation plans are prepared. Systemic measures taken with respect to reputational risk in 2012 included implementation of a number of initiatives limiting the risk of abuses as part of two programmes: the Ethical Conduct Programme and the Abuse Risk Management Programme.

2.4. INDUSTRY OVERVIEW

Macroeconomic environment

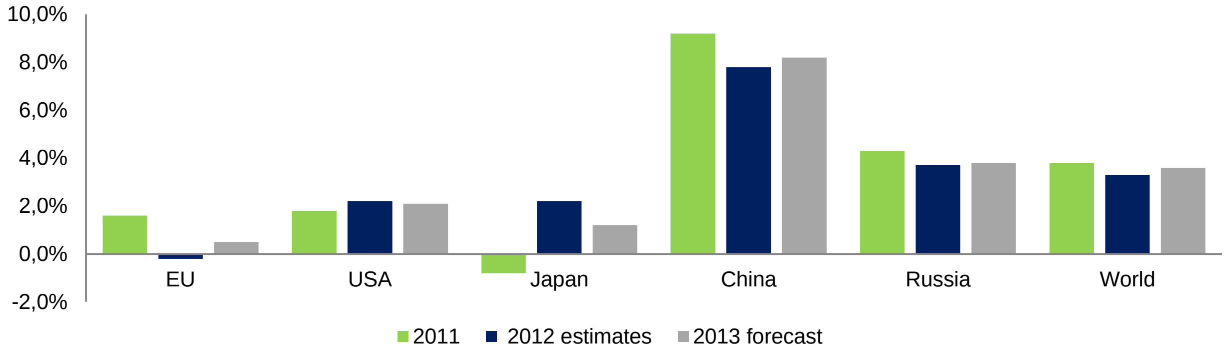
The global economic situation in 2012 was below market expectations. The largest world economies retained a slight growth in the positive territory, but growth rates were lower than in previous years.

In many developed countries financial stability, growth in production and unemployment reduction were supported by actions aimed at introducing more relaxed monetary policy and enhancing market liquidity. In large part, lack of confidence on the market is caused by turmoil in many countries as well as the difficulties in pursuing a balanced fiscal policy.

In 2012, the global economy continued to grow, but the estimated growth rate (3.3%) will be lower than expected half way through the year (0.2pp below the forecast from July 2011). The forecast for 2013 has been affected by a slightly stronger downward correction (of 0.3pp), which has set the expected GDP growth rate at 3.6%.

Despite the remedial action taken by the Member States, the euro area crisis remains the largest threat to the global economic revival. It is estimated that in the euro area 2012 would end with a negative GDP growth rate of (-) 0.4%. Concurrently, a slight pickup in economic growth of 0.2% is expected in the Member States in 2013.[1]

GDP growth in 2011-2013

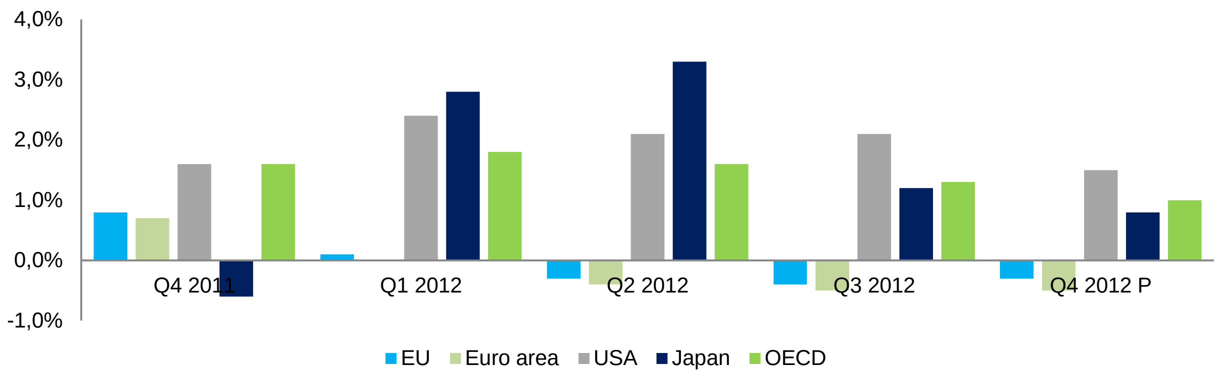


Source: In-house analysis based International Monetary Fund data, October 2012.

The economic difficulties and threats in developed countries (to a large extent attributable to excess government debt) will require further support in the form of appropriate monetary policy, conservative fiscal policy, and further structural reforms.

GDP growth in 2011 and 2012 (y-o-y change)

[1] *World Economic Outlook, International Monetary Fund, October 2012.*



Source: In-house analysis based on Eurostat, OECD, and International Monetary Fund data.

The key internal driver setting the direction for the Company's development and priorities was its continued effort aimed at using its production potential, which has increased and become more flexible following the completion of the 10+ Programme.

- **Situation in the refining sector**

Despite adverse economic conditions, global demand for crude oil increased in 2012 (with a prevailing downward trend in consumption in the developed countries and higher consumption on the developing markets)[2] and crude prices went slightly up.

Industry organisations are estimating average demand for the commodity in 2012 at 89.2 mb/d, which is about 0.9% (0.8 mb/d) more than a year earlier. The average consumption of crude in 2013 is expected to come in at 90.1 mb/d, up 0.9%.[3] Medium-term forecasts by the International Energy Agency (IEA) predict that demand for crude will exceed 95 mb/d in 2017, meaning a compound average growth rate (CAGR) of 1.3%.

IEA estimates indicate that the global growth is driven by rising demand for the commodity in developing countries. In non-OECD countries, growth was estimated at 2.8% in 2012 and is expected to remain at 2.6% (or 44.7 mb/d) in 2013. On the other hand, consumption in developing countries, which was down 1.1% in 2012, may decline by a further 0.7% (to 45.8 mb/d) by 2013. IEA estimates indicate that these trends will prevail in the mid-term, that is until 2017. In 2012, crude oil consumption in Europe was estimated at 14.5 mb/d. It is expected that in 2013 the demand will drop to 14.3 mb/d[4].

- **Competition in the refining sector**

Owing to its state-of-the-art installations built in 2007-2010 as part of the 10+ Programme, the refinery operated by Grupa LOTOS S.A. in Gdańsk processes 10.5m tonnes of crude per year. With a value of nearly EUR 1.43bn, the +10 Programme has been the largest industrial investment project in Poland in the last decade. During its implementation, the company cooperated with global suppliers of state-of-the-art solutions for the petrochemical industry, such as Shell, ABB, CB&I, KBR, Technip and Lurgi. Thanks to the application of the latest technologies, the refinery became a "green", environmentally-friendly and safe production plant.

Key competitors in the region:

- Płock refinery (Orlen Group), Poland – processing capacity of approx. 16m tonnes

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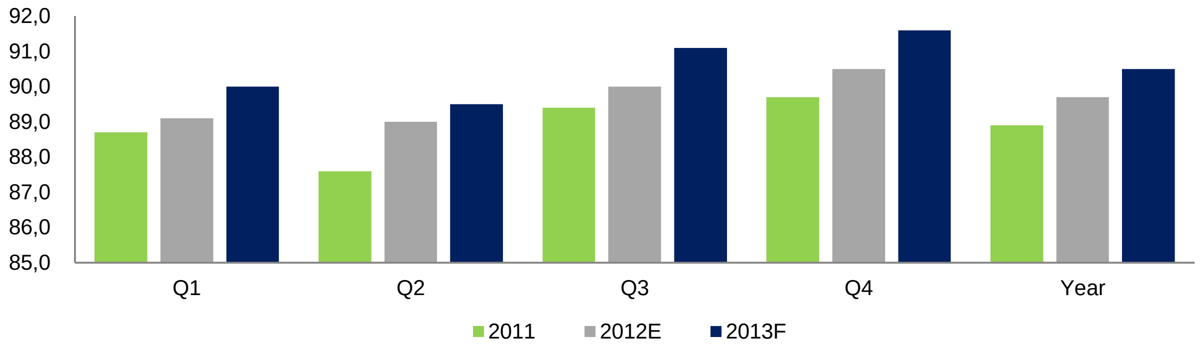
[2] *Oil Market Report, IEA, November 2012.*
[3] *In-house compilation based on OPEC, IEA and US EIA data.*
[4] *Oil Market Report, IEA, November 2012 and December 2012.*

- Schwedt refinery (PCK Raffinerie GmbH), Germany – approx. 12m tonnes
- Leuna refinery (TOTAL Group), Germany – approx. 11m tonnes
- Schwechat refinery (OMV), Austria – approx. 10m tonnes
- Możejki refinery (Orlen Group), Lithuania – approx. 10m tonnes
- Bratislava refinery (Slovnaft, MOL Group), Slovakia – approx. 6m tonnes
- UniPetrol refineries in Kralupy, Litvinov and Pardubice (Orlen Group), the Czech Republic – approx. 4m tonnes

Demand for crude oil (mb/d)



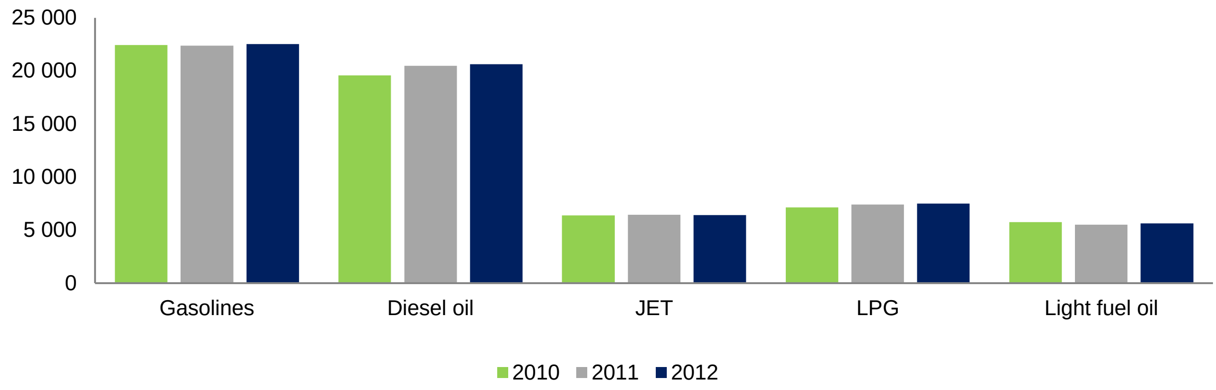
Source: In-house analysis based on IEA data, December 2012.

- **International fuel market**[5]

It is estimated that demand for oil refining products rose in 2012 by 0.7% globally. Stronger demand was also recorded in the gasolines (0.6%) and diesel oil (0.8%) segments. The estimated consumption of LPG and light fuel oil also increased (by 1.2% and 1.8%, respectively). However, the demand for jet fuel slightly fell (-0.4%).

[5] *Mid-Term Oil Market Outlook 2012-2017, JBC Energy, October 2012*

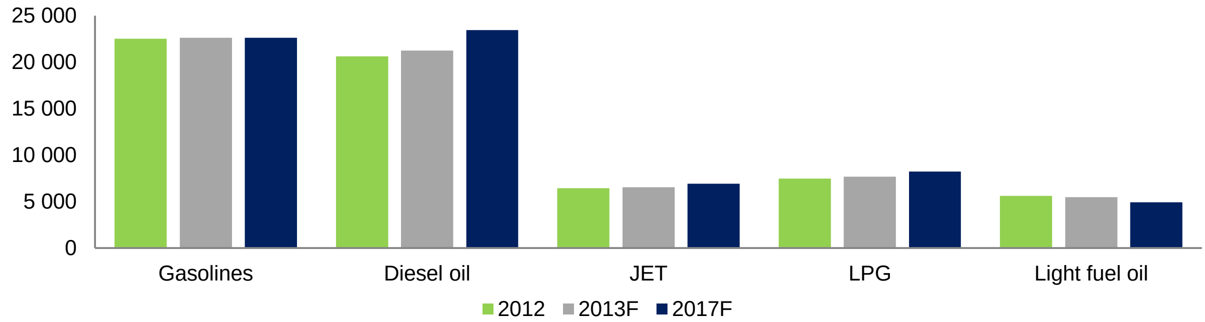
Global consumption of fuels (mbd)



Source: In-house analysis based on JBC data, October 2012.

According to forecasts, overall global consumption of refining products is expected to grow by over 5% until 2017. A significantly higher demand for diesel oil, LPG and JET fuel has been estimated for 2012 (up by 14%, 10% and 8%, respectively). The consumption of gasolines should remain relatively unchanged. Demand for light fuel oil is expected to fall by 13%.

Forecast global consumption of fuels (mbd)

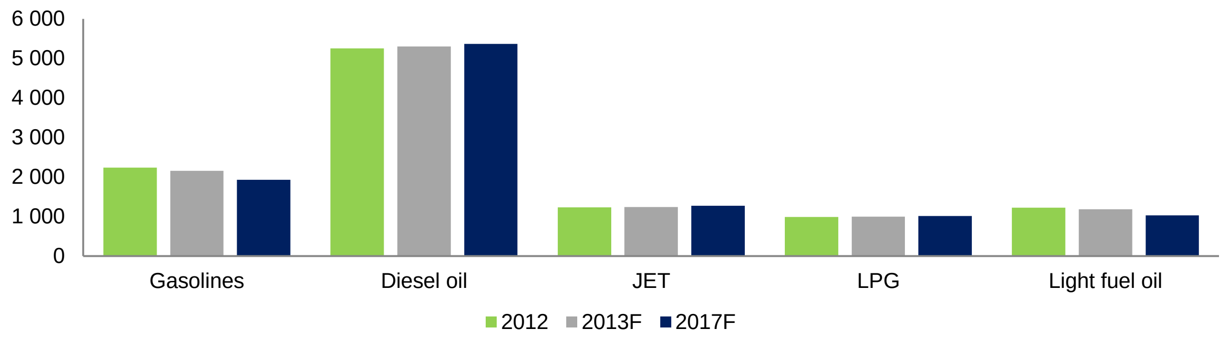


Source: In-house analysis based on JBC data, October 2012.

Consumption of petroleum products in Europe is estimated to decline in 2013 by nearly 3%. The forecast drop in consumption will affect all product groups: gasolines (-4.9%), diesel oil (-1.2%), JET fuel (-2.9%), LPG (-2.7%) and light fuel oil (-2.2%). Lower consumption of fuels in Europe reflects the economic difficulties in the EU Member States and the euro area.

The demand for oil refining products is forecast to fall in Europe by 3% until 2017. According to estimates, one of the reasons behind the decline will be a significant drop in consumption of gasolines by nearly 14%. Lower consumption is also expected on the light fuel oil market (-16%). Concurrently, a strong increase in consumption of middle distillates is expected: diesel oil - by 2.1%, and JET fuel - by 2.8%.

Forecast consumption of fuels in Europe (mbd)



Source: In-house analysis based on JBC data, October 2012.

In the European car market, new passenger car registrations fell significantly (by 7.8%) in 2012, to 12.5m new cars, whereas in the utility vehicles segment new registrations declined by 11%, to 1.6m vehicles (in January-November).

In the group of registered new passenger cars, an increasing interest in diesel fuelled cars has been observed since 2009. The share of such cars in the total new car registrations in Western Europe was nearly 60% (compared with 46% in 2009).[6]

- **Macroeconomic environment in Poland**

In 2012, the GDP growth rate in Poland declined. According to preliminary estimates, GDP in real terms grew by 2.3% over 2011, which is the lowest growth rate since 2009. The decline is chiefly attributable to weaker domestic demand and lower industry and construction output sold. Inflation was down to 3.7%.

According to estimates, the economic slowdown in Poland in 2012 was accompanied by higher unemployment. It is estimated that the unemployment rate was 13.2% in 2012, which was higher by 0.7pp than a year before. After 11 months of 2012, salaries and wages in the non-financial corporate sector increased by 3.6% compared with the corresponding period in 2011, which did not translate into a stronger purchasing power.

- **Polish fuel market**

Despite the previous upward trend in diesel oil consumption in Poland, it is estimated that the growth of demand for the fuel was negative in 2012. This is believed to have been caused by the economic slowdown, and in particular by weaker performance of the construction and transport industry than in prior years, as well as lower growth rate of domestic demand. The average annual retail price of diesel oil has rapidly grown over the last few years. In 2011, it soared 18.1%, and in 2012 it went up by approximately 12.5%. The retail price of approximately PLN 5.60 recorded at the end of 2011 proved to be the limit at which consumers reduced their diesel oil consumption. According to preliminary estimates, diesel oil consumption in 2012 dropped by 6.1%, to 12,5 million tonnes.

Similarly to other European countries, the demand for gasoline declined for another consecutive year, driven by growing prices since 2009, weaker purchasing power and reduced fuel consumption of vehicles driven in Poland.

[6] *European Automobile Manufacturers' Association, www.acea.be*

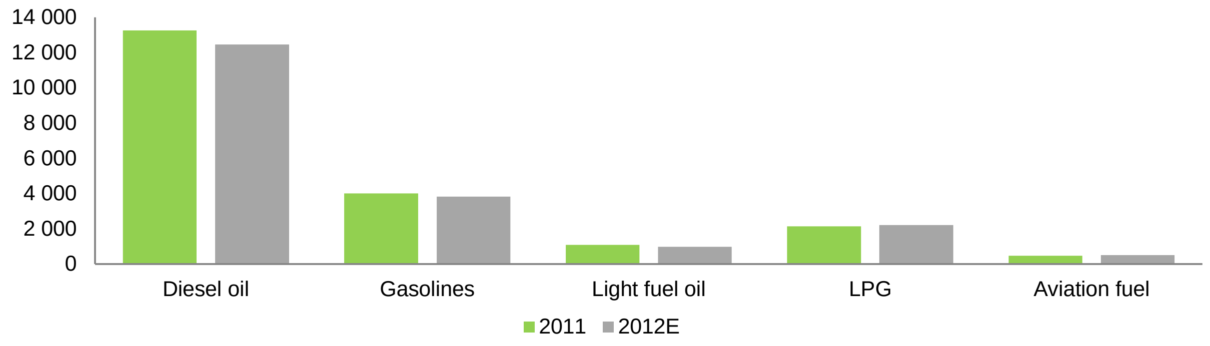
Another factor was the dieselisation of vehicles in Poland. In effect, the demand for gasoline in Poland is estimated at 3.8 million tonnes in 2012, with negative growth of (-) 4.4%.

Given the high prices of gasoline, LPG, a less expensive alternative fuel, gained popularity. In 2012, the estimated consumption of LPG exceeded 2.2 million tonnes. The demand for LPG grew by 2.7%. For several years, the demand for light fuel oil has weakened. The availability of other heating fuels has reduced the demand for light fuel oil in Poland. According to preliminary estimates, light fuel oil consumption in Poland was 1 million tonnes in 2012, which was 10.8% lower than in 2011.

The demand for diesel oil, gasoline, LPG and light fuel oil is estimated to have dropped in aggregate by approximately 5% in 2012. No significant improvement is expected in 2013.

In 2012, owed to hosting the Euro 2012 championship, the estimated passenger traffic at Polish airports increased, as a result of which the consumption of aviation fuel grew by 7% in 2012, to 0.5 million tonnes. Over the last few years, the number of passengers using Polish airports has grown, which resulted in an average annual growth rate of jet fuel consumption of 5%.

Consumption of fuels in Poland ('000 tonnes)

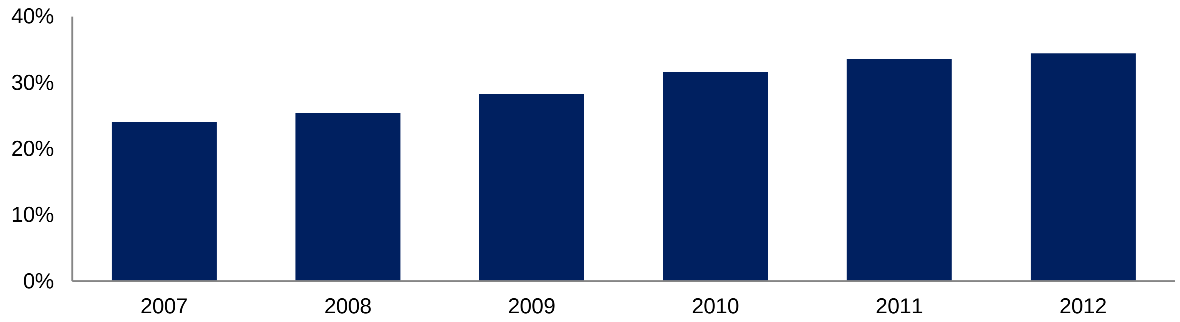


Source: In-house analysis based on Polish Organization of Oil Industry and Trade (POPiHN) data.

- **Market position**

Strengthening the leading sales chains, as well as active search for new growth opportunities helped Grupa LOTOS S.A. increase its market share in the Polish fuel market to 34% in 2012 (up 0.4pp on 2011).

LOTOS Group's share in the domestic fuels market



Source: In-house analysis based on Polish Organization of Oil Industry and Trade (POPiHN) data.

2.5. KEY PRODUCTS, MERCHANDISE AND SERVICES

2012 was another record year for Grupa LOTOS' refinery. The volume of crude oil processed was 9.67m tonnes, the highest in the history of the Gdańsk refinery, which means **that the average annual utilisation rate of the refinery's installed capacities slightly exceeded 92%.** The utilisation of the refinery's installed capacities was adjusted during the year to reflect the prevailing market conditions. Throughput was increased in periods with high refining margins, for example in September and October 2012, when the utilisation rate exceeded 100%.

Key products

- **LOTOS DYNAMIC 98 unleaded gasoline** – modern fuel offering better performance and engine protection than standard products. The gasoline contains antioxidants and washing additives which support better cleaning of the engine, lengthen its useful life and economise fuel consumption.
- **LOTOS DYNAMIC DIESEL diesel oil** – fuel for diesel engines, especially valued by operators of delivery vehicle and lorry fleets. Owing to the use of friction-reducing components, it offers more power efficiency of the engine and guarantees start-up at -32°C. The additives significantly improve nozzle flow capacity and engine lubricity, extend useful life and improve performance of the engine.
- **LOTOS RED heating diesel oil** (ONDCO) – owing to its unique additives and low sulphur content, the product has exceptional parameters in terms of oxidation resistance, anti-corrosive action and maintaining cleanness of nozzles, thus extending the useful life of heating equipment. In addition, emissions of noxious combustion products have been significantly reduced.
- **IZ40 diesel oil** – arctic fuel, guarantees engine start-up at very low temperatures (CFPP of -32°C).
- **LPG** – mixture of liquefied hydrocarbons, consisting primary of propane and butane. With both gasses mixed in correct proportions, the LPG can achieve optimum working parameters.
- **LOTOS Quazar engine oils** – premium product based on state of the art technologies. The product line, which was designed for distribution through the chain of Authorised Service Stations, is for cars which have been used for less than three years. The LOTOS Quazar LLIII 5W-30 oil meets one of the most stringent technical specifications for passenger cars in the world – the German norm VW 504.00/507.00 It is an example of the modern engine oil concept, which is no longer universal, but dedicated to specific users of specific car makes. In 2012, a cooperation agreement was executed with the Association of Volksvagen and Audi Dealers in Poland, which brings together authorised dealers of cars manufactured under VW's German, Spanish and Czech marques. Following the agreement, they joined the group of partner brands, which previously comprised Subaru and KIA.
- **LOTOS Thermal Control engine oils** – product line comprising synthetic, semi-synthetic and mineral products dedicated to passenger cars.
- **LOTOS TURDUST engine oils** – product line for HGVs. The oils meet the requirements of leading engine producers such as Man, Scania, Tatra, MB, Volkswagen, Volvo and Renault and have been approved by them.
- **Industrial oils** is a category comprising gear, hydraulic, turbine and machine oils, as well as industrial lubricants. Grupa LOTOS is consistently expanding the range of products in the hydraulic (**Hydromil**), gear(**Transmil**) and turbine oil (**Remiz**) **product lines.**
- **TDAE and RAE class plasticizers** offered under the QUANTILUS **T50 and QUANTILUS T60 brands**,

used by European and Asian tire and rubber manufacturers. These products meet the requirements of the EU REACH directive concerning the registration of chemical products and have been approved by global tire manufacturers.

- **MODBIT modified bitumens** – state-of-the-art bitumens enhancing pavement resistance to rutting, extending pavement durability and increasing resistance to extreme weather conditions. In 2012, the production technology for rubber-modified bitumen was developed. The new product will be commercialised in 2013.
- **Xylene fraction** is a product launched in 2012, obtained through reformate splitting. It is used as feedstock in plastics production. The xylene separation will further diversify Grupa LOTOS S.A.'s product portfolio and reduce the share of aromatic hydrocarbons in the range of gasoline components produced by the Gdańsk refinery. This will contribute to greater technological flexibility of the refinery, while allowing it to sell some of the components on the fuel or petrochemical market.

Grupa LOTOS S.A.'s revenue by products, merchandise and services

	in the period Jan 1 - Dec 31 2012		in the period Jan 1 - Dec 31 2011	
	PLN '000	**% share**	**PLN '000**	**% share**
Gasolines	5,152,513	**16.6%**	4,463,914	**16.4%**
Naphtha	1,097,071	**3.5%**	480,080	**1.8%**
Reformate	458,827	**1.5%**	477,264	**1.8%**
Diesel oil	15,921,515	**51.2%**	14,791,005	**54.2%**
Light fuel oil	1,129,026	**3.6%**	1,194,980	**4.4%**
Heavy fuel oil	2,140,840	**6.9%**	1,580,725	**5.8%**
Aviation fuel	1,856,016	**6.0%**	1,395,004	**5.1%**
Bunker fuel	125,360	**0.4%**	107,446	**0.4%**
Bitumen production components	1,311,047	**4.2%**	1,431,047	**5.2%**
Base oils	698,124	**2.3%**	695,655	**2.6%**
Liquid gas	354,351	**1.1%**	146,858	**0.5%**
Other refinery products, merchandise and materials	720,326	**2.3%**	411,273	**1.5%**
Total petroleum products, merchandise and materials	**30,965,016**	**99.7%**	**27,175,253**	**99.6%**
Other merchandise and materials	8,167	**0.0%**	10,504	**0.0%**
Services	115,804	**0.4%**	103,647	**0.4%**
Effect of accounting for cash flow hedge accounting	(17,091)	**-0.1%**	(90)	**0.0%**
Total	**31,071,896**	**100.0%**	**27,289,314**	**100.0%**

Grupa LOTOS S.A.'s sales by products, merchandise and services

	in the period Jan 1 - Dec 31 2012		in the period Jan 1 – Dec 31 2011		2012/2011 change
	thousand tonnes	% share	thousand tonnes	% share	%
Gasolines	1,508	**15.1%**	1,447	**14.4%**	**4.2%**
Naphtha	356	**3.6%**	174	**1.7%**	**104.0%**
Reformate	130	**1.3%**	164	**1.6%**	**-20.4%**
Diesel oils	4,586	**45.8%**	4,755	**47.4%**	**-3.6%**
Bunker fuel	51	**0.5%**	39	**0.4%**	**31.7%**
Light fuel oil	338	**3.4%**	404	**4.0%**	**-16.4%**
Heavy fuel oil	1,049	**10.5%**	910	**9.1%**	**15.2%**
JET A-1 fuel	543	**5.4%**	457	**4.6%**	**18.9%**
Base oils	219	**2.2%**	213	**1.5%**	**2.8%**
Bitumen components	757	**7.6%**	978	**9.9%**	**-22.6%**
LPG	140	**1.4%**	64	**0.9%**	**117.8%**
Other refinery products, merchandise and materials	343	**3.4%**	270	**3.8%**	**27.1%**
Total petroleum products, merchandise and materials	**10,019**	**100.0%**	**9,874**	**100.0%**	**1.5%**

In 2012, Grupa LOTOS S.A.'s sales volume increased by 1.5%, to 10,019 thousand tonnes.

Like in the previous years, diesel oil had the largest share in the total sales volume. In 2012, the sales volume of diesel oil was 4,586 thousand tonnes, which accounted for 45.8% of total sales. The second largest item in the structure of the Company's sales were gasolines, whose share in total sales volume was 15.1%. The sales volume of gasolines in 2012 was 1,508 thousand tonnes, having grown year on year by 4.2%. The last item with an approximately 10% share in the Company's total sales volume was heavy fuel oil, whose share in total sales was 10.5%. The sales volume in this product group stood at 1,049 thousand tonnes in 2012 and was 15.2% up on 2011.

Grupa LOTOS S.A.'s sales by products and markets

		in the period Jan 1 - Dec 31 2012		in the period Jan 1 - Dec 31 2011		Change 2011/2010
		thousand tonnes	**% share**	**thousand tonnes**	**% share**	%
Domestic sales	Gasolines	1,105	**11.0%**	1,092	**14.8%**	**1.2%**
	Diesel oils	4,249	**42.4%**	4,645	**63.1%**	**-8.5%**
	Bunker fuel	51	**0.5%**	39	**0.6%**	**31.7%**
	Light fuel oil	338	**3.4%**	404	**5.5%**	**-16.4%**
	Heavy fuel oil	91	**0.9%**	113	**1.5%**	**-20.0%**
	JET A-1 fuel	110	**1.1%**	79	**1.1%**	**40.2%**
	Lubricants	0	**0.0%**	0	**0.7%**	**-**
	Base oils	134	**1.3%**	134	**0.1%**	**-0.2%**
	Bitumen components	757	**7.6%**	978	**9.4%**	**-22.6%**
	LPG	130	**1.3%**	64	**1.3%**	**102.6%**
	Other refinery products, merchandise and materials	320	**3.2%**	161	**2.0%**	**98.3%**

Domestic sales, total		**7 284**	**72.7%**	**7,709**	**73.4%**	**-5.5%**
Export sales	Gasolines	403	**4.0%**	355	**13.3%**	**13.5%**
	Naphtha	356	**3.6%**	174	**6.5%**	**103.8%**
	Reformate	130	**1.3%**	164	**6.1%**	**-20.4%**
	Diesel oils	337	**3.4%**	110	**4.1%**	**206.4%**
	Bunker fuel	0	**0.0%**	0	**0.0%**	**-**
	Heavy fuel oil	958	**9.6%**	797	**29.8%**	**20.3%**
	JET A-1 fuel	433	**4.3%**	378	**14.2%**	**14.5%**
	Base oils	85	**0.9%**	79	**5.2%**	**8.0%**
	LPG	10	**0.1%**	0	**1.3%**	**-**
	Other refinery products, merchandise and materials	24	**0.2%**	109	**8.9%**	**-78.3%**
Total export sales		**2,735**	**27.3%**	**2,165**	**26.7%**	**26.3%**
Total		**10,019**	**100.0%**	**9,874**	**100.0%**	**1.5%**

Domestic sales declined by 425 thousand tonnes in 2012 (down by 5.5% year on year), with a concurrent increase in export sales, whose volume went up by 569 thousand tonnes (up by 26.3% year on year). The key factors driving up Grupa LOTOS S.A.'s export sales in 2012 included an increase in the volume of diesel oil sold (up by 227 thousand tonnes, or 206.4% year on year, to 337 thousand tonnes), and a rise in the volume of naphtha sold (up by 182 thousand tonnes, or 103.8%, to 356 thousand tonnes). Also, 2012 saw an increase in domestic sales of the following products: JET A-1 fuel (up by 40.2%, to 110 thousand tonnes), gas (up by 102.6%, to 130 thousand tonnes) and other refinery products (up by 98.3%, to 320 thousand tonnes). Domestic sales was adversely affected by lower consumption of diesel oil relative to 2011, which resulted in an 8.5% decline in Grupa LOTOS's sales volume of the product, to 4,249 thousand tonnes. The Company also recorded a decline in the volume of light fuel oil and bitumen component sales (down by 16.4%, to 338 thousand tonnes, and 22.6%, to 757 thousand tonnes, year on year, respectively). Sales of base oils remained close to their 2011 level, at 134 thousand tonnes.

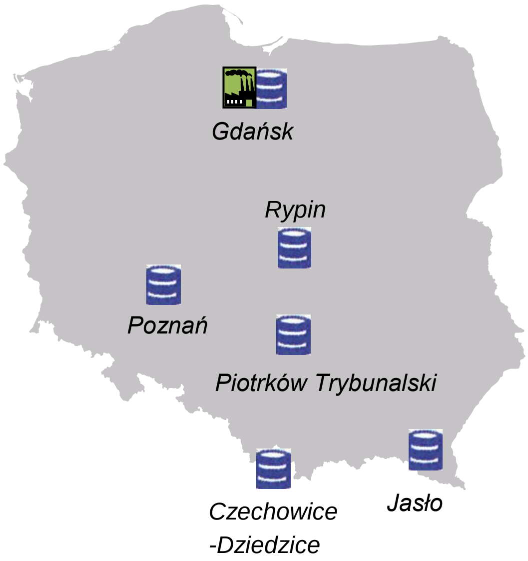
Grupa LOTOS S.A.'s net revenue by markets

	in the period Jan 1–Dec 31 2012		in the period Jan 1–Dec 31 2011	
	PLN '000	**% share**	**PLN '000**	**% share**
Domestic sales:	23,242,552	**74.8%**	21,955,979	**80.5%**
- *products and services*	22,405,127	**72.1%**	21,595,141	**79.2%**
- *merchandise and materials*	837,425	**2.7%**	360,838	**1.3%**
- export sales:	7,829,344	**25.2%**	5,333,335	**19.5%**
- *products and services*	7,829,344	**25.2%**	5,132,174	**18.8%**
- *merchandise and materials*	-	**0.0%**	201,161	**0.7%**
Total	**31,071,896**	**100.0%**	**27,289,314**	**100.0%**

Grupa LOTOS S.A.’s key customers

In both 2012 and 2011, the main customers whose share in Grupa LOTOS S.A.'s total revenue exceeded 10% were LOTOS Paliwa Sp. z o.o. (wholly owned by Grupa LOTOS S.A.) and Shell POLSKA Sp. z o.o. (to the best of the Company's knowledge, no formal links existed between Grupa LOTOS S.A. and Shell POLSKA Sp. z o.o. as at the date of the Directors’ Report on the operations of Grupa LOTOS S.A., except for trade agreements). The respective shares of those companies were: 40.56% and 10.06% in 2012, and 44.51% and 10.99% in 2011.

2.6. LOGISTICS



Refinery *Storage depot*

Grupa LOTOS S.A. takes measures to enhance the logistics and distribution of products, raw materials and components. The actions taken include optimisation of the fuel terminal network, of rail, sea and road transport, taking into account customer expectations, and of seasonal changes in sales, as well as engaging in efforts aimed to reduce costs throughout the logistics chain.

- In 2012, the scope of logistics services was extended, new IT systems for information and data exchange were implemented, the fuel distribution offering was broadened and the process of secondary logistics management was significantly improved. At the same time, preparatory work was conducted to achieve full automation and centralisation of the driver service process at own depots. Planned for completion in 2013, the project will enable standardisation of work and improvement of cost efficiency.
- Smooth operation of the logistics system ensured security of product distribution at Grupa LOTOS S.A., helped meet the statutory requirements on the **creation, maintenance and turnover of mandatory stocks** and enabled the Group to **attain the National Indicative Target** for marketed bio-components.
- In 2012, the Company earned additional revenue from sales of logistics services also to third-party customers, including quality inventory exchange and the **stock ticket service**, consisting in the fee-based maintenance of mandatory reserves of fuels.
- **Freight transport by sea** is a vital element of Grupa LOTOS S.A.'s logistics chain. The Company enjoys a considerable advantage offered by the direct access to product pipelines linking the Gdańsk refinery to the

liquid fuel handling facilities at Port Północny. Sea transport is the main mode of exporting petroleum products and supplying a significant portion of raw materials and components for production. The number of tankers carrying the Company's imports and exports was slightly reduced in 2012, relative to 2011, primarily as a result of optimising the volume of cargo (larger export cargoes of petroleum products, particularly heavy fuel oil) and changing the structure of biocomponent suppliers (significant share of supplies from domestic companies).

- **The liquid fuel handling terminal** operated by Naftoport handles tankers with maximum draught of 15 metres and the capacity to load up to 150 thousand tonnes of crude oil or petroleum products. This allows Grupa LOTOS S.A. to export the surplus products and sell them mainly on the markets of Scandinavia, Northern and Western Europe and the Baltic states. The direct connection to the port also makes it easier to arrange for and carry out import deliveries of petroleum products, mainly the diesel oil and light fuel oil component.
- Grupa LOTOS S.A. enjoys an advantageous position of having a refinery in a short distance from a cargo handling terminal, which allows it to **diversify the sources of supply** and facilitates the shipping of crude oil from the Company's own reserves under the Baltic Sea and in Lithuania and, in the near future, crude oil produced from the reserves under the North Sea.
- Grupa LOTOS S.A. is consistent in its efforts to take over the management of cargo transportation by sea, or to **control the transportation process on the longest possible section of the supply chain**, from the affreightment of ships to the formal handling of sea transport. This ensures greater control and helps streamline the planning process as regards cargo handling at sea ports, allowing the LOTOS Group to reduce the frequency of ship detention and optimise the related costs. In 2012, Grupa LOTOS S.A. took over most of the activities related to securing vessels for sea transport on its own, cutting out third-party intermediation services.
- In 2012, the Company continued **design work related to construction of the sea cargo handling terminal in Martwa Wisła**, in the immediate vicinity of the Gdańsk refinery. The aim of the project is to enable handling of component and product loads with a unit volume of up to five thousand tonnes for exports and imports on Grupa LOTOS S.A.'s own wharf.
- In 2012, LOTOS Kolej operated **rolling stock of ca. 3.6 thousand rail cars** (mainly for the transport of petroleum products) and nearly **100 locomotives**, including one of the most modern electric locomotives: Bombardier TRAXX MS/DC and Siemens ES64F4.
- **Trading and optimisation –** Activities in this area in 2013 will focus on optimising the structure of crudes, which will mainly involve increasing the share of crude supplied by sea. It is expected that deliveries of crude produced by LOTOS Geonafta in Lithuania will start. Work will continue on improving and further integrating the key functions and competences necessary for integrated margin management.
- Grupa LOTOS S.A.'s export sales volumes will depend on the volumes sold in the domestic market, but also on the volumes of crude processed at the Gdańsk refinery and the crude processing structure. Export sales volumes may fall slightly due to the maintenance shutdown of the refinery planned for spring 2013.
- As part of **optimisation of the supply chain** products supplementing the Company's petroleum product mix will be purchased or borrowed. These activities will be particularly intensified during the maintenance shutdown of the Gdańsk refinery.

Grupa LOTOS S.A.'s purchases of raw materials, merchandise and petroleum materials by region

	in the period Jan 1–Dec 31 2012		in the period Jan 1–Dec 31 2011	
	PLN '000	% share	PLN '000	% share
Domestic purchases	3,100,768	10.9%	2,744,616	10.1%
Foreign purchases	25,469,045	89.1%	24,346,144	89.9%
Total purchases	28,569,813	100.0%	27,090,760	100.0%

Grupa LOTOS S.A.'s structure of purchases

	in the period Jan 1–Dec 31 2012		in the period Jan 1–Dec 31 2011	
	PLN '000	% share	PLN '000	% share
Raw materials	28,155,822	93.8%	26,755,406	94.3%
Merchandise	412,334	1.4%	334,312	1.2%
Services	1,092,747	3.6%	981,019	3.5%
Materials	213,451	0.7%	193,572	0.7%
Other purchases*	141,226	0.5%	98,780	0.3%
Total	30,015,579	100.0%	28,363,089	100.0%

**Including tangible assets, tangible assets under construction, prepayments for tangible assets under construction and intangible assets.*

Grupa LOTOS S.A.'s structure of purchases – petroleum products for resale

	in the period Jan 1–Dec 31 2012		in the period Jan 1–Dec 31 2011	
	PLN '000	% share	PLN '000	% share
Diesel oils	192,119	46.6%	83,857	25.1%
Gasolines	220,216	53.4%	249,618	74.7%
Other	-	-	837	0.2%
Total	412,335	100.0%	334,312	100.0%

Grupa LOTOS S.A.'s structure of purchases – raw materials, semi-finished products, chemicals and petroleum materials

	in the period Jan 1–Dec 31 2012		in the period Jan 1–Dec 31 2011	
	PLN '000	% share	PLN '000	% share
Crude oil	25,173,632	89.5%	22,863,835	85.5%
Diesel oil	322	0.0%	657,683	2.5%
MTBE/ETBE gasoline components	332,258	1.2%	295,020	1.1%
FAME	1,463,107	5.2%	1,584,587	5.9%
Gasolines	574	0.0%	40,591	0.1%
Heavy fuel oil	58,339	0.2%	209,861	0.8%

Ethyl alcohol	181,691	**0.6%**	167,220	**0.6%**
Additives	30,592	**0.1%**	25,209	**0.1%**
Gasoil	149,369	**0.5%**	109,065	**0.4%**
Diesel oil components	342,900	**1.2%**	747,426	**2.8%**
Natural gas	406,005	**1.4%**	51,386	**0.2%**
Other	18,691	**0.1%**	4,565	**0.0%**
Total	28,157,480	**100.0%**	26,756,448	**100.0%**

Grupa LOTOS S.A.'s key suppliers

As in 2011, also in 2012 Grupa LOTOS S.A. had two suppliers whose share in total supplies exceeded 10% of Grupa LOTOS S.A.'s total revenue: Switzerland-based Mercuria Energy Trading and UK-based Petraco Oil Company Ltd. Their shares in Grupa LOTOS S.A.'s purchases were as follows: 53.84 % (2011: 37.54 %) and 12.16 % (2011: 29.99 %). To the best of the Company's knowledge, as at the date of publication of this Director's Report there were no formal links between Grupa LOTOS S.A. and any of the suppliers named above, except for trade agreements.

2.7. ENVIRONMENTAL PROTECTION

Grupa LOTOS S.A.'s mission is to pursue innovation-oriented and sustainable development with due regard for the natural environment.

In 2012, expenditure on environmental investments increased. Following completion of the refinery's expansion under the +10 Programme, Grupa LOTOS S.A. focused on improving the efficiency of units installed prior to 2008. The Company's environmental projects are designed to enhance energy efficiency of individual components, lower the use of consumables, reduce fugitive emissions and redirect flare gas.

Grupa LOTOS S.A. is taking active part in an initiative launched by the Minister of Economy, the goal of which is to prepare a document setting out the key challenges facing Polish enterprises by 2050.

The vision of sustainable development described in this document prioritises the following six key areas: social capital; human capital; infrastructure; natural resources; energy; as well as the government's quality and institutions.

In 2012, the Company started to use natural gas as feedstock for hydrogen production and the main fuel, which allowed it to achieve two objectives:

- lower the emissions of carbon dioxide, a basic greenhouse gas, by 100 thousand tonnes in 2012
- lower the emissions of power-generated pollutants, including sulphur dioxide and dust, by approximately 1.5 thousand tonnes and 150 tonnes, respectively.

In 2012, expenditure on environmental investments increased. Following completion of the refinery's expansion under the +10 Programme, Grupa LOTOS S.A. focused on improving the efficiency of units installed prior to 2008. The Company's environmental projects are designed to enhance energy efficiency of individual components, lower the use of consumables, reduce fugitive emissions and redirect flare gas.

Grupa LOTOS S.A.'s environmental fees in 2010-2012 (PLN '000)

	2012	2011	2010
Air emissions	2,980	4,268	3,817
Water withdrawal	140	144	160
Wastewater discharge	298	313	306
Waste landfilling	0	0	0
Total	**3,418**	**4,725**	**4,283**

2.8. RESEARCH AND DEVELOPMENT

Following changes in the applicable laws, in 2012 Grupa LOTOS S.A. developed a technology for and launched a new type of diesel oil with a FAME content of up to 7%.

The Company's R&D activities focused on developing technologies for producing and optimising processes at the oils unit. The key R&D achievements in 2012 included:

- R&D work on production of Group II base oils of high viscosity of >10 cSt at 100 ^{0}C from paraffin fraction,
- developing the technology, production and sale of a Group II base oil with low viscosity of <5.6 cSt at 100 ^{0}C as feedstock in the production of enhanced-quality engine oils,
- developing the technology, production and sale of Group I base oils using the new product – paraffin fraction. Oil efficiency was improved, which helped enhance the energy profile and utilisation rates of the oils unit. Group I+ base oils have a low sulphur content, a better evaporation rate as tested by the Noack method, a higher content of saturated hydrocarbons, and a very high viscosity index (99–110),
- development of the technology, production and sale of low-sulphur light paraffin wax using the new product – paraffin fraction. Low-sulphur paraffin wax is used to manufacture various types of paraffin and paraffin products,
- production and sale of *Base Oil SAE 10 LS* and *Base Oil SAE 30 LS* with sulphur residue below 0.5%m/m, to be used as feedstock for production of higher quality engine oils.

In the scope of road bitumen production technologies:

- R&D work continued on designing a production technology for environmentally friendly bitumen binders with scrap rubber added for use with road mineral-bitumen compounds. In 2012, the final stage of the research work was completed, which involved validation of product properties in final application – test sections were laid using rubber-modified bitumen MODBIT 45/80-55 CR. The thermostability and rheological properties of the bitumen binder in mineral-bitumen compounds were confirmed in practice, which means the product can be brought to market in 2013,

2.9. MATERIAL EVENTS IN 2012

Implementation of the strategy

Despite the dynamic market conditions and economic deceleration, the Company successfully implemented its strategic objectives in 2012. In the operating and marketing areas, the LOTOS Group's implementation of the strategic objectives and achieving relevant ratios set for intermediate stages of the process progressed in line with the original assumptions in 2012. The LOTOS Group's share in the domestic market for fuels (diesel oil, gasoline, light fuel oil) expanded to 34%, thus exceeding the strategic target.

The key prerequisite for the success of the Group's sustainable development strategy is to intensify the exploration and production activities. Achieving this objective by the end of 2015 will enable creation of a strong and stable oil conglomerate, with production activities contributing a significant portion of profits. In 2012, crude output was 262.2 thousand tonnes, including 74.5 thousand tonnes produced in Lithuania.

Material increase in non-cash assets and property, plant and equipment in the period under analysis or projected for further years with sources of financing thereof (expenditure completed, in progress and commenced) and their structure by application according to the Company's strategy

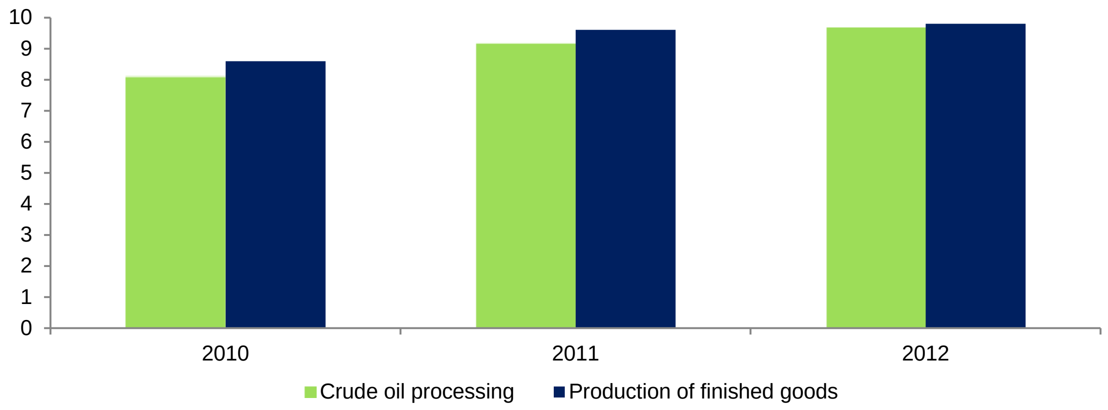
The LOTOS Group's investment plans were presented in the published document entitled "The LOTOS Group's strategy for 2011–2015 and development directions until 2020". In this scope, the LOTOS Group's total capital expenditure in 2011–2015 will not exceed PLN 5.7bn, with 68% of that figure representing capital expenditure in the upstream segment and 32% on the development of the downstream segment. The structure of sources of financing the investment projects will account for LOTOS Group's target value of the debt to equity ratio.

Refinery

Grupa LOTOS S.A.'s refinery is one of the newest and most advanced production plants in Europe. Its excellent condition is chiefly attributable to the 10+ Programme, which was completed in 2011. Even though the refinery has been in operation for nearly 40 years, the average in-service life of installed units is approx. 11 years. Grupa LOTOS S.A. has implemented an Integrated Management System compliant with the norms for quality (ISO 9001), environmental protection (ISO 14001) and occupational health and safety (ISO 18001).

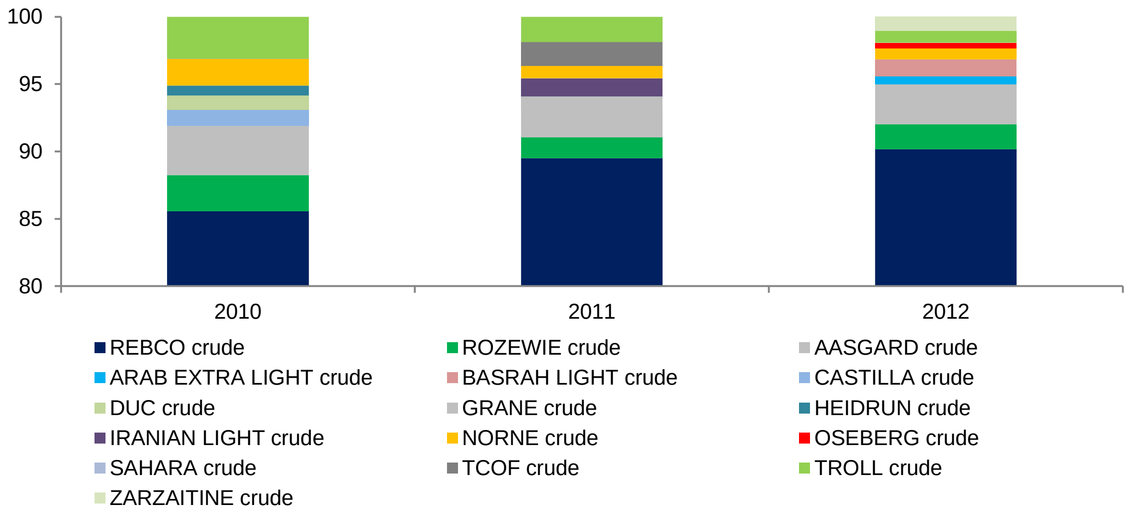
2012 was another record year for Grupa LOTOS' refinery. The volume of crude oil processed was 9.67m tonnes, the highest in the history of the Gdańsk refinery, which means **that the average annual utilisation rate of the refinery's installed capacities slightly exceeded 92%.** The utilisation of the refinery's installed capacities was adjusted during the year to reflect the prevailing market conditions. Throughput was increased in periods with high refining margins, for example in September and October 2012, when the utilisation rate exceeded 100%.

Crude oil processing and production of finished products at the Grupa LOTOS refinery (million tonnes)

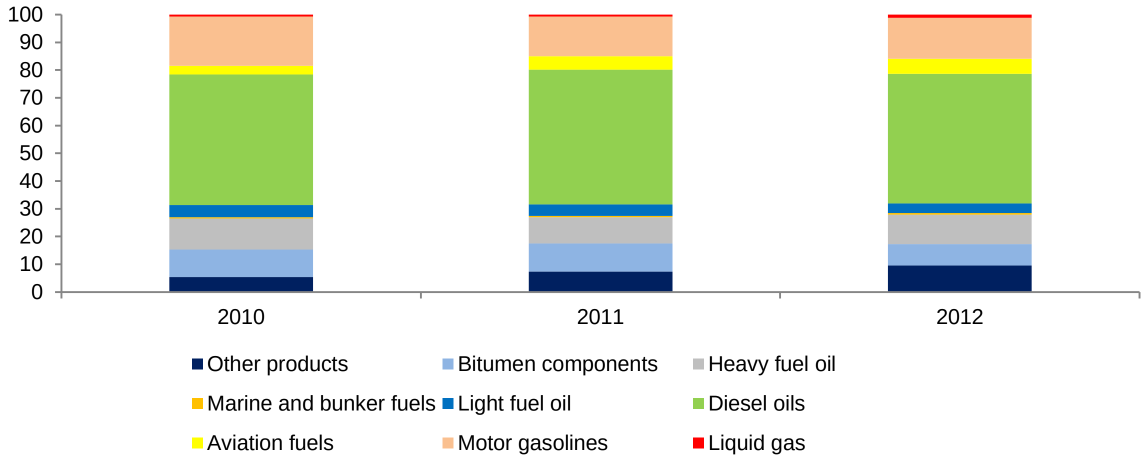


As in previous years, **the main type of crude processed** was the Russian **REBCO** crude, whose share in the total volume of crudes was approx. 90.2% and remained relatively flat on 2011. Crude oil imported by sea, including approx. 180 thousand tonnes of Rozewie crude supplied by LOTOS Petrobaltic, accounted for the balance of the crude used. The selection of crudes for processing was based on output optimisation, aimed at using emerging opportunities to increase the refinery's processing margin.

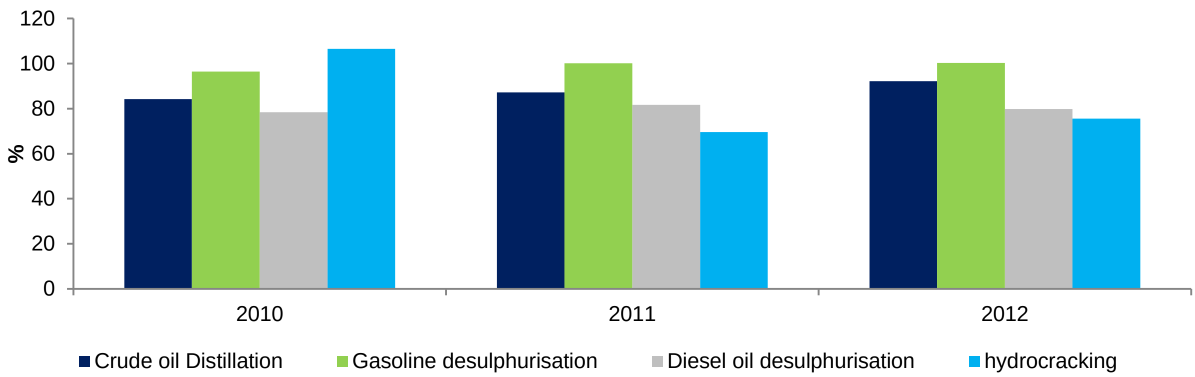
Throughput by types of crudes (%)



Finished products by weight (%)



Utilisation of the refinery's processing capacities (%)



Apart from crude oil, other production inputs included fuel components and feedstock purchased for further processing, as well as enhancing additives. The last category comprises biofuels (i.e. ethanol, ETBE and FAME), which are added to fuels to achieve the National Indicative Target.

On February 7th 2012, quality requirements for liquid fuels were changed by virtue of the Minister of Economy's regulation, whereby the permitted content of fatty acid methyl esters (FAME) in diesel oil was increased from 5% to 7%. As a result, on February 14th 2012, the first batch of **diesel oil with a 7% FAME content (B7) was produced at the refinery.** . The change made it possible to attain the National Indicative Target in 2012 with minimum sales of 100 per cent biodiesel (B100).

A significant event in Grupa LOTOS S.A.'s refining operations was **commissioning of the high pressure gas pipeline** constructed in partnership with PGNiG and PSG. The launch of the pipeline, along with the pressure reduction stations, enabled the refinery to considerably increase natural gas consumption. Natural gas is used at Grupa LOTOS S.A.'s refinery as fuel in process furnaces, the Company's CHP plant boilers, and as feedstock for hydrogen production. In the production of hydrogen, it replaced the previously used fuel oil and liquid gas. As a result, the carbon footprint of refining operations was reduced.

In terms of product portfolio diversification, a major event was launch of the **xylene separation unit** at Grupa LOTOS' refinery at the end of May 2012. The unit relies on reformate as feedstock, i.e. high-octane number component used in the manufacture of gasolines. From the reformate, the xylene fraction is recovered –

hydrocarbons used in the petrochemical industry. This helps reduce the number of motor gasoline components, which tend to be less in demand in Poland and in Europe, while obtaining a valuable non-fuel raw material. In 2012, the xylene separation unit produced some 28 thousand tonnes of the xylene fraction.

Aviation fuel

Since the beginning of 2013, aviation fuel is sold directly at the Frederick Chopin Airport in Warsaw. Currently, the Company's key clients at the Warsaw airport include Air France, KLM and TNT aircraft. Objectives for 2013–2015 include the intensification of sales and extension of sale of aviation fuel at other airports in Poland.

LPG (Liquefied Petroleum Gas)

Sales of LPG increased in 2012. The increase is attributable to the increased demand for cheaper substitute fuel, that is LPG, in response to growing prices of other engine fuels. Another driver of the increase was the introduction of high-pressure natural gas from the new pipeline to the refinery's network.

Plans and prospects for the segment

A significant event in Grupa LOTOS S.A.'s refining operations was **commissioning of the high pressure gas pipeline** constructed in partnership with PGNiG and Pomorska Spółka Gazownictwa (PSG). The launch of the pipeline, along with the pressure reduction stations, enabled the refinery to considerably increase natural gas consumption. Natural gas is used at Grupa LOTOS S.A.'s refinery as fuel in process furnaces and the Company's CHP plant boilers, and it has replaced fuel oil and liquid gas as feedstock in hydrogen production. As a result, the carbon footprint of refining operations was reduced.

The major shift towards natural gas as fuel in refining processes was a springboard for other projects aimed to enhance efficiency of oil refining processes and improve the refinery's energy efficiency. The possibility of using natural gas as a fuel is exploited in the construction of the **Hydrogen Recovery Unit**. The unit will act to recover hydrogen, liquid gas and gasoline distillates from refinery gases, which have been so far fed into the fuel gas network and which will be replaced with natural gas as a cheaper fuel source. The project will be implemented in 2013–2015.

In 2013, the Group will continue **design work related to construction of the sea cargo handling terminal in Martwa Wisła**, in the immediate vicinity of the Gdańsk refinery. The aim of the project is to enable handling of component and product loads with a unit volume of up to five thousand tonnes for exports and imports on Grupa LOTOS S.A.'s own wharf.

The plan of actions designed to implement the strategic objective of increasing the conversion ratio and intensifying crude processing, provided that in 2012 the front-end engineering design phase starts for the complex of refining units which would process the heavy residue from crude oil processing into high-value products. Towards the end of 2011, a growth option was selected consisting in the **construction of a coking unit**. In 2012, a licence for the coking process was selected and purchased, and the front-end engineering design of the unit was developed. Technologies for accompanying processes were also purchased and a number of necessary analyses and method statement were prepared. The process of selecting utilities suppliers and product customers began. In 2013, an integrating conceptual design of the entire project will be developed, terms and conditions of utilities supplies and product acceptance will be agreed upon, and steps will be taken to secure appropriate financing for of the project. The construction of the coking unit will be completed in 2015.

2.10. MATERIAL AGREEMENTS AND COURT PROCEEDINGS IN 2012

2.10.1. AGREEMENTS SIGNIFICANT FOR THE OPERATIONS IN 2012

No.	Counterparty	Date	Subject matter of the agreement/largest agreement	Estimated net value of all agreements (PLN)	More information	Link
1	BP Group	Jan 4 2012	Sale of liquid fuels	1,841m[2]	Current Report No. 1/2012	http://inwestor.lotos.pl/1185/p,194,i,653/raporty_i_dane/raporty_biezace/umowy_zawarte_pomiedzy_grupa_lotos_sa_a_podmiotami_grupy_kapitalowej_bp
2	TNK Trade Ltd.	Jan 25 2012	Purchase of crude oil	705m[2]	Current Report No. 3/2012	http://inwestor.lotos.pl/1185/p,194,i,656/raporty_i_dane/raporty_biezace/umowy_zawarte_pomiedzy_grupa_lotos_sa_a_tnk_trade_ltd
3	Petraco Oil Company Ltd.	Feb 29 2012	Purchase of crude oil	626m[1]	Current Report No. 9/2012	http://inwestor.lotos.pl/1185/p,194,i,662/raporty_i_dane/raporty_biezace/umowy_zawarte_pomiedzy_grupa_lotos_sa_a_petraco_oil_company_ltd
4	Eminent Energy Ltd.	Apr 2 2012	Purchase of crude oil	841m[1]	Current Report No. 12/2012	http://inwestor.lotos.pl/1185/p,194,i,665/raporty_i_dane/raporty_biezace/zawarcie_umowy_na_dostawy_ropy_naftowej_pomiedzy_grupa_lotos_sa_a_eminent_energy_ltd
5	Mercuria Energy Trading S.A.	Apr 3 2012	Purchase of crude oil (two contracts concluded at the same time)	808m	Current Report No. 13/2012	http://inwestor.lotos.pl/1185/p,194,i,666/raporty_i_dane/raporty_biezace/zawarcie_umowy_na_dostawy_ropy_naftowej_pomiedzy_grupa_lotos_sa_a_mercuria_energy_trading_sa
6	Statoil Group	Apr 19 2012	Purchase of crude oil	935m[1]	Current Report No. 14/2012	http://inwestor.lotos.pl/1185/p,194,i,667/raporty_i_dane/raporty_biezace/zawarcie_umow_pomiedzy_grupa_lotos_sa_a_grupa_kapitalowa_statoil
7	Mercuria Energy Trading S.A.	Apr 30 2012	Purchase of crude oil	1,060m[1]	Current Report No. 15/2012	http://inwestor.lotos.pl/1185/p,194,i,668/raporty_i_dane/raporty_biezace/zawarcie_umowy_na_dostawy_ropy_naftowej_pomiedzy_grupa_lotos_sa_a_mercuria_energy_trading_sa
8	Chevron Group	May 9 2012	Sale of heavy fuel oil	683m[2]	Current Report No. 16/2012	http://inwestor.lotos.pl/1185/p,194,i,669/raporty_i_dane/raporty_biezace/zawarcie_umow_o_wartosci_umowy_znaczacej_pomiedzy_grupa_lotos_sa_a_grupa_kapitalowa_chevron
9	LOTOS Kolej Sp. z.o.o.	May 16 2012	Annex to the agreement for provision of transport services	2,751m	Current Report No. 18/2012	http://inwestor.lotos.pl/1185/p,194,i,671/raporty_i_dane/raporty_biezace/aneks_do_umowy_znaczacej_pomiedzy_grupa_lotos_sa_a_lotos_kolej_sp_z_oo
10	Petraco Oil Company Ltd.	Jul 4 2012	Purchase of crude oil	1,500m[1]	Current Report No. 25/2012	http://inwestor.lotos.pl/1185/p,194,i,678/raporty_i_dane/raporty_biezace/zawarcie_umow_o_wartosci_znaczacej_pomiedzy_grupa_lotos_sa_a_petraco_oil_company_ltd
11	Mercuria Energy Trading S.A.	Jul 4 2012	Purchase of crude oil	702m[1]	Current Report No. 26/2012	http://inwestor.lotos.pl/1185/p,194,i,679/raporty_i_dane/raporty_biezace/zawarcie_umow_o_wartosci_znaczacej_pomiedzy_grupa_lotos_sa_a_mercuria_energy_trading_sa

No.	Counterparty	Date	Subject matter of the agreement/largest agreement	Estimated net value of all agreements (PLN)	More information	Link
12	The Shell Group	Aug 22 2012	Purchase of crude oil	643m[1]	Current Report No. 27/2012	http://inwestor.lotos.pl/1185/p,194,i,680/raporty_i_dane/raporty_biezace/zawarcie_umow_o_wartosci_znaczacej_pomiedzy_grupa_lotos_sa_a_grupa_kapitalowa_shell
13	Statoil Group	Aug 23 2012	Purchase of crude oil	651m[1]	Current Report No. 28/2012	http://inwestor.lotos.pl/1185/p,194,i,681/raporty_i_dane/raporty_biezace/zawarcie_umow_o_wartosci_znaczacej_pomiedzy_grupa_lotos_sa_a_grupa_kapitalowa_statoil
14	Mercuria Energy Trading S.A.	Sep 12 2012	Purchase of crude oil	1,249m[1]	Current Report No. 29/2012	http://inwestor.lotos.pl/1185/p,194,i,682/raporty_i_dane/raporty_biezace/zawarcie_umow_o_wartosci_znaczacej_pomiedzy_grupa_lotos_sa_a_mercuria_energy_trading_sa
15	PKN Orlen	Sep 12 2012	Sale of liquid gas	651m[2]	Current Report No. 30/2012	http://inwestor.lotos.pl/1185/p,194,i,683/raporty_i_dane/raporty_biezace/zawarcie_umow_o_wartosci_znaczacej_pomiedzy_grupa_lotos_sa_a_grupa_kapitalowa_pkn_orlen
16	BP Group	Oct 1 2012	Sale of diesel oil	626m[1]	Current Report No. 31/2012	http://inwestor.lotos.pl/1185/p,194,i,684/raporty_i_dane/raporty_biezace/zawarcie_umow_o_wartosci_znaczacej_pomiedzy_grupa_lotos_sa_a_grupa_kapitalowa_bp
17	Mercuria Energy Trading S.A.	Oct 19 2012	Purchase of crude oil	811m[1]	Current Report No. 33/2012	http://inwestor.lotos.pl/1185/p,194,i,686/raporty_i_dane/raporty_biezace/zawarcie_umow_o_wartosci_znaczacej_pomiedzy_grupa_lotos_sa_a_mercuria_energy_trading_sa
18	Petraco Oil Company Ltd.	Oct 26 2012	Purchase of crude oil	820m[1]	Current Report No. 34/2012	http://inwestor.lotos.pl/1185/p,194,i,687/raporty_i_dane/raporty_biezace/zawarcie_umow_o_wartosci_umowy_znaczacej_pomiedzy_grupa_lotos_sa_a_petraco_oil_company_ltd
19	The Shell Group	Nov 27 2012	Purchase of crude oil	913m[1]	Current Report No. 38/2012	http://inwestor.lotos.pl/1185/p,194,i,692/raporty_i_dane/raporty_biezace/zawarcie_umow_o_wartosci_umowy_znaczacej_pomiedzy_grupa_lotos_sa_a_spolkami_grupy_kapitalowej_shell
20	LOTOS Tank Sp. z.o.o.	Dec 21 2012	Sale of aviation fuel	2,500m	Current Report No. 42/2012	http://inwestor.lotos.pl/1185/p,194,i,696/raporty_i_dane/raporty_biezace/zawarcie_umowy_na_sprzedaz_paliwa_lotniczego_pomiedzy_grupa_lotos_sa_a_lotos_tank_sp_z_oo
21	Statoil Group	Dec 21 2012	Purchase of crude oil	746m[1]	Current Report No. 43/2012	http://inwestor.lotos.pl/1185/p,194,i,697/raporty_i_dane/raporty_biezace/zawarcie_umow_o_wartosci_umowy_znaczacej_pomiedzy_grupa_lotos_sa_a_spolkami_grupy_kapitalowej_statoil
22	Petraco Oil Company Ltd.	Dec 21 2012	Purchase of crude oil	17.7bn	Current Report No. 44/2012	http://inwestor.lotos.pl/1185/p,194,i,698/raporty_i_dane/raporty_biezace/zawarcie_umowy_na_dostawy_ropy_naftowej_pomiedzy_grupa_lotos_sa_a_petraco_oil_company_ltd
23	Mercuria Energy Trading S.A.	Dec 24 2012	Purchase of crude oil (two contracts concluded at the same time)	1,300m	Current Report No. 45/2012	http://inwestor.lotos.pl/1185/p,194,i,699/raporty_i_dane/raporty_biezace/zawarcie_umow_o_wartosci_znaczacej_pomiedzy_grupa_lotos_sa_a_mercuria_energy_trading_sa
24	The Shell Group	Dec 31 2012	Sale of liquid fuels	4.7bn[1]	Current Report No. 46/2012	http://inwestor.lotos.pl/1185/p,194,i,700/raporty_i_dane/raporty_biezace/zawarcie_umow_o_wartosci_znaczacej_pomiedzy_grupa_lotos_sa_a_s

No.	Counterparty	Date	Subject matter of the agreement/largest agreement	Estimated net value of all agreements (PLN)	More information	Link
						polkami_grupy_kapitalowej_shell
25	BP Group	Dec 31 2012	Sale of liquid fuels	1.18bn[1]	Current Report No. 47/2012	http://inwestor.lotos.pl/1185/p,194,i,702/raporty_i_dane/raporty_biezace/zawarcie_umow_o_wartosci_znaczacej_pomiedzy_grupa_lotos_sa_a_spolkami_grupy_kapitalowej_bp
26	Statoil Group	Dec 31 2012	Sale of liquid fuels	9.3bn[1]	Current Report No. 48/2012	http://inwestor.lotos.pl/1185/p,194,i,703/raporty_i_dane/raporty_biezace/zawarcie_umow_o_wartosci_znaczacej_pomiedzy_grupa_lotos_sa_a_spolkami_grupy_kapitalowej_statoil
			Agreements concluded after the balance-sheet date			
27	ADM Group	Jan 15 2013	Purchase of biocomponents	745m	Current Report No. 2/2013	http://inwestor.lotos.pl/1185/p,194,i,705/raporty_i_dane/raporty_biezace/zawarcie_umow_o_wartosci_znaczacej_pomiedzy_grupa_lotos_sa_a_spolkami_grupy_kapitalowej_adm
28	AB LOTOS Geonafta	Jan 18 2013	Purchase of crude oil	822m	Current Report No. 3/2013	http://inwestor.lotos.pl/1185/p,194,i,706/raporty_i_dane/raporty_biezace/zawarcie_umowy_na_dostawy_ropy_naftowej_pomiedzy_grupa_lotos_sa_a_spolka_ab_lotos_geonafta
29	Neste Group	Jan 22 2013	Sale of gasoline	813m[2]	Current Report No. 5/2013	http://inwestor.lotos.pl/1185/p,194,i,709/raporty_i_dane/raporty_biezace/zawarcie_umow_o_wartosci_znaczacej_pomiedzy_grupa_lotos_sa_a_spolkami_grupy_kapitalowej_neste

1) total value of agreements with the counterparty since the release of the previous current report (following the execution of the described agreement, the criterion of value of a significant agreement was met).

1) total value of agreements with the counterparty in 12 months preceding the agreement (following the execution of the described agreement, the criterion of value of a significant agreement was met).

Sales to petroleum companies

Given the falling number of international oil and gas companies operating organised service station networks in Poland, maintenance of a 30% share in the fuels market in the next few years may be achieved through such measures as establishing and extending cooperation with super and hypermarket chains, and seeking opportunities to maximise margins.

In 2013, the Company will supply fuels to the following petroleum companies: Statoil, Shell, BP and Lukoil. The achievement of sales targets is supported by a customer structure designed to maximise margins.

2.10.2. MATERIAL RELATED-PARTY TRANSACTIONS EXECUTED ON NON-ARMS' LENGTH TERMS

In the year ended December 31st 2012, no related-party transactions were concluded on non-arms' length terms.

2.10.3. AGREEMENT WITH QUALIFIED AUDITOR OF FINANCIAL STATEMENTS

Based on the resolution adopted by the Supervisory Board of Grupa LOTOS S.A. on December 17th 2009, Ernst &Young Audit Sp. z o.o., entered in the register of entities qualified to audit financial statements maintained by the National Board of Chartered Auditors under entry No. 130, was selected as the qualified auditor to audit the Company's financial statements for 2010, 2011 and 2012.

On May 18th 2010, Grupa LOTOS S.A. and Ernst & Young Audit Sp. z o.o. of Warsaw concluded an agreement providing amongst other things for:

- review of the separate and consolidated financial statements for the first six months of 2010, 2011 and 2012,
- audit of the separate and consolidated financial statements in 2010–2012.

Total remuneration for the audit, review and verification procedures (PLN '000)

	2012	**2011**
Audit of the annual separate and consolidated financial statements of Grupa LOTOS S.A.(1)	**351**	351
Confirmation services(1), including:	**284**	284
- review of the semi-annual separate and consolidated financial statements of Grupa LOTOS S.A.	**284**	284
Other services (2)	**-**	4
Tax advisory services	**-**	-
Total	**635**	**639**

(1) Fees for the audit, review and verification of the financial statements, as well as for other services provided by Ernst & Young Audit Sp. z o.o. under the agreement of May 18th 2010 regarding the review of the separate and consolidated financial statements for the first six months of 2010, 2011 and 2012 and for the audit of the separate and consolidated financial statements in 2010–2012.

(2) Fees paid for auditor training services.

2.10.4. COURT, ARBITRATION OR ADMINISTRATIVE PROCEEDINGS

In 2012 no court, arbitration or administrative proceedings were pending concerning the Issuer's or its subsidiary's liabilities or debts with a value (total value of proceedings) equal to or exceeding 10% of the Company's equity.

3. FINANCIAL STANDING OF GRUPA LOTOS S.A.

3.1. GRUPA LOTOS S.A. 2012 RESULTS

3.1.1. STATEMENT OF COMPREHENSIVE INCOME

In 2012, Grupa LOTOS S.A. posted PLN 31,071.9m in net revenue (up by 13.9% on 2011), driven mainly by rising prices of petroleum products on global markets, a higher average annual USD exchange rate (up 10.1% on 2011) and a 1.5% growth in sales volumes. The Company's average selling price was PLN 3,101/t in 2012 (up PLN 338/t or 12.2% on 2011).

Macroeconomic data

(USD/bbl)	2012	2011	2012-2011	2012/2011
DATED Brent FOB prices	**111.67**	111.26	0.41	*0.4%*
Urals CIF Rotterdam prices	**110.18**	109.07	1.11	*1.0%*
Brent/Urals differential *	**1.27**	1.68	-0.41	*-24.4%*
Model refining margin USD/bbl**	**5.53**	3.41	2.12	*62.0%*

** Brent vs. Urals spread.*

***Model margin for the output structure in the averaged scenario of typical annual operation of Grupa LOTOS's refinery, assuming maximized yields of middle distillates. An annual throughput has been assumed to correspond to the maximum distillation capacity if Urals crude was the only feedstock, whose value is determined as the difference between DTD Brent and the Urals Rtd vs. forward Dtd Brent spread.*

Petroleum products (USD/t)	2012	2011	2012-2011	2012/2011
Crack margin: gasoline	**190.97**	142.91	48.06	*33.6%*
Crack margin: naphtha	**88.36**	85.06	3.3	*3.9%*
Crack margin: Diesel oil (10 ppm)	**137.23**	118.88	18.35	*15.4%*
Crack margin: Light fuel oil	**108.06**	91.68	16.38	*17.9%*
Crack margin: Aviation fuel	**178.78**	169.8	8.98	*5.3%*
Crack margin: Heavy fuel oil	**-217.55**	-235.84	18.29	*7.8%*

Currency (USD/PLN)	2012	2011	2012-2011	2012/2011
USD/PLN exchange rate at end of period	**3.10**	3.42	-0.32	*-9.4%*
Average PLN/USD exchange rate	**3.26**	2.96	0.30	*10.1%*

The total volume of petroleum products, merchandise and materials sold by the Company in 2012 reached 10,018.7 thousand tonnes (i.e. 1.5% up on 2011). The share of domestic sales in the total sales volume fell by 6.4pp.

In 2012, cost of sales of Grupa LOTOS S.A. was PLN 29,691.2m (up by 14.7% relative to 2011). The average unit cost of sales stood at PLN 2,964 per tonne, which is PLN 341 per tonne, or 13.0%, more than in 2011. As the unit cost of sales increased more than the average selling price, Grupa LOTOS S.A.'s sales margin in 2012 was down by 2.5% relative to 2011. Grupa LOTOS S.A.'s gross profit in 2012 was PLN 1,380.7m, having decreased by PLN 15.4m relative to 2011.

Distribution costs increased by PLN 55.4m (up by 10.3% relative to 2011), driven chiefly by a rise in unit distribution cost caused by higher average annual USD/PLN exchange rate and an increased share of export sales in total sales volume.

In 2012, the Company's administrative expenses remained relatively flat year on year.

In 2012, the Company reported a profit on other operating activities of PLN 7.5m (2011: net loss of PLN -17.1m), which accounted for, among other things, gain on disposal of CO_2 emission allowances of PLN 14.5m. The negative balance in 2011 included impairment loss on tangible assets under construction of PLN 12.9m related to the IGCC project.

In 2012, Grupa LOTOS S.A. posted PLN 556.3m in **operating** profit (down by PLN 47.1m or 7.8% on 2011), which comprised profit of the downstream segment that was affected by:

- the weighted average method used by the Company to measure decrease in inventories reduced the operating result by PLN 47.4m (in 2011 it contributed PLN 978.4m),
- fluctuations of the USD exchange rate in 2012 resulted in net foreign exchange losses on operating activities of PLN 31.2m, connected mainly with feedstock purchases (in 2011 - net foreign exchange losses on operating activities of PLN 319.4m),
- higher crack margins on fuels and heavy fuel oil;
- lower crack margin on other refining products.

Statement of comprehensive income of Grupa LOTOS S.A. (PLNm)

	2012	2011	2012-2011	2012/2011
Revenue	**31,071.9**	27,289.3	3,782.6	*13.9%*
Cost of sales	**-29,691.2**	-25,893.2	-3,798.0	*14.7%*
Gross profit	**1,380.7**	1,396.1	-15.4	*-1.1%*
Distribution costs	**-595.7**	-540.3	-55.4	*10.3%*
Administrative expenses	**-236.2**	-235.3	-0.9	*0.4%*
Other income	**18.5**	4.8	13.7	*285.4%*
Other expenses	**-11.0**	-21.9	10.9	*-49.8%*
Operating profit	**556.3**	603.4	-47.1	*-7.8%*
Finance income	**523.2**	247.4	275.8	*111.5%*
Finance costs	**-162.8**	-526.4	363.6	*-69.1%*
Gain on disposal of investments	**52.1**	0.0	52.1	-
Pre-tax profit	**968.8**	324.4	644.4	*198.6%*
Corporate income tax	**-132.4**	-16.7	-115.7	*692.8%*
Net profit	**836.4**	307.7	528.7	*171.8%*

The Company posted a profit on financing activities of PLN 360.4m chiefly as a result of:

- dividends received in 2012 of PLN 287.5m,
- foreign exchange gains on remeasurement of bank borrowings and other debt instruments of PLN 127.8m,
- net gain on measurement and settlement of market risk hedging derivative instruments of PLN 93.1m,
- net loss on interest on debt, interest income and commission fees of PLN -147.0m.

Starting from January 1st 2011, Grupa LOTOS S.A. introduced cash flow hedge accounting with respect to foreign-currency denominated loans intended for the financing of the 10+ Programme, designated as hedges of future USD-denominated petroleum product sales transactions. As a consequence, in the period from January 1st to December 31st 2012, foreign exchange gains taken to the cash flow hedging reserve were PLN 472.2m.

In 2012, the net gain on measurement and settlement of market risk hedging transactions at Grupa LOTOS S.A. was PLN 93.1m and included:

net gain on settlement and measurement of derivative instruments (forwards) hedging the foreign exchange risk of PLN 137.2m.

The net loss on settlement and measurement of futures hedging the prices of carbon (CO_2) allowances amounted to PLN 7.5m, net loss on IRS transactions hedging interest rates was PLN 22.2m and net loss on settlement and measurement of transactions hedging the prices of petroleum products stood at PLN 14.4m in 2012.

The net loss on financing activities of PLN -279.0m posted in 2011 was chiefly attributable to foreign exchange losses (PLN -286.6m), negative measurement and settlement of financial instruments (PLN -109.7m), negative balance of offsetting interest on debt, interest income and commission fees (PLN -121.2m) and dividend received (PLN 240.5m).

The profit on the Company's financing activities recorded in 2012 and net proceeds from the sale of LOTOS Parafiny shares of PLN 52.1m resulted in a year-on-year increase in net profit in 2012 (up by 171.8%, to PLN 836.4m).

3.1.2. STATEMENT OF FINANCIAL POSITION

Assets (PLNm)

	Dec 31 2012	Dec 31 2011	Change	%
Total assets	**16,012.1**	16,449.5	-437.4	*-2.7%*
Total non-current assets	**8,143.6**	8,374.8	-231.2	*-2.8%*
Property, plant and equipment	**6,800.0**	7,079.0	-279.0	*-3.9%*
Intangible assets	**90.2**	83.4	6.8	*8.2%*
Shares	**910.5**	857.0	53.5	*6.2%*
Derivative financial instruments	**0.0**	12.1	-12.1	*-100.0%*
Other non-current assets	**342.9**	343.3	-0.4	*-0.1%*
Total current assets	**7,868.5**	8,048.8	-180.3	*-2.2%*
Inventories	**5,705.7**	5,637.3	68.4	*1.2%*
Trade receivables	**1,670.5**	2,177.3	-506.8	*-23.3%*
Current tax assets	**9.4**	73.5	-64.1	-
Derivative financial instruments	**121.4**	37.2	84.2	*226.3%*
Other current assets	**358.6**	119.9	238.7	*199.1%*
Cash and cash equivalents	**2.9**	3.6	-0.7	*-19.4%*
Assets held for sale	**0.0**	25.9	-25.9	-

As at December 31st 2012, the Company's total assets were PLN 16,012.1m.

The decline (down 437.4m) of total assets were mainly driven by:

- PLN 279.0m decline in property, plant and equipment, chiefly attributable to depreciation write-offs,
- a PLN 506.8m drop in trade receivables, largely on the back of a lower average net selling price and a decline in sales volume in December 2012 relative to December 2011,
- a PLN 238.7m increase in other current assets, mainly as a result of higher level of deposits at (earmarked for financing of the maintenance shutdown scheduled for 2013), loans advanced to LOTOS Petrobaltic S.A. and receivables from the state budget other than income tax.

Financial position – equity and liabilities (PLNm)

	Dec 31 2012	Dec 31 2011	Change	%
Equity and liabilities	**16,012.1**	16,449.5	-437.4	*-2.7%*
Total equity	**7,052.3**	5,833.4	1,218.9	*20.9%*
Share capital	**129.9**	129.9	0.0	*0.0%*
Share premium	**1,311.3**	1,311.3	0.0	*0.0%*
Cash flow hedging reserve	**-36.8**	-419.3	382.5	-
Retained earnings	**5,647.9**	4,811.5	836.4	*17.4%*
Total non-current liabilities	**4,449.3**	4,978.5	-529.2	*-10.6%*
Bank borrowings	**4,069.6**	4,786.9	-717.3	*-15.0%*
Derivative financial instruments	**88.3**	127.4	-39.1	*-30.7%*
Deferred tax liability	**246.1**	23.2	222.9	*960.8%*
Employee benefit obligations	**45.3**	41.0	4.3	*10.5%*
Total current liabilities	**4,510.5**	5,637.6	-1,127.1	*-20.0%*
Bank borrowings	**1,462.6**	1,682.1	-219.5	*-13.0%*
Derivative financial instruments	**102.5**	129.4	-26.9	*-20.8%*
Trade and other payables	**2,161.9**	2,802.0	-640.1	*-22.8%*
Employee benefit obligations	**35.9**	31.2	4.7	*15.1%*
Other liabilities and provisions	**747.6**	992.9	-245.3	*-24.7%*

Grupa LOTOS S.A.'s equity was PLN 7,052.3m as at the end of 2012 (up PLN 1,218.9m on 2011), largely on the back of the PLN 836.4m net profit earned in 2012 and the PLN 382.5m foreign exchange gains on measurement of cash flow hedges net of the tax effect taken to the cash flow hedging reserve.

The share of equity in total equity and liabilities was up from 35.5% in 2011 to 44.0% in 2012.

The Company carried lower liabilities (down by PLN 1,656.3m) chiefly as a result of the following:

- lower liabilities under borrowings (down by PLN 936.8m), mainly owed to repayments and their measurements at lower exchange rates,
- lower trade liabilities (down by PLN 640.1m), owed to, among other factors, lower value of crude oil purchased in December 2012 compared with December 2011, as well as different delivery and payment dates,
- a PLN 245.3m decline in other current provisions and liabilities attributable to a decrease in liabilities to the state budget other than income tax.

As at December 31st 2012, the Company's financial debt was PLN 5,532.2m (down PLN 936.8m relative to December 31st 2011). The ratio of financial debt (adjusted for free cash) to equity was 78.4% (32.4pp less than as at December 31st 2011).

In the reporting period, the Company carried no material consolidated off-balance-sheet items other than described in Note 33 to the financial statements of Grupa LOTOS S.A. for 2012.

3.1.3. STATEMENT OF CASH FLOWS

Cash flows (PLNm)

	2012	2011	Change
Cash flows from operating activities	**468.3**	138.9	329.4
Cash flows from investing activities	**68.3**	-31.4	99.7
Cash flows from financing activities	**-747.9**	-112.2	-635.7
Change in net cash	**-240.4**	21.1	-261.5
Cash and cash equivalents at beginning of the period	**-166.0**	-187.1	21.1
Cash and cash equivalents at end of the period	**-406.4**	-166.0	-240.4

As at December 31st 2012, the Company's cash balance (including current account overdrafts) was PLN -406.4m. In the twelve months of 2012, net cash flows were negative at PLN -240.4m (down PLN 261.5m on 2011).

Net cash from the Company's operating activities was PLN 468.3m (PLN 329.4m more than in 2011, primarily as a result of lower working capital requirements due to a year-on-year decrease in prices of crude oil and petroleum products as at the end of 2012).

In 2012, net cash from investing activities was PLN 68.3m and was mainly related to dividends received, proceeds from sale of shares in related entities and expenditure related to loans advanced to related parties, purchase of property, plant and equipment and bank deposits for financing of maintenance shutdown in 2013.

Cash flows from financing activities of PLN -747.9m followed chiefly from the negative balance of proceeds from borrowings and outflows on principal and interest payments.

3.1.4. ASSESSMENT OF FACTORS AND NON-RECURRING EVENTS AFFECTING THE OPERATING PERFORMANCE

The only non-recurring item which had an effect on the results reported by Grupa LOTOS S.A. for 2012 was a PLN 21.0m net gain from sale of shares in LOTOS Parafiny.

3.1.5. EXPLANATION OF DIFFERENCES BETWEEN ACTUAL FINANCIAL PERFORMANCE AND PREVIOUSLY PUBLISHED FORECASTS

Grupa LOTOS S.A. did not publish any separate performance forecasts for 2012.

3.2. CAPITAL EXPENDITURE

3.2.1. EXPENDITURE ON PROPERTY, PLANT AND EQUIPMENT

Total expenditure on property, plant and equipment incurred by the Company in 2012 was PLN 141.9m, up 23.7% on 2011. Most of the expenditure was spent on the upgrade and development of the units at the Gdańsk refinery, and in particular construction of new furnaces – 200F1 and 200 F2, extension of the natural gas supply unit, upgrade of the furfural extraction unit and of the xylene separation unit.

The table presents capital expenditure incurred by Grupa LOTOS S.A. in 2012 (PLN '000).

	Capital expenditure Jan 1 - Dec 31 2012
Construction and assembly work	79,167
Procurement from external suppliers – purchases	45,775
Purchase of intangible assets	15,556
Other capital expenditure	1,415
Total	**141,913**

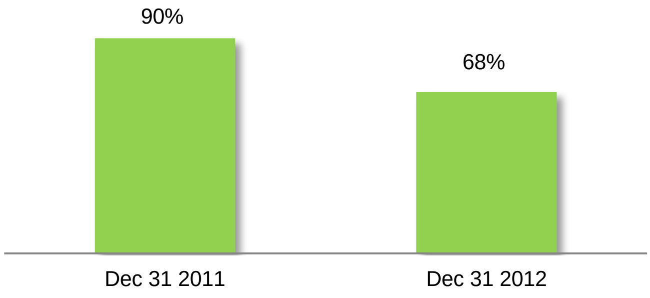
3.2.2. EQUITY INVESTMENTS

In 2012, Grupa LOTOS S.A. did not make any equity investments outside of the group of related entities, described in detail in Section 1.1.2. For ownership changes at the LOTOS Group, see page 9.

3.2.3. ASSESSMENT OF FEASIBILITY OF PLANNED INVESTMENTS, INCLUDING EQUITY INVESTMENTS IN THE CONTEXT OF AVAILABLE FUNDING

In 2012, the LOTOS Group companies managed their liquidity position in an effective manner. The high level of Grupa LOTOS S.A.'s debt is serviced on a regular basis. In 2012, the Company repaid a portion of its debt related to the 10+ Programme projects. The net debt to equity ratio declined in 2012 by 22pp (from 90% to 68%).

Gearing ratio – the ratio of net debt (financial debt adjusted by free cash) to equity



The improvement of the debt ratio confirms the Company's ability to manage its liquidity position and the current debt level, and proves the financing strategy to be a correct one.

As at the date of release of this Directors' Report, i.e. as at March 21st 2013, the Company did not expect any changes in its financing structure.

3.3. FINANCING SOURCES

3.3.1. CREDIT FACILITY AGREEMENTS AND LOANS ADVANCED IN 2012

For more information on Grupa LOTOS S.A.'s bank borrowings as at December 31st 2012 and December 31st 2011, see Note 23 to the separate financial statements of Grupa LOTOS S.A. for 2011; for description of loans advanced by the Company, see Note 33 to the financial statements.

➢ **Credit facility agreement for the refinancing and financing of inventories of Grupa LOTOS S.A.**

On October 10th 2012, Grupa LOTOS S.A. and a syndicate of five banks, comprising:

- BANK POLSKA KASA OPIEKI S.A. of Warsaw, Poland,
- BRE BANK S.A. of Warsaw, Poland,
- ING BANK ŚLĄSKI S.A. of Katowice, Poland,
- NORDEA BANK AB (publ) of Stockholm, Sweden,
- SOCIETE GENERALE S.A. of Paris, France,

executed a credit facility agreement to refinance the existing inventory financing facility granted to Grupa LOTOS S.A. under a credit facility agreement of December 20th 2007, as amended, by a bank syndicate comprising: BANK POLSKA KASA OPIEKI S.A. of Warsaw, POWSZECHNA KASA OSZCZĘDNOŚCI BANK POLSKI S.A. of Warsaw, BRE BANK S.A. of Warsaw and NORDEA BANK POLSKA S.A. of Gdynia.

The agreement provides for a revolving credit facility of up to USD 400m (PLN 1,268m, translated at the USD/PLN mid-exchange rate quoted by the National Bank of Poland for October 10th 2012), intended to finance/refinance Grupa LOTOS S.A.'s inventories. The lending period is 12 months, starting from December 20th 2012, with an option to extend it for subsequent 12-month periods. The credit facility is secured primarily by an agreement on registered pledge over the Company's inventories (along with related assignment of rights under inventory storage agreements and insurance policies), and an agreement on pledge over cash receivables under an agreement for the keeping of bank accounts of Grupa LOTOS S.A. concluded in connection with the credit facility agreement (along with a power of attorney over the accounts).

The other terms and conditions of the credit facility agreement, including provisions concerning penalties, do not differ from those commonly used in agreements of such type.

The agreement is subject to a condition precedent, i.e. it will enter into force once the Company's Supervisory Board adopts a resolution approving the agreement.

On October 30th 2012, Grupa LOTOS S.A. submitted to BANK POLSKA KASA OPIEKI S.A., acting as credit facility agent, a resolution of the Grupa LOTOS Supervisory Board concerning approval of the credit facility agreement of October 10th 2012, concluded between the Company and a syndicate of five banks, comprising

Loans advanced to subsidiaries in the year ended December 31st 2012

Related entity	Loan agreement date	Principal, as specified in agreement		Maturity date	Security	Financial terms and conditions (interest rate)
		PLN	Currency			
LOTOS Exploration and Production Norge AS	Feb 22 2012	31,635 (1)	USD 10,000	Jan 31 2013 (2)	blank promissory note with a "protest waived" clause and promissory note declaration	The loan bore interest at a floating rate based on 3M LIBOR plus margin.
LOTOS Exploration and Production Norge AS	Mar 16 2012	31,688 (1)	USD 10,000	Jan 31 2013 (2)	blank promissory note with a "protest waived" clause and promissory note declaration	The loan bore interest at a floating rate based on 3M LIBOR plus margin.
LOTOS Petrobaltic S.A.	Aug 29 2012	33,081 (1)	USD 10,000	Jul 31 2013	blank promissory note with a "protest waived" clause and promissory note declaration	The loan bears interest at a floating annual interest rate based on 6M LIBOR USD plus margin.
LOTOS Petrobaltic S.A.	Sep 27 2012	30,624 (1)	USD 9,500	Jul 31 2013	blank promissory note with a "protest waived" clause and promissory note declaration	The loan bears interest at a floating annual interest rate based on 6M LIBOR USD plus margin.
LOTOS Petrobaltic S.A.	Dec 24 2012	92,000	-	Dec 31 2015	blank promissory note with a "protest waived" clause and promissory note declaration	The loan bears interest at a floating annual interest rate based on 6M WIBOR plus margin.

(1) *Translated at the USD/PLN mid-exchange rate quoted by the National Bank of Poland for the loan agreement date.*
(2) *Loan was repaid in full on December 28th 2012.*

In addition, on January 31st 2012, LOTOS Gaz S.A. w likwidacji (in liquidation) repaid another portion (PLN 650 thousand) of the PLN 2,000 thousand loan contracted on June 29th 2010. By December 31st 2012, the company repaid PLN 1,750 thousand under the loan. Under another annex signed on November 30th 2012, the repayment date for the outstanding loan amount was extended until October 31st 2013.

In the year ended December 31st 2012, annexes were signed whereby the final dates for repayment of the loans granted to LOTOS Gaz S.A. w likwidacji (in liquidation) under the following loan agreements were postponed as follows:

- loan agreement of March 8th 2011 (for PLN 247 thousand), loan agreement of March 29th 2011 (for PLN 352 thousand), and loan agreement of August 5th 2011 (for PLN 160 thousand) - the repayment date was extended until May 31st 2013,
- loan agreement of May 26th 2011 (for PLN 123 thousand) - the repayment date was extended until October 31st 2013,
- loan agreement of October 31st 2011 (for PLN 90 thousand) - the repayment date was extended until August 31st 2013.

The loans bear interest at a fixed annual interest rate based on 3M WIBOR plus margin.

3.3.2. SURETIES, GUARANTEES AND OTHER COLLATERAL

As at December 31st 2012, Grupa LOTOS S.A. had a PLN 240,000 thousand blank promissory note deposited at the Customs Office in Gdańsk as lump-sum security for excise duty for the amount of PLN 800,000 thousand. The security is valid until August 19th 2013.

3.3.3. ASSESSMENT OF FINANCIAL RESOURCES MANAGEMENT

In 2012, Grupa LOTOS S.A. was able to meet all of its liabilities towards third parties. In the period from January 1st to December 31st 2012, the Company used investment and working capital overdraft facilities. As at December 31st 2012, the Company had available funds of PLN 237.7m under working capital facilities. As at December 31st 2012, the balance of overdraft facilities was PLN 409.2m.

For more information on the structure of debt under bank borrowings, see Note 25 to the financial statements of Grupa LOTOS S.A. for the year ended December 31st 2012.

In connection with the credit facilities relating to the execution of the 10+ Programme and the facility for the refinancing of inventories, Grupa LOTOS S.A. is required to maintain the Tangible Consolidated Net Worth ratio at least at the level specified in facility agreements.

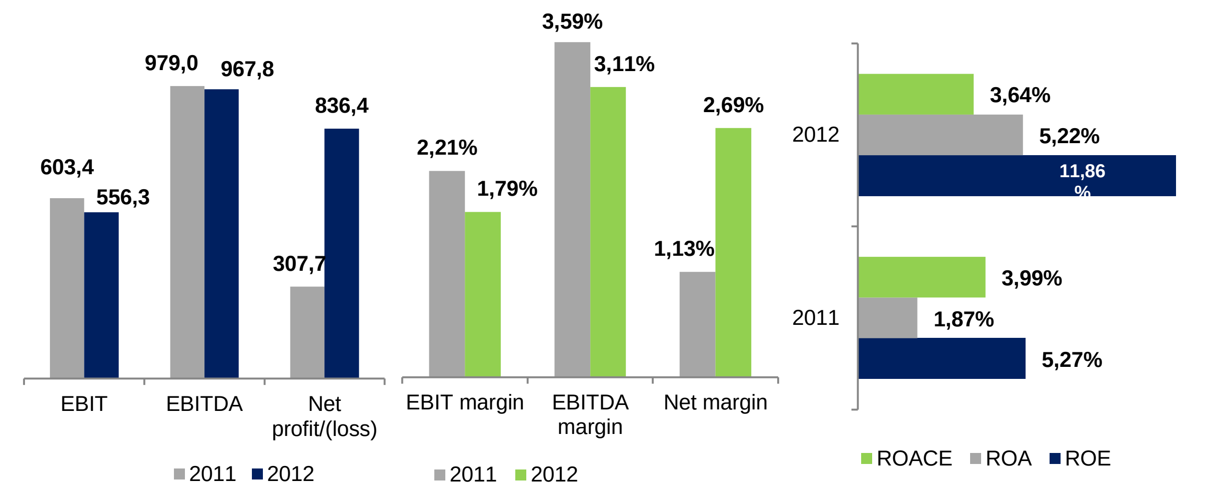
In addition, in connection with the refinancing facility, the Company is also required to meet a financial covenant of maintaining the Loan to Pledged Inventory Value Ratio at a level not higher than specified in the facility agreement.

As at December 31st 2012 and December 31st 2011, the covenants were complied with.

A brief assessment of Grupa LOTOS S.A.'s overall economic and financial standing has been prepared in the form of a ratio analysis covering margins, liquidity, turnover and debt levels.

Profitability ratios

(PLNm or %)

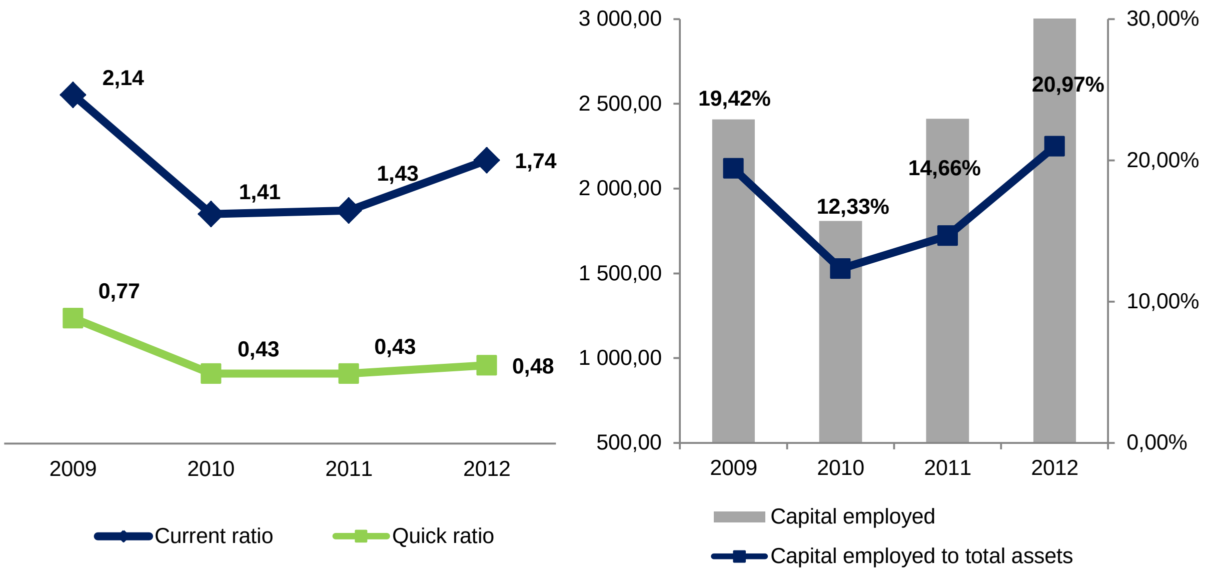


- fall of the EBIT and EBITDA margin due to lower operating result (down by 7.8%) with a concurrent increase in revenue (up by 13.9%);
- significantly higher net profit (up by 171.8%) on a lower revenue increase (up by 13.9%), lower total assets (down by 2.7%) and higher equity (up by 20.9%), resulted in improvement of the net margin, as well as ROE and ROA ratios reflecting the rate of return on invested equity and the profitability of asset;
- lower EBIT (down by 7.8%) and higher equity (up by 20.9%) drove ROACE down by 0.4pp despite a 16.8% lower net financial debt.

Formulas of the profitability ratios	
EBIT margin	operating profit/(loss) to net sales
EBITDA	EBIT before amortisation/depreciation
EBITDA margin	EBITDA to net sales
Net margin	net profit/(loss) to net sales
Return on equity (ROE)	net profit/(loss) to equity at the end of period
Return on assets (ROA)	net profit/(loss) to assets at the end of period
Return on average capital employed (ROACE)	operating profit/(loss) after tax to equity plus long-term and short-term borrowings and other debt instruments and net of cash and other current financial assets (as at the end of the period)

Liquidity ratios

(PLNm, absolute value or %)

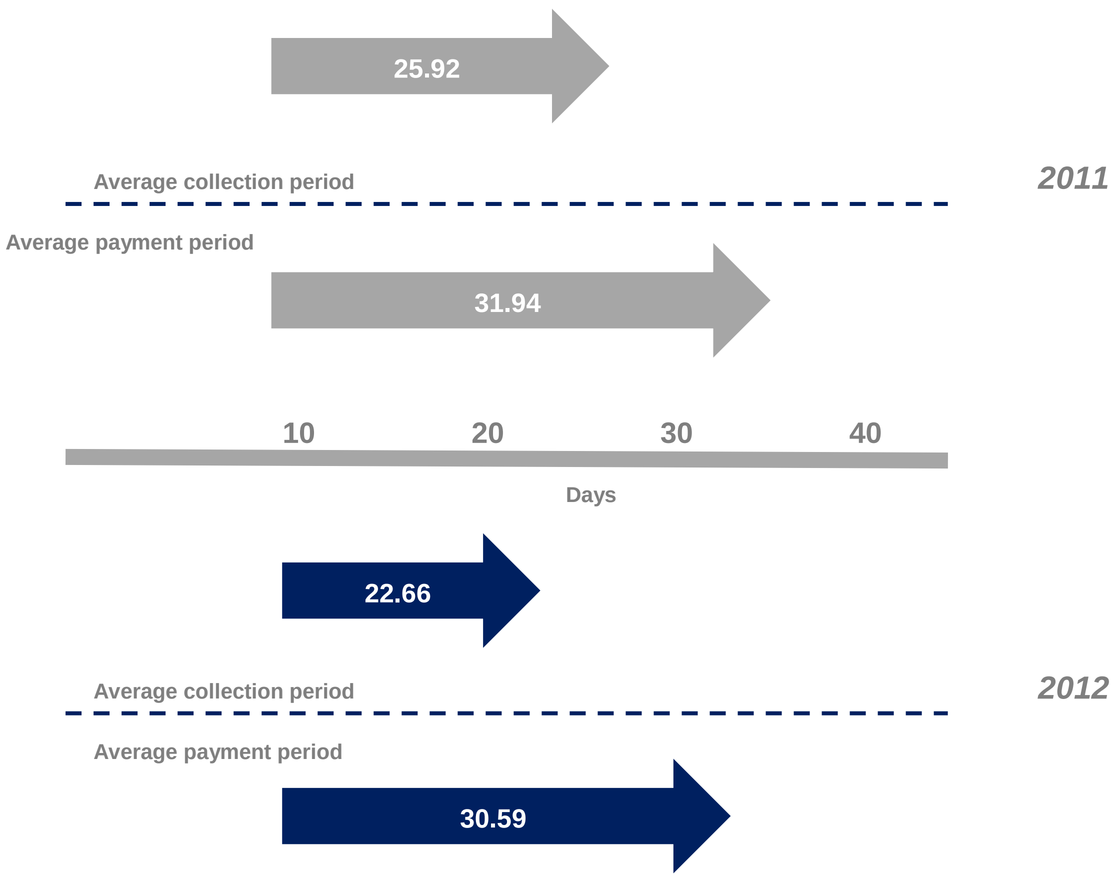


- Current ratio (1.74) and quick ratio (0.48) higher year on year (by 22.2% and 12.1%, respectively), owing to a decrease in current assets (down by 2.2%) lower than in current liabilities (down by 20.0%),
- a PLN 946.8m increase in capital employed, in connection with the fact that current liabilities decreased faster than current assets (down by PLN 1,127.1m and PLN 180.3m, respectively), and an increase of the share of capital employed in total assets.

Formulas of the liquidity ratios	
Current ratio	current assets to current liabilities (as at the end of the period)
Quick ratio	current assets net of inventories to current liabilities (as at the end of the period)
Capital employed	current assets net of current liabilities (as at the end of the period)
Capital employed to total assets	capital employed to total assets (as at the end of the period)

Collection/repayment periods

(days)

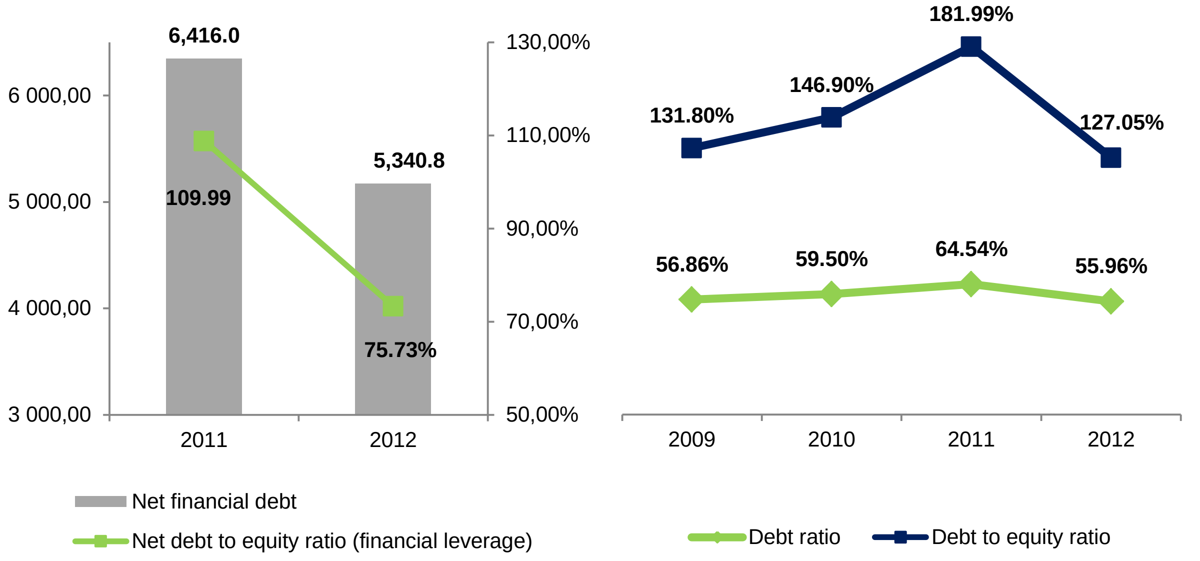


- shortening of the collection period and of the payment period at the Company level in 2012: the collection period shortened by three days as average trade receivables decreased (down by 0.7%) and revenue grew (up by 13.9%); the payment period shortened by one day as the average trade payables grew slower (up by 9.5%) than cost of sales (up by 14.7%).

Calculation of collection/repayment periods	
Average collection period (days)	average trade receivables to net sales times 365 (or 366) days of a given period
Average payment period (days)	average trade payables to cost of sales times 365 (or 366) days of a given period

Capital structure and debt ratios

(PLNm or %)



- decrease in the share of liabilities in financing assets by 8.6pp, as liabilities decreased faster (down by 15.6%) than assets (down by 2.7%),
- decrease in net debt to equity ratio (financial leverage) by 34.3pp, as net financial debt fell (by 16.8%) while equity grew (by 20.9%),
- decrease in debt to equity ratio by 54.9pp, as liabilities fell (by 15.6%) and equity increased (by 20.9%).

Formulas for the capital structure and debt ratios	
Debt ratio	total liabilities to total assets (as at the end of the period)
Net financial debt	long-term and short-term borrowings and other debt instruments net of cash and other current financial assets (as at the end of the period)
Net debt to equity ratio (financial leverage)	long-term and short-term borrowings and other debt instruments net of cash and other current financial assets to equity (as at the end of the period)
Debt to equity ratio	total liabilities to equity (as at the end of the period)

Given the deceleration of the global economy, to ensure the Group’s stable development, the Management Board of Grupa LOTOS S.A. implemented the Optimal Expansion Programme in the period from January 1st to the end of 2012. The efficiency improvement measures set forth in the Programme produced a financial effect of PLN 834m. The decision was made in line with the strategic objectives for 2011–2015, following the fast-changing macroeconomic landscape.

3.3.4. USE OF ISSUE PROCEEDS TO IMPLEMENT THE ISSUE OBJECTIVES

Grupa LOTOS S.A. did not issue any securities in 2012.

4. GRUPA LOTOS SHARES

4.1. GRUPA LOTOS SHARES ON THE WARSAW STOCK EXCHANGE

The Company shares are listed on Giełda Papierów Wartościowych w Warszawie S.A. (WSE). Trade in securities is settled in PLN.

ISIN	Warsaw Stock Exchange	Thomson Reuters	Bloomberg
PLLOTOS00025	LTS	LTOS.WA	LTS PW

In 2012, Grupa LOTOS shares were included in the following indices:

- WIG
- WIG 20
- WIG Paliwa
- RESPECT Index.

As at December 31st 2012, the Company's market capitalisation was PLN 5.351bn. The share capital is divided into 129,873,362 shares with a par value of PLN 1 per share. Each share confers the right to one vote at the Company's General Meeting.

The Company's stock started 2012 with a price of PLN 24.00 per share. In 2012, the year low price was PLN 21.30 and the year high price was PLN 43.78. At the year end, the price stood at PLN 41.20.

Price of Grupa LOTOS shares (PLN)

	Low	High	Closing price
2009	7.2	32.8	31.8
2010	25.1	37.9	36.4
2011	22.3	49.5	23.3
2012	**21.3**	**43.8**	**41.2**

Based on WSE data.

According to data furnished by the WSE, the total value of trades on the Company shares, that is the aggregate value of all transactions in Grupa LOTOS securities concluded in 2012, was PLN 2.013bn. 54.10% of Grupa LOTOS shares were traded in 2012. The average trading volume per session was 282 thousand shares.

Trade in Grupa LOTOS stock

	Trading value (PLNm)	Share in trade (%)	Average trading volume per session
2009	3,642.6	1.1	381,938
2010	3,684.3	0.9	234,464
2011	3,299.1	1.3	377,048
2012	**2,013.2**	**1.1**	**282,163**

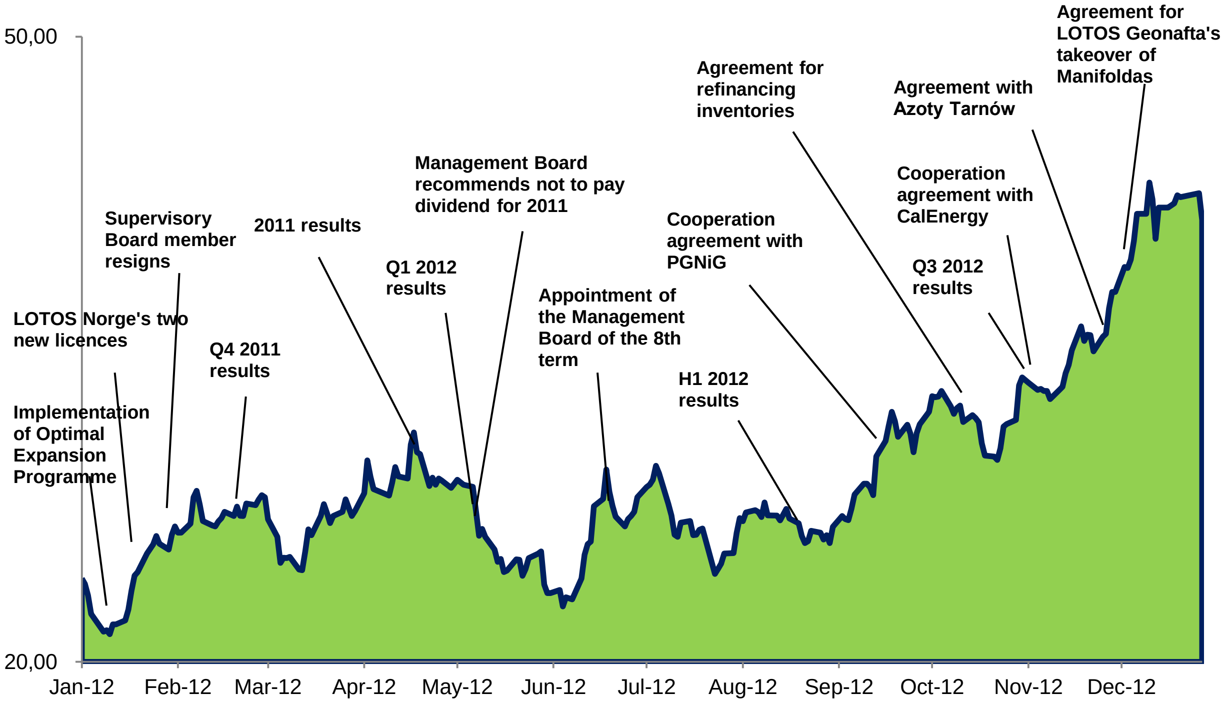
Based on WSE data.

The world's key markets closed out the year 2012 on a bullish note. London's S&P100, New York's NASDAQ Composite and France's CAC40 indices all posted gains of more than a dozen per cent. The Warsaw Stock Exchange saw an uptrend as well. The all year increase in WIG (all-caps index of the main market) was 26.2%, while WIG-20 rose by slightly over 20%. WIG-PALIWA (the index of fuel companies) advanced by 39.0%. Against the background of the economic deceleration in Europe, debt crisis in the eurozone and economic problems in the US, investors' positive sentiments were spurred by decisions of bodies responsible for monetary policy (Monetary Policy Council (RPP), ECB and Fed).

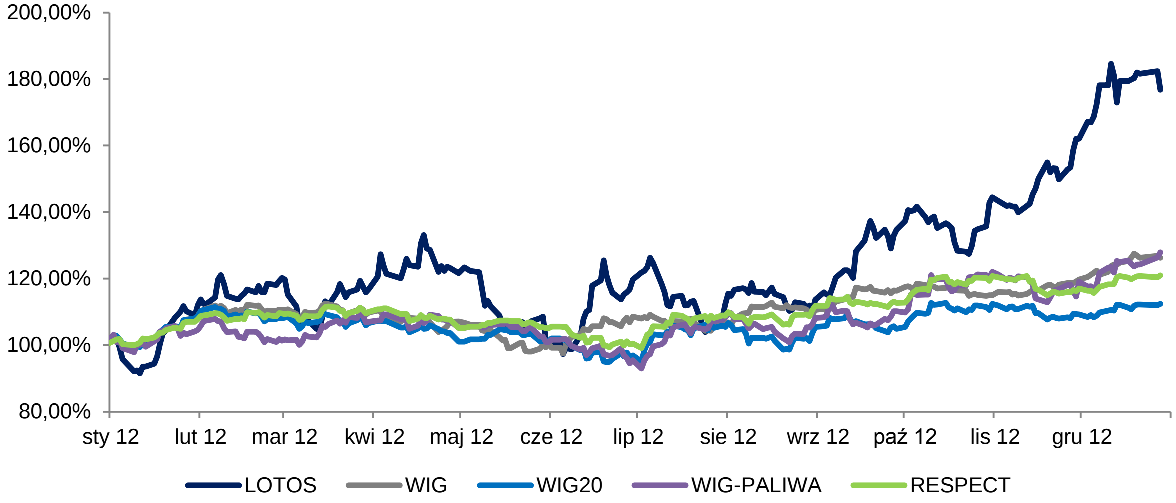
Two major trends were observed in Grupa LOTOS S.A. stock price dynamics in 2012. In the first half of the year, there was a horizontal movement in the stock price, amid increased trading volumes. The strong price rebound in the early June proved a catalyst for a strong uptrend: over the year, the price of Grupa LOTOS stock went up by 76.8%. The price reached its low on January 11st 2012 (PLN 21.33 per share) and peaked on December 11th 2012 (PLN 43.00 per share).

In 2012, the uptrend in Grupa LOTOS S.A. share price was stronger than in the exchange indices WIG, WIG20 and WIG-PALIWA (fuel sector index); the price growth rate significantly overtook the market. Over 2012, the RESPECT index of socially responsible companies grew by 29.2%.

Price of Grupa LOTOS shares in 2012



Price of Grupa LOTOS shares against exchange indices in 2012



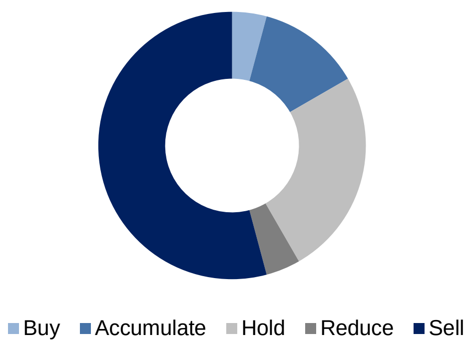
* Rebased (100 = closing price at December 31st 2011)

➢ **Brokers' recommendations in 2012**

To the best of the Company's knowledge, 24 recommendations (including recommendation updates) were issued in 2012:

- 1 recommendation "Buy"
- 3 recommendations "Accumulate"
- 6 recommendations "Hold"
- 1 recommendation "Reduce"
- 13 recommendations "Sell"

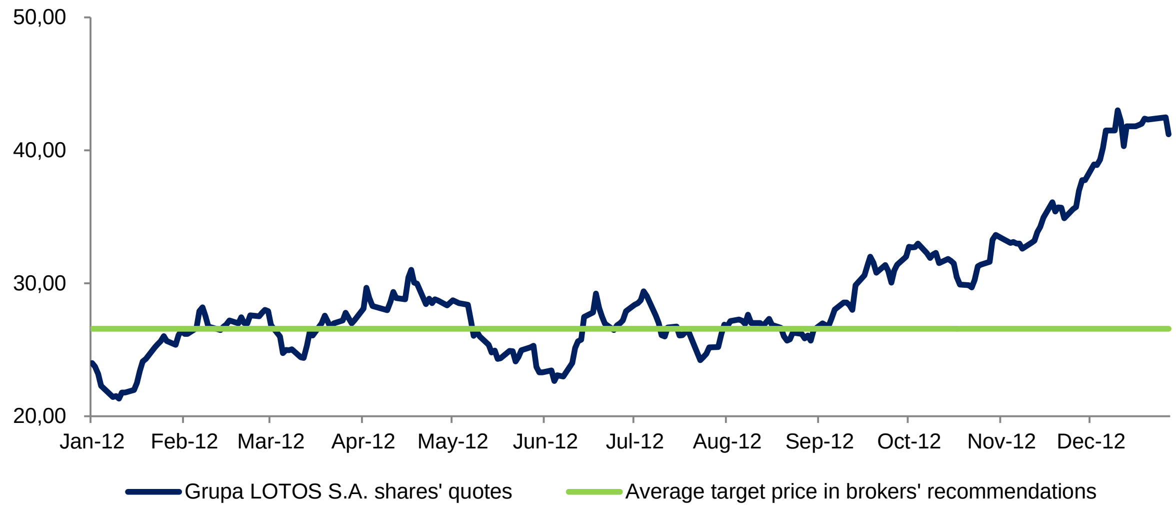
Structure of brokers' recommendations for Grupa LOTOS shares



According to the brokers, the target price of Grupa LOTOS shares fluctuated from PLN 19.40 to PLN 38.90. The average price of Grupa LOTOS shares was PLN 26.58 in 2012.

The market value of Grupa LOTOS shares fluctuated from PLN 21.30 to PLN 43.78. At the end of 2012, the price of Grupa LOTOS shares stood at PLN 41.20.

The average target price in brokers' recommendations against the market price of Grupa LOTOS shares



4.2. DIVIDEND POLICY

Distributions of dividend for 2011–2015 are subject to the Company's strategy for 2011–2015, providing for optimising of financing of the LOTOS Group. Grupa LOTOS S.A.'s financial strategy provides for distributing up to 30% of net profit as dividend.

The Management Board of Grupa LOTOS S.A. recommended that no part of the 2011 net profit be distributed among the Company's shareholders.

On June 28th 2012, acting upon the Management Board's recommendation, the General Meeting resolved to distribute the 2011 profit as follows:

- PLN 306,169,935.90 was transferred to statutory reserve funds,
- PLN 1,500,000.00 was transferred to the Special Account designated for financing corporate social responsibility (CSR) projects.

Dividend and dividend yield (PLN)

Financial year	Dividend	Dividend per share	Share price at the year end	Dividend yield
2005	0.0	0.0	44.2	-
2006	40,932,000.0	0.4	49.3	0.7
2007	0.0	0.0	44.5	-
2008	0.0	0.0	12.0	-
2009	0.0	0.0	31.8	-
2010	0.0	0.0	36.4	-
2011	**0.0**	**0.0**	**23.3**	**-**

** Dividend yield – dividend per share to price per share.*

Historical dividend per share (PLN)

Financial year	Dividend per share	% of net profit	Dividend record date	Dividend payment date
2005	0.0	0.0	-	-
2006	0.4	10.1	Jun 11 2007	not later than Jul 31 2007
2007	0.0	0.0	-	-
2008	0.0	0.0	-	-
2009	0.0	0.0	-	-
2010	0.0	0.0	-	-
2011	**0.0**	**0.0**	**-**	**-**

***** *Dividend record date – date on which the list of shareholders entitled to receive dividend for a given financial year is determined.*

*** Dividend payment date – date on which dividend is paid to the Company's shareholders.*

4.3. ACQUISITION OF TREASURY SHARES

Grupa LOTOS S.A. did not buy back own shares in 2012.

4.4. SHARES AND EQUITY INTERESTS HELD BY MANAGEMENT/SUPERVISORY STAFF

To the best of the Company's knowledge, only the two following members of management staff hold shares in Grupa LOTOS as at March 31st 2013.

Aggregate number and par value of the Company shares and shares in the Company's related entities, held by management and supervisory staff

Management/supervisory staff	Number of Grupa LOTOS shares	Par value of shares (PLN)
Management Board, including:	9,636	9,636
Mr Marek Sokołowski	**8,636**	**8,636**
Mr Zbigniew Paszkowicz	**1,000**	**1,000**
Supervisory Board	0	0
Total	**9,636**	**9,636**

To the best of the Company's knowledge, as at March 21st 2013 members of the management and supervisory staff did not hold any shares in Grupa LOTOS's related entities.

4.5. AGREEMENTS WHICH MAY GIVE RISE TO CHANGES IN THE SHAREHOLDER STRUCTURE

The Management Board of Grupa LOTOS S.A. has no knowledge of any agreements which may give rise to future changes in the number of shares held by the existing shareholders and bondholders.

5. CORPORATE GOVERNANCE

5.1. SHAREHOLDER STRUCTURE

5.1.1. SIGNIFICANT HOLDINGS OF SHARES

Changes in 2011–2012

- **Series C shares in Grupa LOTOS S.A. at the Polish National Depository of Securities and in public trading on the stock exchange**

In Current Reports No. 34/2010 of December 30th 2010, No. 1/2011 of January 5th 2011 and No. 2/2011 of January 7th 2011, the Company reported that Krajowy Depozyt Papierów Wartościowych S.A. (KDPW S.A. – National Depository for Securities) resolved to accept, to the depository of securities, 16,173,362 ordinary bearer Series C shares in the Company and mark them with ISIN code PLLOTOS00025.

On January 10th 2011, the Grupa LOTOS shares specified above were registered with the Polish NDS and the WSE Management Board decided to introduce them, by way of the ordinary procedure, to trading on the main market.

Following the registration, the total number of shares marked with ISIN code PLLOTOS00025 was 129,804,251.

- **Reduction of ING Otwarty Fundusz Emerytalny's share of total vote at the General Meeting of Grupa LOTOS S.A.**

In Current Report No. 8/2011 of February 7th 2011, the Company reported that, following the sale transaction of Grupa LOTOS shares, settled on February 2nd 2011, ING Otwarty Fundusz Emerytalny reduced its share in total vote at the General Meeting of Grupa LOTOS below 5%. Prior to the transaction, ING Otwarty Fundusz Emerytalny held 6,640,532 Grupa LOTOS shares, representing 5.11% of share capital. On February 7th 2011, 5,957,442 Grupa LOTOS shares, representing 4.59% of share capital, were registered in ING Otwarty Fundusz Emerytalny's securities account.

Grupa LOTOS shares in the State Treasury's portfolio

At the end of 2011, the State Treasury held a total of 69,076,392 ordinary bearer shares in the Company, representing 53.19% of the share capital and in total vote at the General Meeting (GM) of Grupa LOTOS S.A. In 2012, no change occurred in the of key shareholding structure.

Shareholders holding at least 5% of total vote at the GMs convened in 2012

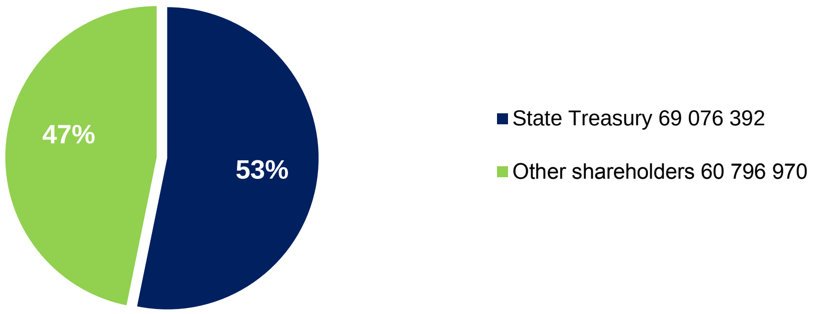
Shareholder	GM date	Number of votes	Share of the votes at GM	Share in total vote
State Treasury	Feb 29 2012	**69,076,392**	78.8%	**53.2%**
	Jun 28 2012		84.6%	
	Nov 28 2012		76.1%	

Shareholders as at December 31st 2011, December 31st 2012 and March 21st 2013

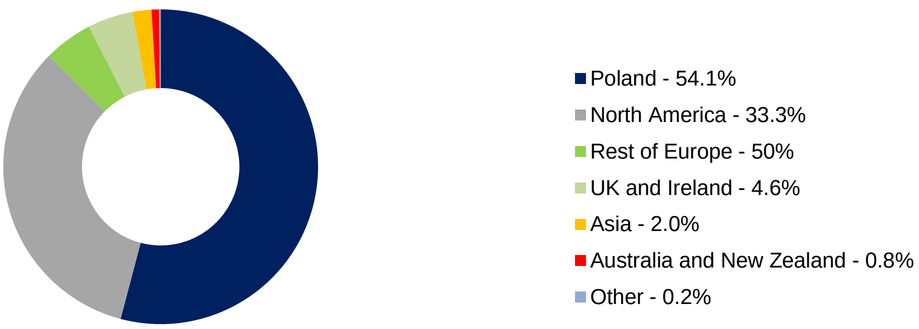
Shareholders	Number of shares/votes	Par value of shares	% of the share capital/ total vote at GM
State Treasury	69,076,392	69,076,392	***53.2%***
Other shareholders	60,796,970	60,796,970	***46.8%***
Total	129,873,362	129,873,362	***100.0%***

To Grupa LOTOS's knowledge, the shareholder structure as at the date of release of this report was as follows:

Shareholder structure as at December 31st 2011, December 31st 2012 and March 21st 2013



Geographical structure of minority interests

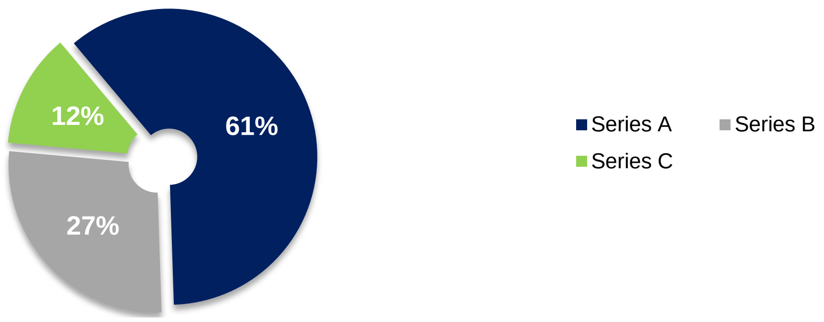


** Based on the identified minority interests.*

- **Structure of share capital**

The share capital of Grupa LOTOS S.A. is divided into 129,873,362 fully paid-up ordinary shares with a par value of PLN 1 per share; each share carries the right to one vote at the GM and the right to dividend.

Structure of Grupa LOTOS S.A.' share capital by series



5.1.2. HOLDERS OF SECURITIES WHICH CONFER SPECIAL CONTROL POWERS, WITH THE DESCRIPTION OF THE POWERS

Grupa LOTOS S.A. has not issued any securities which would vest the shareholders with any special control powers.

5.1.3 SPECIAL RIGHTS OF THE STATE TREASURY AND HOW THESE RIGHTS ARE EXERCISED IN COMPANIES

The Act on Special Rights Vested in the Minister Competent for the State Treasury and How Those Rights Should Be Exercised at Certain Companies or Groups of Companies Operating in the Power, Crude Oil and Gaseous Fuels Sectors, dated March 18th 2010 (Dz. U. No. 65, item 404) ("the Act"), introduced the institution of a special officer responsible for the protection of critical infrastructure. Under the Act, the minister competent for the State Treasury has the right to raise and objection against a resolution adopted, or any other act in law performed, by the Company's Management Board to make a disposition with respect to any of the assets included in the single list of facilities, installations, equipment, and services comprising critical infrastructure, referred to in Art. 5b.7.1 of the Polish Crisis Management Act of April 26th 2007, if such disposition constitutes a real threat for the operation, continuity of operation and integrity of critical infrastructure. The minister competent for the State Treasury may also raise an objection with respect to any resolution by the Company's governing body providing for:

- dissolution of the Company,
- changes in the intended use or discontinuation of use of any of the Company's assets (1) included in the single list of facilities, installations, equipment, and services comprising critical infrastructure, referred to in Art. 5b.7.1 of the Polish Crisis Management Act of April 26th 2007,
- change in the Company's business profile,

- sale or lease of the Company's business or its organised part, or creation of any proprietary interest therein,
- adoption of the budget, plan of investment activities, or a long-term strategic plan,
- relocation of the Company's registered office abroad,

if the implementation of any such resolution could constitute a real threat for the operation, continuity of operation and integrity of critical infrastructure.

(1) such assets comprise:

- in the power sector – infrastructure used for the purpose of generation or transmission of electricity;

- in the oil sector – infrastructure used for the purpose of production, refining, processing, storage and transmission via pipelines of crude oil and petroleum products, as well as seaports used for handling crude oil and petroleum products;

- in the gaseous fuels sector – infrastructure used for the purpose of production, refining, processing, storage and transmission via gas pipelines of gaseous fuels, as well as LNG terminals.

In accordance with the Act, the Company's Management Board, acting in consultation with the minister competent for the State Treasury and the Head of the Government Centre for Security, has the right to appoint and remove from office a special officer responsible for critical infrastructure protection at the Company. The special officer's duties include in particular providing the minister competent for the State Treasury with information on the execution by the Company's governing bodies of any of the acts in law referred to above, providing the Head of the Government Centre for Security with information on critical infrastructure whenever requested, and –in cooperation with the Head of the Government Centre for Security – providing and receiving to or from other entities information on any threats to the critical infrastructure.

The special officer responsible for protection of critical infrastructure is authorised to request from company governing bodies any documents or explanations regarding the issues referred to above, and, having analysed them, is required to submit the same to the minister competent for the State Treasury and the Head of the Government Centre for Security, along with the officer's written position, including grounds, regarding any issue at hand. On July 11th 2011, Grupa LOTOS S.A. received a notification to the effect that its assets have been included in the list of assets, facilities, installations, equipment, and services comprising critical infrastructure. On August 23rd 2011, the Management Board of Grupa LOTOS S.A. appointed a special officer responsible for protection of critical infrastructure.

5.1.4. LIMITATIONS ON THE EXERCISE OF VOTING RIGHTS AT THE GENERAL MEETING

One share in Grupa LOTOS S.A. confers the right to one vote at its GM. However, pursuant to the Company's Articles of Association, the voting rights of Company shareholders are limited in such a manner that none of them can exercise more than 10% of the total vote at the Company as at the day on which the General Meeting is held, with a proviso that for the purpose of determining the obligations of buyers of significant holdings of shares provided for in the Act on Public Offering, Conditions Governing the Introduction of Financial Instruments to Organised Trading, and Public Companies of July 29th 2005, and the Act on Insurance Activity of May 22nd 2003, such limitation of voting rights is deemed non-existent.

The above limitation does not apply to:

1) shareholders which as at the date of the General Meeting's resolution imposing the limitation of voting rights are holders of shares conferring more than 10% of the total vote at the Company;

2) shareholders acting together with shareholders defined in item 1 pursuant to agreements concerning joint exercise of voting rights.

For the purpose of limiting the voting rights as referred to above, the votes of shareholders bound by a parent-subsidiary relationship shall be aggregated in the following manner:

1. A shareholder shall be any person, including a parent and a subsidiary of such person, directly or indirectly entitled to exercise voting rights at the General Meeting under any legal title, including persons who do not hold shares in the Company, in particular usufructuaries, pledgees, holders of rights under depositary receipts, as defined in the Act on Trading in Financial Instruments of July 29th 2005, as well as persons entitled to participate in the General Meeting despite having disposed of their shareholdings after the record date.

2. A parent or a subsidiary shall be any person which:

   1) meets the relevant criteria set forth in Art. 4.1.4) of the Commercial Companies Code, or

   2) is a dominant company, a subsidiary or both a dominant company and a subsidiary within the meaning of the Act on Competition and Consumer Protection of February 16th 2007, or

   3) is a parent, ultimate parent, subsidiary, lower-tier subsidiary, jointly-controlled entity or both a parent (including an ultimate parent) and a subsidiary (including a lower-tier subsidiary and a jointly-controlled entity) within the meaning of the Accountancy Act of September 29th 1994, or

   4) exerts (in the case of a parent) or is subject to (in the case of a subsidiary) significant influence within the meaning of the Act on the Transparency of Financial Relations between State Authorities and State-Controlled Enterprises, as well as on Financial Transparency of certain Entrepreneurs, of September 22nd 2006, or

   5) whose votes conferred by Company shares held directly or indirectly are aggregated with votes of other person or persons pursuant to the Act on Public Offering, Conditions Governing the Introduction of Financial Instruments to Organised Trading, and Public Companies of July 29th 2005, in connection with the holding, disposal or acquisition of significant holdings of shares in the Company.

Shareholders whose votes are aggregated or reduced pursuant to the rules described above, are jointly referred to as a Grouping. The aggregation of votes consists in adding up all the votes held by individual shareholders in a

Grouping. The reduction of votes involves decreasing the total number of votes at the General Meeting held by shareholders in a Grouping.

The reduction of votes is made as follows:

1) the number of votes of the shareholder holding the highest number of votes in the Company from among all the shareholders in a Grouping is reduced by the number of votes in excess of 10% of the total number of votes in the Company held by all the shareholders in the Grouping;

2) if, despite the reduction referred to above, the total number of votes held by the shareholders in the Grouping exceeds 10% of the total vote at the Company on the date the General Meeting is held, the number of votes held by the other shareholders in the Grouping is further reduced. Such further reduction is made in a sequence established based on the number of votes held by individual shareholders in the Grouping (from the highest to the lowest). The number of votes of the Grouping is further reduced until the number of votes held by the shareholders in the Grouping does not exceed 10% of the total vote at the Company;

3) if the sequence for the purpose of the reduction of votes cannot be established due to the fact that one or more shareholders hold the same number of votes, the votes of shareholders holding the same number of votes are reduced proportionally, with fractional numbers rounded down to the whole number of shares. To the extent not provided for above, the rules set forth in the preceding items apply accordingly;

4) a shareholder whose voting rights have been limited in each case retains the right to exercise at least one vote;

5) the limitation of voting rights also applies to shareholders absent from the General Meeting.

In order to determine the basis for aggregation or reduction of votes, each of the Company's shareholders, the Management Board, the Supervisory Board, and individual members of these bodies, as well as the Chairperson of the General Meeting, may request that a Company shareholder subject to the limitation of voting rights disclose whether it is a parent or a subsidiary of any other Company shareholder within the meaning of the Company's Articles of Association. The authority referred to in the previous sentence includes also the right to request a Company shareholder to disclose the number of votes held individually or jointly with other shareholders with respect to which it is a parent or a subsidiary within the meaning of the Company's Articles of Association. A person who fails to perform or improperly performs the disclosure obligation referred to in the first sentence may exercise its voting rights from a single share only, until the disclosure obligation is duly fulfilled, and any attempts to exercise its voting rights from the remaining shares are ineffective.

When in doubt, the provisions concerning the limitation of voting rights are interpreted in accordance with Art. 65.2 of the Civil Code.

The limitation of voting rights expires once the shareholding of a Company shareholder which as at the date of the General Meeting's resolution imposing the limitation of voting rights held shares conferring more than 10% of the total vote at the Company falls below 5% of the Company's share capital.

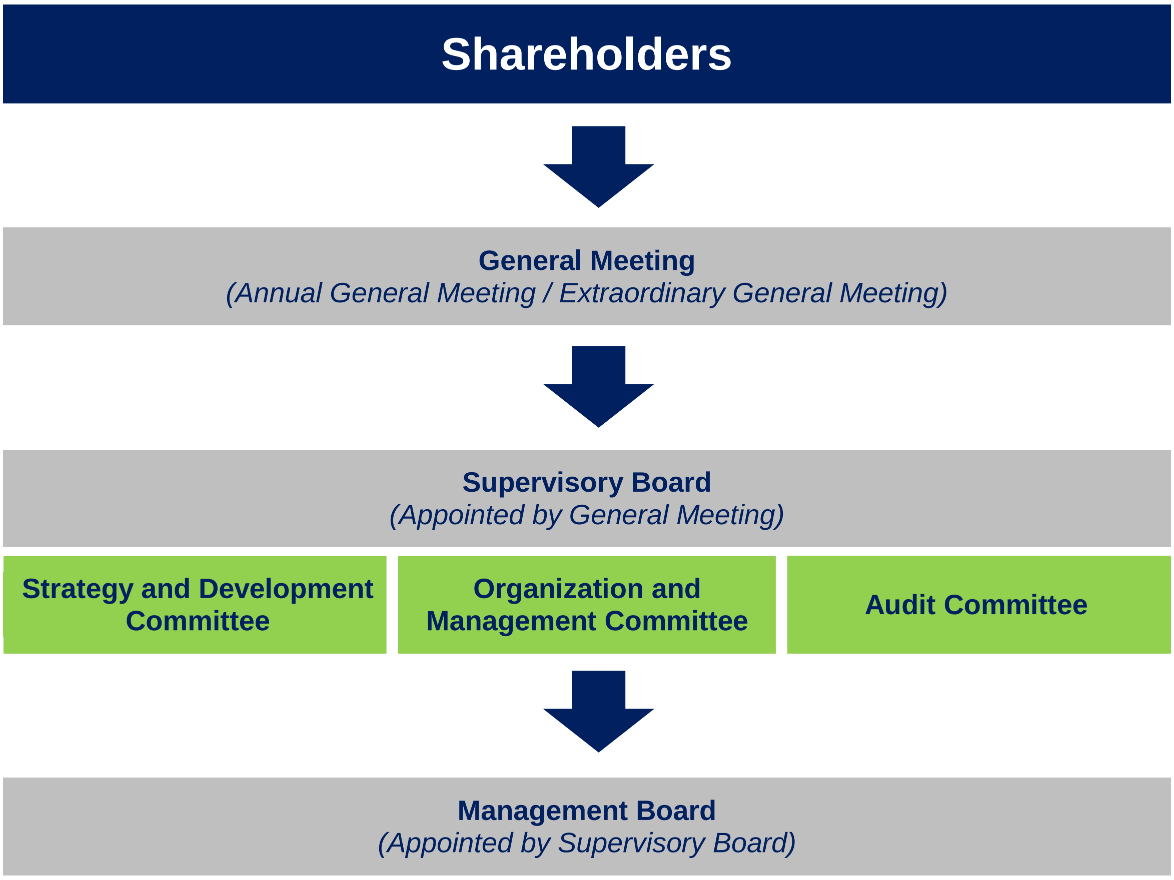
Subject to the relevant provisions of the Commercial Companies Code, a material change may be introduced in the Company's business profile without the buy-out of Company shares held by the shareholders who do not agree to such a change.

5.1.5. RESTRICTIONS ON TRANSFERABILITY OF SECURITIES

No restrictions apply to transferability of ownership rights to any shares issued by Grupa LOTOS S.A.

5.2. THE COMPANY'S GOVERNING BODIES

Grupa LOTOS S.A. – corporate governance structure



5.2.1. GENERAL MEETING OF GRUPA LOTOS S.A.

The General Meeting (GM) of Grupa LOTOS S.A. operates under the Company's Articles of Association (consolidated text of December 21st 2012 and the Rules of Procedure for the General Meeting of the Company (consolidated text of August 26th 2009).

General Meetings are held at the Company's registered office and are convened by the Management Board of Grupa LOTOS S.A., as provided for in the Articles of Association or in the Commercial Companies Code, by publishing an announcement on the Company's website and in the manner determined for publication of current reports, in accordance with the provisions of the Act on Public Offering, Conditions Governing the Introduction of Financial Instruments to Organised Trading, and Public Companies.

In 2012, an Annual General Meeting (AGM) was held on June 28th. The right to convene an AGM rests also with the Supervisory Board in the event that the Management Board fails to convene it within six months after the end of the financial year.

Extraordinary General Meetings (EGM) are convened by the Management Board on its own initiative, by the Supervisory Board (if the Supervisory Board deems it appropriate), or by shareholders representing at least half of the Company's share capital or at least half of the total vote at the Company. In 2012, an EGM was held twice, on February 29th and November 28th.

A shareholder or shareholders representing at least 1/20 of the Company's share capital may request that an EGM be convened and that certain items be placed on the agenda of a General Meeting. If an EGM is not convened within two weeks of the submission of such a request to the Management Board, the Registry Court may authorise the requesting shareholders to convene the Extraordinary General Meeting.

A request to convene a General Meeting and include particular items on its agenda, made by parties entitled to do so, should be presented with grounds. A shareholder or shareholders representing at least 1/20 of the Company's share capital may, before a GM, submit to the Company draft resolutions concerning items which have been or are to be placed on the agenda of the General Meeting.

Only persons who are the Company shareholders sixteen days prior to the date of a General Meeting (i.e. on the date of registration of participation in the GM) are entitled to participate in the General Meeting. Holders of rights under registered shares or provisional certificates (*świadectwa tymczasowe*) as well as pledgees and usufructuaries holding voting rights are entitled to participate in the General Meeting, provided that they are entered in the Share Register on the registration date. A Shareholder may participate in a General Meeting and exercise voting rights in person or by proxy. The proxy is obliged to disclose to the shareholder any circumstances leading to any actual or potential conflict of interests and may vote exclusively in line with the voting instructions issued by the appointing shareholder.

Any matter to be discussed at a General Meeting is subject to prior consideration by the Supervisory Board. No resolution may be adopted on matters not included in the agenda of the General Meeting, unless the Company's entire share capital is represented at the GM and no objections to the adoption of such resolution are raised by any of the persons participating in the GM, with the exception of motions to convene an Extraordinary General Meeting and procedural motions. Resolutions of a General Meeting are adopted by the absolute majority of votes, unless the Articles of Association or Commercial Companies Code provide otherwise. Resolutions and proceedings of a General Meeting are recorded by a notary public. The minutes of the GM are signed by the Chairman of the GM and the notary public. The powers and proceedings of the General Meeting of Grupa LOTOS S.A. are stipulated in detail in the Association and Rules of Procedure for the General Meeting.

5.2.2. SUPERVISORY BOARD OF GRUPA LOTOS S.A.

The Supervisory Board of Grupa LOTOS S.A. operates under the Company's Articles of Association (consolidated text of December 21st 2012) and the Rules of Procedure for the Supervisory Board of Grupa LOTOS S.A. (consolidated text of December 17th 2009).

According to the provisions of the Company's Articles of Association currently in force, the Supervisory Board may comprise five to nine members, appointed for a joint three-year term of office by the General Meeting in a secret ballot, by an absolute majority of votes, from an unlimited number of candidates. The number of Supervisory Board members is determined by the General Meeting. The Chairperson of the Supervisory Board is appointed by the General Meeting, while the Deputy Chairperson and the Secretary are elected by the Supervisory Board from among its other members. A Supervisory Board member or the entire Board may be removed at any time prior to expiry of the office term.

Notwithstanding the above, the State Treasury is entitled to appoint and remove from office one member of the Supervisory Board, as long as it remains a shareholder in the Company.

The Supervisory Board exercises ongoing supervision over the Company's business, across all areas of its operations. The Supervisory Board performs its duties collectively, but it may delegate its members to individually perform certain tasks or functions and may set up ad hoc or standing committees to exercise supervision in specific areas of the Company's activities. Standing committees include the Audit Committee, Strategy and Development Committee and Organisation and Management Committee.

Members of the Supervisory Board	Function on Supervisory Board of 8th term	Supervisory Board of 8th term	Biography, professional experience
 **Wiesław Skwarko**	Chairman	Jun 27 2011–	http://www.lotos.pl/inwestorski/aktualnosci/wiadomosci/28830
 **Marcin Majeranowski**	Deputy Chairman	Feb 29 2012–	http://www.lotos.pl/inwestorski/aktualnosci/wiadomosci/29001
 **Oskar Pawłowski**	secretary	Jun 27 2011–	http://www.lotos.pl/inwestorski/aktualnosci/wiadomosci/28836
 **Małgorzata Hirszel**	member	Jun 27 2011–	http://www.lotos.pl/inwestorski/aktualnosci/wiadomosci/28836
 **Agnieszka Trzaskalska**	member	Feb 29 2012–	http://www.lotos.pl/inwestorski/aktualnosci/wiadomosci/29001

 **Michał Rumiński**	member	Jun 27 2011–	http://www.lotos.pl/inwestorski/aktualnosci/wiadomosci/28836
Leszek Starosta	Deputy Chairman member	Jan 1–Jun 27 2011 Jun 27 2011–Feb 29h 2012	http://www.lotos.pl/inwestorski/aktualnosci/wiadomosci/28836

Procedures for and the scope of powers and duties of the Supervisory Board are defined in the Rules of Procedure for the Supervisory Board of Grupa LOTOS S.A.

Supervisory Board's committees Dedicated standing committees:

The Supervisory Boards' Strategy and Development Committee (SDC)

Members	Position held on the SDC during the Supervisory Board's 8th term of office	Term of office
Wiesław Skwarko	Chairman	Jul 11 2011 –
Małgorzata Hirszel	member	Jul 11 2011 –
Michał Rumiński	member	Jul 11 2011 –
Agnieszka Trzaskalska	member	Mar 8 2012 –
Marcin Majeranowski	member	Mar 8 2012 –
Rafał Wardziński	member	Jul 11 2011–Jan 27 2012 (resigned from the Supervisory Board)

provides opinions and recommendations to the Supervisory Board on matters related to planned investment programmes with a material bearing on the Company's asset base.

Organisation and Management Committee (OMC)

Members	Position held on the OMC during the Supervisory Board's 8th term of office	Term of office
Agnieszka Trzaskalska	Chairwoman	Mar 8 2012 –
Małgorzata Hirszel	member	Jul 11 2011 –
Oskar Pawłowski	member	Jul 11 2011 –
Marcin Majeranowski	member	Mar 8 2012 –
Leszek Starosta	Chairman	Jul 11 2011–Feb 29 2012 (removed from the Supervisory Board)
Michał Rumiński	member	Jul 11 2011–Mar 8 2012 (resigned from membership in the OMC)

provides the Supervisory Board with opinions and recommendations regarding the management structure, organisation-related solutions, remuneration system and recruitment of personnel, with a view to enabling the Company to achieve its

The Supervisory Board's Audit Committee (AC)

Members	Position held on the AC during the Supervisory Board's 8th term of office	Term of office
Michał Rumiński,	Chairman (since Aug 11 2011)	Jul 11 2011 –
Oskar Pawłowski,	member	Jul 11 2011 –
Wiesław Skwarko,	member	Jul 11 2011 –
Marcin Majeranowski	member	Mar 8 2012 –
Rafał Wardziński,	member	Jul 11 2011–Jan 27 2012 (resigned from the Supervisory Board)

provision of ongoing advisory support to the Supervisory Board with respect to proper implementation of the policies related to budgetary and financial reporting, the Company's internal control function and cooperation with its

➢ **Delegation of specific duties to individual Supervisory Board members**

The Supervisory Board may delegate its members to perform specific supervisory duties individually.

In performance of its powers, the Supervisory Board, by virtue of its decision of October 24th 2012 (Resolution No. 58/VIII/2012), delegated Mr Oskar Pawłowski to independently perform supervision over the legal aspects related to the Company's continued participation in the consortium developing the YME field and the dispute with the field's operator.

While Mr Marcin Majeranowski, by virtue of Resolution No. 66/VIII/2013 of January 11th 2013, was delegated to independently perform supervision over the execution of the capital reconstruction programme of the LOTOS Group and the implementation of the programme's schedule.

5.2.3. MANAGEMENT BOARD OF GRUPA LOTOS S.A. AND POWERS OF INDIVIDUAL MEMBERS

The Management Board of Grupa LOTOS S.A. operates pursuant to the Company's Articles of Association, as adopted by virtue of Management Board Resolution No. 6/VI/2007 dated January 23rd 2007 and approved by virtue of Supervisory Board Resolution No. 70/VI/2007 dated January 29th 2007. From January 1st 2012 until the end of the seventh term of office, the Management Board of Grupa LOTOS S.A. consisted of the following persons:

Management Board Members	Function
Paweł Olechnowicz	President of the Management Board, Chief Executive Officer
Mariusz Machajewski	Vice-President of the Management Board, Chief Financial Officer
Marek Sokołowski	Vice-President of the Management Board, Chief Operation Officer
Maciej Szozda	Vice-President of the Management Board, Chief Commercial Officer

In view of the expiry of the Management Board's seventh term of office, the Supervisory Board, following a recruitment procedure, resolved to appoint five members of the Management Board of the eighth joint term of office, commencing as of June 28th 2012.
From June 28th 2012 to December 31st 2012 and as at the date of release of these financial statements, the Company's Management Board of the eighth term of office was composed of the following persons:

Management Board Members	Function	Scope of responsibilities
 **Paweł Olechnowicz**	President of the Management Board, Chief Executive Officer	In charge of the overall management and direction of the LOTOS Group's operations.
 **Mariusz Machajewski**	Vice-President of the Management Board, Chief Financial Officer	In charge of the overall management of the Company's economic, financial and accounting functions, as well as the assets and restructuring processes. Also, in charge of oversight of development of corporate guidelines and standardisation of processes in the area of agreement execution, counterparty selection and assessment, as well as development of IT systems and telecommunications services.
 **Zbigniew Paszkowicz**	Vice-President of the Management Board, Exploration and Production	In charge of overall management of the LOTOS Group's upstream segment, including upstream companies.
 **Marek Sokołowski**	Vice-President of the Management Board, Chief Operation Officer	In charge of the overall production and technical management, technology development and capex programmes (technical and technological development projects). In 2004–2011, Mr. Sokołowski was in charge of the refinery extension – the 10+ Programme. Also responsible for oversight of companies allocated to the Group's operating segment.
 **Maciej Szozda**	Vice-President of the Management Board, Chief Commercial Officer	In charge of the overall management of marketing, supply and distribution processes at the LOTOS Group. Also responsible for oversight of companies allocated to the Group's marketing segment.

For more information of the professional experience of the Management Board's members, see the Company's Web page at: http://inwestor.lotos.pl/1137/lad_korporacyjny/struktura_organizacyjna#group-people-1

The Management Board represents Grupa LOTOS S.A. before third parties and manages its corporate affairs. Moreover, the individual members of the Management Board perform duties in line with the division of powers and responsibilities resulting from their operational functions within the Company. Each member of the Management Board is also authorised to represent the Company in all court and out-of-court transactions relating to the operation of the Company's business, with the exception of matters reserved for the General Meeting or Supervisory Board under the Commercial Companies Code or the Company's Articles of Association, as well as matters falling outside the scope of ordinary management of the business where they require the Management Board's prior resolution and matters within the powers of another member of the Management Board.

The following matters require the Management Board's resolution:

1. Setting the organisational rules of the Company, including organisation of the Company's business,
2. Setting annual budget for the Company,
3. Adopting strategy for the LOTOS Group,
4. Setting rules of procedure for the Company's business as required under the law,
5. Making the Company's equity investments and implementing all projects related to capital expenditure in property, plant and equipment (with the exception of replacement projects) with a value of up to PLN 100,000,
6. Exercising the Company's voting rights at the General Meetings of the subsidiaries, with regard to:
   - Appointing or removing members of the Management and Supervisory Boards,
   - Coverage of loss,
   - Increasing or reducing the share capital,
   - Merging with another company or transforming the company,
   - Selling or leasing the Company's business and/or encumbering it with usufruct rights,
7. Appointing and removing members of the Management and Supervisory Boards who are appointed or removed directly by Grupa LOTOS S.A.,
8. Establishing companies under commercial law,
9. Acquiring and selling shares in limited-liability companies,
10. Acquiring and selling shares, except where the shares are acquired or disposed in public trading in securities, unless such acquisition or disposal results in gaining or losing the status of the parent,
11. Acquiring and disposing of real property, perpetual usufruct rights or interest in real property,
12. Establishing or joining partnerships, organisations or ventures which involve unlimited liability enforceable against the Company's assets,
13. Preparing:
    - the Company's financial statements for the previous financial year, in accordance with the Polish Accountancy Act, with the Directors' Report on the Company's operations for the previous financial year,
14. consolidated financial statements and a report on the LOTOS Group's operations for the previous financial year,
15. Convening annual and extraordinary General Meetings in due time, on its own initiative, at a written motion of the Supervisory Board or at a request of a shareholder or shareholders representing at least one-tenth of the share capital, as well as in other cases as provided for in the Commercial Companies Code,
16. Setting the agenda of a GM,

17. Matters falling outside the scope of ordinary management of the enterprise,
18. Matters which have been objected to by at least one of the members of the Management Board,
19. Matters which must be resolved by way of Management Board resolutions if so required by the President of the Management Board or at least half of the members of the Management Board, and which fall within the scope of responsibilities of particular members of the Management Board,
20. Granting powers of proxy.

Pursuant to the provisions of the Commercial Companies Code and the Company's Articles of Association, the Management Board, having obtained the Supervisory Board's opinion, is authorised to move to the GM for issuance of new shares or buyback of the existing shares. Further, if authorised accordingly by the relevant provisions of the Company's Articles of Association and the GM's resolution, the Management Board may, by way of a resolution(s) decide to issue new shares within the authorised share capital defined by the General Meeting.

Ordinary matters of the Company, not requiring the Management Board's resolution, are carried out by the President acting independently and by individual members of the Management Board, in line with the division of powers and responsibilities defined under the Organisational Rules of Grupa LOTOS.

Moreover, the President of the Management Board conducts and supervises the Company's corporate matters in the scope of:

- Convening and presiding over meetings of the Management Board,
- Maintaining the Management Board's documentation, files and meeting minutes,
- Performing obligations under commercial law and matters relating to the register of entrepreneurs,
- Ensuring that necessary services are rendered to the Company's governing bodies and minutes of proceedings are prepared,
- Representing the Management Board before the Company's other governing bodies, subject to the provisions of
- the Commercial Companies Code and the Company's Articles of Association.

Rules of procedure for the Management Board, including procedures for calling meetings, adopting and archiving resolutions, as well as the scopes of powers and duties of individual Board members are set fort in

the Rules of Procedure for the Management Board of Grupa LOTOS S.A.

- **Rules governing appointment and removal of management staff**

In accordance with the Articles of Association of Grupa LOTOS S.A., the Management Board may be composed of three to seven members. The Supervisory Board appoints and determines the number of members of the Management Board. Members of the Management Board are appointed by the Supervisory Board following a qualification procedure carried out pursuant to the Regulation of the Polish Council of Ministers of March 18th 2003 concerning qualification procedures for members of management boards of certain commercial-law companies (Dz. U. No. 55, item 476), taking into consideration "The Best Practices to be Followed in the Selection of Candidates to Governing Bodies of Companies of Key Importance to the State Treasury," defined by the Minister of State Treasury.

Management Board members are appointed for a joint term of three years. The President, Vice-Presidents and Members of the Management Board, as well as the entire Management Board, may at any time be removed from office or suspended in duties by the Supervisory Board if there is a valid reason for doing so. Each Member's mandate expires no later than on the date of the General Meeting which approves the financial statements for the previous full financial year. Supervisory Board resolutions to appoint or remove a Management Board member or the entire Management Board from office require that at least two thirds of Supervisory Board members are present and voting. A Management Board member's mandate expires upon resignation from office.

5.2.4. RULES FOR AMENDING THE ARTICLES OF ASSOCIATION OF GRUPA LOTOS S.A.

An amendment to the Articles of Association requires that a relevant resolution be adopted by the General Meeting by an absolute majority of votes, save for amendments to Par. 10.1 of the Articles of Association which require that four fifths of the total vote be cast in favour of the amending resolution and at least half of the Company's share capital be represented at the General Meeting.

After the General Meeting adopts a resolution on amending the Company's Articles of Association, the Management Board of Grupa LOTOS S.A. notifies a registry court of the amendments. The amendments come into force upon their registration by the court. A consolidated text of the Articles of Association incorporating the amendments is then produced by the Supervisory Board provided that the Board receives relevant authorisation from the General Meeting. On November 28th 2012, the Extraordinary General Meeting of Grupa LOTOS S.A., by virtue of its Resolutions No. 2-6, amended the Company's Articles of Association. The amendments were registered with the National Court Register on December 17th 2012. The consolidated text of the Company's Articles of Association was adopted by the Supervisory Board in its Resolution No. 64/VIII/2012 of December 21st 2012.

5.3. CORPORATE GOVERNANCE PRINCIPLES APPLICABLE AT GRUPA LOTOS S.A. IN 2012

Voluntary corporate governance principles applied by Grupa LOTOS S.A.

➢ **Code of Best Practice for WSE Listed Companies, Chapter I Recommendations, item 1**

The key objectives that Grupa LOTOS S.A. pursues by adhering to the rules of corporate governance include:

- transparency of its operations as a listed company,
- trust in its relations with stakeholders,
- consistency in creating value for shareholders.

➢ **The Company's information policy and relations with the capital market**

Grupa LOTOS S.A. is keen to ensure that its relations with investors and stakeholders are forged and fostered based on the values of equality and dialogue to find solutions satisfactory for both parties. The Company is open to new communication tools and content exchange platforms and strives to improve the quality of its message.

Grupa LOTOS's Investor Relations Team (IR) makes every effort to present to investors a precise, reliable and transparent picture of the Company's operations and financial standing. The team provides up-to-date information in compliance with the principles of involvement of, availability to and equal treatment of all market participants.

The Company uses a broad range of IR tools, including mailing, participation in conferences for shareholders, presentations, conference calls, one-on-one meetings, open-house days for analysts and investors and participation in Akcja Inwestor (Investor Campaign) organised by the Puls Biznesu daily which awarded the Company for its active participation in the 2012 campaign.

Odpowiada Inwestorom

In 2012, the Investor Relations Team supported the Company's Management Board in organising meetings with investors and maintaining regular relations with equity analysts and capital market institutions. On October 15th 2012, the annual Analyst's Day was organised in Gdańsk, with the development of the LOTOS service station network being its leading theme.

The Company's Internet Investor Relations Service has been designed with a view to reaching a broader range of interested parties. The service is updated on an ongoing basis, and published in Polish and English.

The corporate events calendar (quarterly earnings reports, operations of the GM and other events at the LOTOS Group which might affect the price of the Company shares) is published in the bookmark "Investor's Calendar". The calendar includes links to relevant materials (periodic reports, management presentations, .mp3 files with recordings of the Management Board's conference calls with analysts and all documents relating to the GM).

Code of Best Practice for WSE Listed Companies, Chapter I Recommendations, item 3

Pursuant to Par. 8 of the Company's Articles of Association, the Management Board is authorised to make the decision, if any, to broadcast in real time the proceedings of the General Meeting.

Code of Best Practice for WSE Listed Companies, Chapter I Recommendations, item 5

Remuneration of the Management Board and Supervisory Board members is subject to limitations and conditions prescribed under the Act on Remunerating Persons Who Manage Certain Legal Entities of March 3rd 2000 (Compensation Cap Act) (Dz. U. of 2000 No 26, item 306, as amended).

On November 13th 2009, the Supervisory Board – acting within the powers vested in it by Par. 13.2.1 of the Company's Articles of Association and the Act of March 3rd 2000 – decided that Vice-Presidents of the Company's Management Board would receive remuneration equal to six-fold the average monthly salary in the non-financial corporate sector, net of bonuses paid from profit in the fourth quarter of the preceding year, as announced by President of the GUS (Central Statistics Office). Concurring with the proposal of the Supervisory Board, contained in Resolution No. 63/VII/2009 of November 13th 2009, on December 17th 2009 the Extraordinary General Meeting determined the same remuneration policy for President of the Management Board, while repealing the General Meeting's resolution of August 18th 2000, which until then defined the rules of remuneration for members of the Management Board.

In 2000, acting within its powers vested in it under Par. 9.4 of the Company's Articles of Association, the Extraordinary General Meeting determined the remuneration policy for the members of the Supervisory Board. Pursuant to the policy, Supervisory Board members receive monthly remuneration equal to the average monthly salary in the non-financial corporate sector net of bonuses paid from profit in the fourth quarter of the preceding year, as announced by the President of the GUS (Central Statistics Office).

In line with the amended Compensation Cap Act, in 2012 the members of the Supervisory and Management Boards were entitled to receive individual monthly remuneration in an amount determined on the basis of the average monthly remuneration in the enterprise sector (net of bonuses paid out from profit) in the fourth quarter of 2009.

- **Code of Best Practice for WSE Listed Companies, Chapter I Recommendations, item 9**

Composition of the Supervisory and Management Boards by sex

	Management Board of Grupa LOTOS S.A.		Supervisory Board	
	Women	Men	Women	Men
Dec 31 2009	0	4	1	6
Dec 31 2010	0	4	2	5
Dec 31 2011	0	4	1	5
Dec 31 2012	**0**	**5**	**2**	**4**

Supervisory Board	Number of women	Number of men
Jan 1–Jan 27 2012	1	5
Jan 27–Feb 29 2012	1	4
Feb 29–Dec 31 2012	2	4

Management personnel by sex (as at December 31st 2012)

	Number of women	Number of men
Management Board	0	5
Senior management	7	34
Lower management	41	85
Total	**48**	**123**

- **Code of Best Practice for WSE Listed Companies, Chapter I Recommendations, item 10**

In 2008, the Management Board of Grupa LOTOS S.A. adopted the comprehensive Corporate Social Responsibility Strategy for Grupa LOTOS S.A. until 2012.

In 2011, the document was reviewed through wide-ranging consultations with our stakeholders. Based on the review, focused on the evaluation of previous activities and their context, and on eliciting related expectations, we updated the Strategy whose objectives - as in the case of the objectives of the Company's business strategy - look forward to 2015.

Mission

Our mission is to pursue innovation-oriented sustainable development in the areas of exploration, production and processing of hydrocarbons and marketing of high-quality products, which is conducive to creating lasting value for shareholders, ensuring customer satisfaction, enhancing and leveraging the employee potential, and which is carried out:

- in accordance with corporate social responsibility principles,
- in an environmentally friendly manner, and
- in compliance with the energy security policy.

The Company strives to emerge as the most reputable oil company in the Baltic Sea region, widely recognised for:

- high-quality petroleum products,
- best-quality customer service, and
- professional management style.

The **overriding strategic objective** is to create value for shareholders through optimised utilisation of human and material resources and implementation of development programmes in the field of:

- exploration and production,
- crude processing,
- marketing.

Corporate social responsibility strategy

The LOTOS Group's strategy incorporates social, environmental, ethical and human rights concerns into the Group's core operations and business strategy.

The efforts we undertake in the social and business spheres, in our relations with key stakeholders and in corporate governance are aimed principally to:

- ensure compliance with law and ethical standards,
- increase our positive contribution to social development,
- mitigate possible adverse impacts of our operations and the associated risks,
- maximise our chances for sustainable development over the long term.

- **Values underlying the LOTOS Group's corporate social responsibility:**

- **cleanliness** – stands for compliance with the most exacting environmental standards, commitment to ethical and fair competition, and counteracting human rights abuses,

- **openness** – stands for the right attitude towards change, external needs and expectations, future-oriented approach, and dynamic expansion of international operations,
- **innovation** – stands for the capacity to recognise people's intellectual capital and skills driving the strength and prospects of the LOTOS brand,
- **responsibility** – stands for the right attitude towards mankind and its future, the environment, security of our home country and its international position. Anticipating and addressing the consequences of our decisions

Code of Ethics

In the Code of Ethics implemented in 2012, employees of the LOTOS Group committed to behave in accordance with the following ethical values:

- ✓ **professionalism**
- ✓ **respect**
- ✓ **transparency**
- ✓ **cooperation**

As a company committed to social responsibility in all areas of operations, Grupa LOTOS S.A. endorses and abides by the ten principles of **United Nations Global Compact**, a voluntary international corporate citizenship initiative of unprecedented reach, which the Company joined in 2009.

The system of fundamental CSR values is aligned with key LOTOS brand values which rest on three pillars:

THE FOUNDATIONS OF THE LOTOS GROUP CORPORATE SOCIAL RESPONSIBILITY STRATEGY		
I **SOCIAL RESPONSIBILITY**	**II** **ENVIRONMENTAL RESPONSIBILITY**	**III** **BUSINESS RESPONSIBILITY**
Creation of values for the benefit of the social environment	**Creation of values for the benefit of the natural environment**	**Creation of values for the benefit of economy**
Our activity is characterised by respect for the intellectual capital and diversity, and compliance with human rights standards, including freedom speech and freedom of association. We play an active role in creating new jobs and enhancing the quality of human capital in the areas influenced by our operations. We act to prevent social exclusion and other social issues falling within the scope of the Group's competencies.	Our efforts are geared to limit our negative environmental impact on an ongoing basis, by adherence to relevant standards in the production and processing of hydrocarbons, as well as compliance with stringent environmental standards in the production, transport and sales of oil and petroleum products. In our production activities we employ the best available, state-of-the-art techniques, while remaining on a constant lookout for new technological solutions. We aim to identify and develop ways to harness renewable energy.	In managing our relationship with the outside world, we strive to be predictable and reliable, adhering to ethical standards, based on the principles of transparency and partnership, which influences our profit-making activities and long-term value creation. We carry out initiatives designed to improve security in the energy sector in Poland and in countries, in which we operate, in a socially and environmentally responsible manner. Providing the Polish market with stable fuel supplies, we also engage in the exploration and production of both conventional and unconventional hydrocarbons.

- **Code of Best Practice for WSE Listed Companies, Section I Recommendations, item 11 quality of reporting**

Grupa LOTOS S.A.'s Communications Office is responsible for maintaining a coherent and transparent communication policy of the LOTOS Group by cultivating continued relations with the media. The manner of operation and responsibility of the office are set forth in Grupa LOTOS's procedures and are subject to periodical review and assessment.

Participation in the WSE's RESPECT Index demonstrates Grupa LOTOS S.A.'s adherence to the high reporting standards.

RESPECT Index

Since November 19th 2009, Grupa LOTOS has been continuously included in the first index of socially responsible companies in the CEE region, the RESPECT Index (Responsibility, Ecology, Sustainability, Participation, Environment, Community, Transparency), which includes companies listed on the regulated market of the WSE and excelling in the quality of reporting, investor relations or disclosure standards. The project is designed to identify companies managed in a responsible and sustainable manner. On January 24th 2013, for the sixth time Grupa LOTOS was selected for inclusion in the RESPECT Index which currently comprises 20 listed names.

The RESPECT Index also takes into account the criteria of profitability related to dividend payments and pre-emptive rights, which provide insight into the economic standing of the companies included in the Index.

Grupa LOTOS S.A. takes steps to introduce best practices in such areas as environmental protection, health and safety at work and security of management systems, which have not been regulated by the Polish law. It was the first oil company to secure the Integrated Management System certificate and adopt Global Compact Principles

GRI-compliant Integrated Annual Reports published

In addition to the annual report published in line with the Minister of Finance's Regulation on current and periodic information to be published by issuers of securities, dated February 19th 2009, comprising this Directors' Report, for the fourth time the Company is preparing the electronic version of its integrated report. It contains two consolidated reports: financial report and social report. The former has been prepared in accordance with the International Financial Reporting Standards (IFRS), and the latter – with the Global Reporting Initiative's Sustainable Reporting Framework (G3 GRI).

Obligatory corporate governance principles applied by Grupa LOTOS S.A.

- **Code of Best Practice for WSE Listed Companies, Sections II–IV**

The Best practices section of the Company's website contains up-to-date information on corporate governance at Grupa LOTOS S.A.: Company's and Group's annual Statements of Compliance with corporate governance principles, and reports released via the EBI system.

Since its stock exchange floatation in June 2005, Grupa LOTOS S.A. has adhered to most of the recommendations contained in "Best Practices in Public Companies", and as of early 2008 it follows the Code of Best Practice for WSE Listed Companies, amended by the WSE Supervisory Board resolution of November 21st 2012. As from January 1st 2013, Grupa LOTOS S.A. has applied the Code of Best Practice for WSE Listed Companies as amended by the WSE on November 21st 2012, which is available from the Company's website.

In 2012, Grupa LOTOS S.A. complied with most of the obligatory corporate governance principles set fort in the Code of Best Practice for WSE Listed Companies.

In line with the comply-or-explain principle, which provides that companies should either comply with corporate governance rules or explain any recurring or non-recurring instances of non-compliance, the Management Board has published non-compliance lists with relevant explanations since 2008.

Corporate governance non-compliance reports are released via the EBI system, similarly to current reports. Acting under Par. 29.3 of the WSE Rules, on January 27th 2012 the Company reported a one-off non-compliance with **Rule 5 contained in Section III** of the Code of Best Practice for WSE Listed Companies related to Rafał Wardziński's resignation from the Supervisory Board on that day.

Internal audit and risk management systems in the process of preparing financial statements

In line with the Minister of Finance's Regulation on current and periodic information to be published by issuers of securities, dated February 19th 2009, the Management Board is responsible for the internal control function and its efficient application in the financial reporting process.

Financial statements are prepared, approved and released to the public by following an internal procedure whereunder oversight of the financial reporting process lies within the remit of the Head of Finance and Accounting Centre's Office and the person responsible for keeping the Company's accounting books (Chief Accountant). Responsibility for preparing the consolidated and separate financial statements lies with the Financial Reporting Office of the Parent Company.

The basis for the preparation of consolidated financial statements are the International Financial Reporting Standards (IFRS), based on the financial statements of Grupa LOTOS S.A. and of the entities controlled by Grupa LOTOS S.A.

The Parent and LOTOS Petrobaltic S.A., LOTOS Exploration and Production Norge AS, LOTOS Asfalt Sp. z o.o., LOTOS Oil S.A., LOTOS Paliwa Sp. z o.o., LOTOS Kolej Sp. z o.o., LOTOS Tank Sp. z o.o., and LOTOS Serwis Sp. z o.o. maintain their accounts in accordance with the accounting policies prescribed by the IFRS. The other Group companies maintain their accounting books in accordance with the accounting standards defined in the Polish Accountancy Act of September 29th 1994 and the accounting policies and standards applicable at their foreign locations. Consolidated financial statements include adjustments which are absent from the accounting books of the Group's entities applying accounting standards other than IFRS, and which have been introduced to ensure consistency of the entities' financial information with the IFRS.

In order to ensure accounting uniformity, the accounting policies effective at the Company were implemented across the LOTOS Group companies for application in preparing their consolidation packages.